

Superannuation Efficiency and Performance Unit
Retirement, Advice and Investment Division
The Treasury
Langton Crescent
Parkes, ACT 2600

Via Email: YFYS@treasury.gov.au

19 April 2024

Dear Treasury,

Consultation – Annual Superannuation Performance Test – Design Options

The Financial Advice Association of Australia¹ (FAAA) welcomes the opportunity to provide feedback to Treasury on the annual superannuation performance test – design options consultation paper.

The FAAA is a professional association that represents financial advisers. We approach this issue from a different perspective. We are not and have not been involved in the application of the test at a super fund level or in the calculation of results. We are however aware of some of the issues with the testing regime and have received a lot of feedback from our members, particularly as a result of the extension of the testing regime to Trustee Directed Products in 2023. We are therefore limited in our capacity to respond to this consultation paper, however we have nonetheless set out some high level views below.

In principle, the FAAA supports a performance testing regime and an increased focus on performance. We expect our members to carefully consider performance and to actively give thought to moving clients where performance is poor. We are also conscious that this needs to be done carefully as there may be reasons for clients to remain in underperforming products, such as tax reasons, the cost to move and proximity to retirement.

Views on the Current Design

The first point that we would like to make is that the test has been effective. This is highlighted by Chart 1 on page 6 in the consultation paper, which reveals that only one of 14 MySuper funds who have failed the test, have been able to survive. This is a very strong message and highlights that

¹ The Financial Advice Association of Australia (FAAA) is the largest association representing the financial advice profession in Australia, with over 10,000 members. It was formed in 2023 following the merger of the two leading financial planning/advice bodies in Australia – the Financial Planning Association (FPA) and the Association of Financial Advisers (AFA). With this merger, a united professional association that advocates for the interests of financial advisers and their clients across the country was created.

there are deep consequences in failing the test. It is unclear to us, whether any of the 12 products who exited, or the one who is in the process of exiting the market, were worthy of retaining. We are equally concerned about the future and whether experiencing a failure could reliably become a terminal factor. This is important as it may have a significant, and not always positive impact on how super funds operate and have negative consequences for impacted members.

We are conscious that super funds who have strong investment performance and low fees will have much greater comfort and confidence to pursue a range of investments. On the other hand, super funds who have had previous years of poor performance, and are close to the border, are likely to be much more risk averse and careful in what they do. This might have a negative impact upon their future performance. They may take less risks and transition to an index hugging model. It is right to question whether this is the right outcome for the members of these funds/options.

Amongst our members, some of the key feedback so far from the performance testing regime have been the following points:

- Typically Choice fund members have much higher account balances, and thus operating the testing on the basis of a \$50,000 account balance may not fairly reflect their actual performance.
- Choice members will naturally have a higher number of investment options in their superannuation investment portfolio. There have been concerns as to whether this has been fairly addressed.
- Whilst longer term performance testing results for some funds/options, consistent with the 8 – 10 year timeframe that has been tested so far, may have been poor, the fund or options more recent performance might have been strong. From an adviser's perspective, recent performance is very important, and poor performance that is over five years ago, yet still captured in the testing regime, is less relevant. Advisers are unlikely to recommend a client move away from a fund with strong three year performance, because the 8 – 10 year performance is poor. The longer term performance timeframe does tend to penalise funds for the long term, making it very difficult to recover.
- The performance measure takes no account of service standards and product functionality. Inevitably higher service standards and more complex products will cost more. This testing regime does not call out funds who have low service standards.

Views on Alternative Designs

Our other feedback on the consultation paper and the design options is as follows:

- We note the point made under administration fees in two places, where some stakeholders prefer a longer lookback period. We disagree with this. Performance testing has had a real impact on administration fees, which is very positive for consumers. If fees have been

brought down as a result, then this should be recognised. The thing that matters is what the fees will be next year, not what they were five, eight or ten years ago.

- We favour a multi-metric approach and particularly one that includes a hierarchical design. Whilst making it a multi-layered model will add complexity, this will also help to address situations like those that we have raised above, where long term performance may be below average, however recent performance is strong.
- We have reservations about extending the performance testing to retirement phase products. This is particularly the case with annuity type products that cannot be readily compared and are significantly impacted by interest rates at the time of commencement. Equally as the paper recognises, they cannot be changed easily without serious consequences. The establishment of some form of comparator tool is certainly worthy of further consideration. There are other important differences with account based pensions. We would suggest that more thought might need to go into this before further extending the performance testing to retirement phase products.
- We strongly agree that it is both unnecessary and inappropriate to extend the testing regime to other products such as SMSFs, direct assets and defined benefit funds.
- As stated above, we recognise the significant consequences of the performance testing regime. We believe that there is room for change, through some form of hierarchical model that provides secondary testing situations without introducing any level of arbitrary decision making on the part of APRA.
- In terms of barriers to consolidation we accept the argument that the Government can do more from a tax perspective to allow the consolidation of legacy investment options. This would reflect the existing options available to merge funds. We would strongly encourage this action to help address the large number of legacy investment options.

Conclusion

The FAAA welcomes the opportunity to provide feedback on this consultation paper. We appreciate the importance of this consultation and the performance testing regime. At a high level, we are supportive of sensible change to the testing regime, although we believe that it is important to avoiding adding excessive complexity and cost. Please contact me on 0417 280 270 if you have any questions.

Yours sincerely,



Phil Anderson

General Manager Policy, Advocacy & Standards
Financial Advice Association of Australia