Law Council
OF AUSTRALIA

ASIC Consultation Paper 203: Age pension estimates in superannuation forecasts: Update to RG 229

Australian Securities and Investments Commission

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Executive Summary

The Law Council supports the refinement of *Regulatory Guide 229*.[1]

The Law Council broadly supports the proposed provision for trustees to include the age pension in benefit projections, on an optional basis.

The Law Council is not making a submission on all of the questions posed in *Consultation Paper 203*.[2] The comments focus on technical issues rather than policy matters.

In summary, our comments are:

- The requirement for age pension estimates to include an assumption that the member has a partner requires clarification in relation to the assumed income and assets of that partner. Alternatively the requirement could be that the estimate assumes the member is single.
- A projection that includes the age pension should be required to include an explanation of the assumptions used in identifying the pension amount.
- Projections should be able to use a default retirement age if the Fund does not have the member's date of birth.
- The circumstances in which ASIC will adopt a 'no action' position, where the trustee adopts the methodology provided in RG 229 and the Class Order, require clarification.
- The calculation of administrative fees for the purposes of projections should be expressed to exclude *ad hoc* fees of an incidental nature.
- The refinements proposed in the Consultation Paper may not necessarily result in more trustees providing retirement projections to their members.
- The Law Council suggests that ASIC consider additional refinements. Some examples are:
  - allowing more realistic assumptions about contribution rates; and
  - allowing trustees to incorporate by reference the prescribed text in relation to warnings and assumptions.

[1] Australian Securities and Investment Commission, *Regulatory Guide 229: Superannuation Forecasts* (2011) <www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/rg229-published-7-December-2011.pdf/$file/rg229-published-7-December-2011.pdf>.

[2] Australian Securities and Investment Commission, *Age pension estimates in superannuation forecasts: Update to RG 229 (*2013) <www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/cp203-published-20-March-2013.pdf/$file/cp203-published-20-March-2013.pdf>

Purpose

1. This submission supports the refinement of *Regulatory Guide 229*.[3] The Law Council agrees that refinements of ASIC's policy may assist in addressing barriers to trustees providing retirement projections to their members.

2. This submission has been prepared for the Law Council of Australia by the Superannuation Committee (the Committee) of the Law Council's Legal Practice Section. The Committee's objectives are to ensure that the law relating to superannuation in Australia is sound, equitable and demonstrably clear. The Committee drafts submissions and provides comments on the legal aspects of virtually all proposed legislation, circulars, policy papers and other regulatory instruments which affect superannuation funds.

Proposal A1 (Summary of refinements)

> **ASIC Proposal:** We propose to make refinements to our policy to address certain issues that may have limited adoption by super funds of retirement estimates for their members.
>
> **A1Q2**: Do you agree that refinements of our policy are necessary to address barriers to super funds relying on our relief to provide retirement estimates for their members? If not why not?

3. The Committee agrees that refinements of ASIC's policy may assist in addressing barriers to trustees providing retirement projections to their members. However the Law Council suggests that the prohibition against including the age pension in retirement forecasts is not necessarily the reason why more trustees have not chosen to include forecasts with their periodic statements.

4. Anecdotally, the Committee understands that some trustees will still be unlikely to issue retirement forecasts, even if the proposed changes are implemented, or will still refrain from including the age pension in their forecasts. There is a general aversion to issuing forecasts which pertain to complex matters, based on overly simplified assumptions where there is a real risk of the assumptions not holding true for individual members. Some trustees are more comfortable simply promoting their online calculators and access to financial advisers, without providing simplistic and imperfect forecasts of benefits.

Assumptions about contributions

5. The Committee suggests that trustees may view the required assumption that contributions in the preceding year will continue to be made in each future year until retirement as too simplistic and too likely to be incorrect in individual cases. This is a disincentive to providing projections. The factors that are most easily identified as giving rise to unrealistic projections include:

- Superannuation guarantee contributions will gradually increase from 9% to 12% over the next few years. Therefore projections based on contributions being made at the current superannuation guarantee rate until retirement may be substantially

[3] Ibid.

lower than if the expected increases in the rate of superannuation guarantee contributions are factored in.

- An assumption that one-off contributions in a particular year will continue to be made in subsequent years is likely to significantly overstate the projection, especially in obvious cases where members have relied on the 'bring forward' rules to make a non-concessional contribution of $450,000 in a single year.
- Projections on the basis of contributions in excess of the concessional contributions cap are also likely to be unrealistic, particularly in light of the Government's recent announcement that members will be permitted to withdraw any contributions in excess of the concessional contributions cap.

6. The Committee suggests that ASIC consider additional refinements that allow trustees to make more realistic assumptions about future contribution rates. (Also, see our comments on 'today's dollars' in paragraphs 9–11.)

Assumptions about rate of return

7. The Committee suggests that trustees may view the required assumption of a 3% rate of return post inflation as unrealistic, and potentially misleading, for members invested in options that have a target or expected rate of return which is materially different from 3%.

8. The Committee understands that ASIC may have a preference for a uniform assumption about investment earnings, and for that reason may not wish to revisit that assumption. The Committee suggests however that trustees may believe the target rate of return for the member's investment option(s) would provide a more useful projection, and the requirement for a uniform assumption about investment earnings may be a disincentive to providing projections.

'Today's dollars'

9. The prescribed disclosures include a statement that the estimates are in 'today's dollars', and RG 229.60 states that:

> Using the investment earnings rate specified in [CO 11/1227] will result in a retirement estimate being expressed in today's dollars. Therefore, there is no need to separately consider the effect of inflation on the retirement estimate.

10. The Committee queries whether an estimate that solely relies on an assumed earning rate is adequate to support the statement that estimates are in 'today's dollars'. The prescribed formula does not provide for wage indexation, and as a result the contribution projections are not in 'today's dollars' – there is effectively an assumption that the real rate of contributions decreases over time.

11. The Committee suggests that ASIC consider asking the Australian Government Actuary to review the formula, with a view to recommending additional refinements that allow for assumed increases in contributions in line with a suitable benchmark such as an assumed rate of inflation or an assumed rate of increase in Average Weekly Ordinary Time Earnings.

Incorporation by reference of prescribed warnings and explanations

12. For those trustees that are comfortable with issuing projections based on simplified assumptions, the length of the prescribed text setting out warnings and explaining

the assumptions is potentially an impediment to sending projections with benefit statements. This text could add up to one-and-a-half pages to the length of a benefit statement, and for large funds that issue benefit statements more than once a year, this could amount to printing hundreds of thousands of additional pages per annum. This could be an impediment for some funds, whether from a marketing and member engagement perspective (i.e. out of an aversion to adding to the length of member communications) and/or from an additional cost perspective.

13. The Committee suggests that ASIC consider an alternative approach in relation to disclosure of the prescribed text. For example, ASIC could publish the prescribed text on the ASIC web-site and allow trustees to incorporate those details by reference. Alternatively, trustees could be permitted to publish the prescribed text on their own web-sites.

Proposal B1 (Inclusion of the age pension in a retirement estimate)

> **ASIC Proposal:** We propose to amend RG 229 and issue a class order to amend [CO11/1227] to allow a super fund trustee (if they wish) to include an estimate of the age pension in a member's superannuation forecast.
>
> **B1Q1**: Do you agree with our proposal to allow trustees to include the age pension in a retirement estimate?
>
> **B1Q2** Should it instead be mandatory for a trustee to include the age pension in a retirement estimate?

14. The Committee agrees that super trustees should be able to include an age pension estimate in a retirement projection that relies on ASIC's relief.

15. The Committee submits that including the age pension should not be mandatory.

16. For the reasons mentioned in paragraph 4, if the inclusion of the age pension were to be mandatory trustees that would otherwise be open to issuing retirement projections may not do so, simply to avoid having to make a comment on their members' potential eligibility for the age pension.

Proposal B2 (Inclusion of the age pension in a retirement estimate)

> **ASIC Proposal:** We propose to require that, if the super fund includes an estimate of the age pension, the pension estimate must use the following assumptions:
>
> (a) the member qualifies for the age pension under s 43 of Social Security Act 1991;
>
> (b) the member owns their own home, and has no other assets or income affecting the amount of the age pension other than a single superannuation fund retirement benefit lump sum, which is applied on the date of the estimate to purchase an account-based pension that provides the member with income in that year equal to the annual income stream amount; and

(c) the member has a partner and the partner has the same income and assets as the member.

B2Q1: Do the proposed assumptions reflect realistic circumstances for a substantial part of the Australian population? What additional or alternative assumptions should be prescribed?

17. The Committee submits that the application of assumption (c), that the member has a partner and the partner has 'the same income and assets as the member', is unclear.

18. The Committee expects the intention is simply that projections which include the age pension must adopt an assumption that the age pension estimate is at half the rate for a couple entitled to a full pension. If so, the Committee suggests assumption (c) would be better expressed as follows:

    (c) the member has a partner who jointly owns the home with the member, also qualifies for the age pension under s 43 of the *Social Security Act 1991* and has no other assets or income (including superannuation) that would affect the amount of the age pension.

19. Assumption (c) could also be interpreted as requiring an assumption that the member's partner has a superannuation fund benefit of the same amount, payable at the same time and also taken as an account based pension. The Committee suggests that this would be an unrealistic assumption, and would unnecessarily complicate the projection.

20. Alternatively, the Committee suggests that ASIC consider replacing assumption (c) with an assumption that the member is single. We note the rationale for the assumption is that around two-thirds of Australians are living in a couple relationship at age pension eligibility age. However the Committee notes that assuming the pension is at the single person rate would simplify the projection and also simplify the explanation of the assumptions.

21. The amended Class Order does not include any reference to an explanation of the assumptions for the pension amount. The Committee submits that where the age pension is included in the estimate, for a member to understand the estimate there must be an explanation of the basis for the assumed pension amount. We think it unlikely that a member will realise how the assumed pension amount is derived unless an explanation of the assumptions is specified.

22. To address this, the Committee suggests that the 'Standard Information' set out in paragraph 12(b) also be modified when age pension amounts are included, to include a bullet point explaining the pension assumptions. This is in addition to the prescribed wording in Proposal B3. (If our suggestion in paragraph 13 were adopted, this explanation would be included in the prescribed text published on the ASIC web-site or the fund's web-site.)

Proposal B3

ASIC Proposal: We propose to require that, if the super fund includes an estimate of the age pension, it must also include the following prescribed consumer warning in close proximity to the age pension estimate:

You may not be eligible for some or all of this age pension amount if you (or your partner) have income or assets in addition to this super fund.

Pension rates and eligibility rules may change between now and when you retire.

B3Q1: Does the proposed prescribed wording provide sufficient warning to super fund members about their eligibility for the age pension and caution in relying on the figures given?

23. The Committee supports the proposed prescribed wording.

Proposal B4

ASIC Proposal: We propose to issue a class order to amend [CO 11/1227] to specify that the retirement estimate must be calculated based on the retirement at the age the super fund member will become eligible for the age pension.

B4Q1: Do you agree with our proposal? If not, what age do you think should be assumed for retirement?

B4Q2: Are there any practical difficulties for super funds in implementing our proposal?

24. In order to calculate the age at which a particular member will become eligible for the age pension, the Fund will need each member's date of birth. The Committee understands that superannuation funds often do not have records of the date of birth for all members.

25. The Committee suggests that the amended Class Order recognise that a retirement age of 65 can be used if the Fund's records do not include the member's date of birth.

Proposal B6

ASIC Proposal: We propose to clarify in RG 229 our original intent that we will not take action if a super fund trustee follows the prescribed assumptions and methodology set out in this guide. We do not consider that it is necessary for a trustee to make specific inquiries to determine whether a member's individual circumstances match the prescribed assumptions.

B6Q1: Do you agree with our proposed approach? If not why not?

B6Q2: Does our proposed approach appropriately address industry concerns about potentially misleading or deceptive estimates?

26. The Committee agrees with ASIC's proposed approach, but we have some comments on the proposed amendments to RG 229.

27. The proposed amendment to RG 229.14 replaces:

> It is up to a trustee to determine whether a retirement estimate is misleading, or is likely to mislead.'

with:

> However, we will not take action if a trustee follows the prescribed assumptions and methodology set out in this guide.

28. However no amendment is made to RG 229.16, which states that:

> We consider that a retirement estimate calculated in the manner specified, and using the assumptions specified, in [CO 11/1227] is more likely to be misleading if it is prepared for a member:
>
> (a) of an eligible rollover fund;
>
> (b) of a defined benefit fund;
>
> (c) with an account with a small balance;
>
> (d) with an account in de-accumulation, rather than accumulation phase; and
>
> (e) who is aged 65 years and over.

29. Amended RG 229.14 gives the impression the trustee can rely on the prescribed assumptions and methodology in all circumstances, but RG 229.16 appears inconsistent with this.

30. If ASIC intends that the 'no action' position will only apply in limited circumstances, this should be clearly specified in the Guide. For example, RG 229.16 should specify that ASIC's 'no action' position does not apply in the circumstances listed (and in respect of paragraph (d) should specify what is a 'small balance' for this purpose).

31. If ASIC intends that the 'no action' position will apply in all circumstances where the trustee uses the methodology in the Class Order, this should be reflected in RG 229.16.

32. RG229.22 and 229.23 include statements to the effect that if a trustee does not provide personal advice in giving a retirement estimate it is likely to be providing factual information and does not need to rely on the relief. It would be helpful if the Guide included some guidance on which aspects of the methodology provided for in the relief are considered to constitute personal advice.

33. In particular, it would be helpful if the Guide explains whether ASIC believes that including any or all of the factors prescribed in the relief – such as actual administration fees, actual insurance premiums, actual prior year contributions, actual retirement age – results in the projection being personal advice in the absence of the relief? For example, if a projection uses a standard retirement age of 65 and administration fees and insurance premiums that are expressed to reflect the fund's average per member, would ASIC take the view that the relief is not required? Guidance on this issue would assist trustees in assessing whether they can give projections in circumstances where the Guide suggests that using the methodology in the Class Order is more likely to be misleading.

Proposal B7

ASIC Proposal: We propose to issue a class order to amend:

(a) [CO 11/1227] to clarify that any amount of administration fees and costs effectively paid or borne by the super fund member in the previous year (either directly or indirectly) should be included in the calculation of a retirement estimate; and

(b) the reference in [CO 11/1227] to 'management of the assets of the entity' to clarify that the definition of administration fees only excludes costs related to the management of investment of the super fund's assets.

B6Q1: Do you agree with our proposal in relation to administration fees? If not why not?

34. The Committee supports modifying the calculation of administration fees so that the projections are not affected by the particular fee structure the Fund has adopted. Accordingly, the Committee supports in principle the inclusion of administration fees that are deducted from Fund assets in addition to administration fees that are deducted from member accounts.

35. The Committee suggests however that the applicable definitions in the Class Order could be improved.

36. The definition of 'administration fees' would include a range of *ad hoc* fees that happen to be incurred in a particular year, such as fees for family law requests, partial withdrawals and investment switches. As the administration fees for the purposes of the projection are assumed to be incurred going forward, these types of fees should be excluded.

37. The fees that should be excluded can easily be identified by referring to the fees and costs that are excluded from management costs under paragraph 102(2) in Schedule 10 to the Corporations Regulations. The Committee suggests that the definition of administration fees include an additional paragraph excluding these amounts.

38. The Committee also suggests the following technical changes to the proposed terms of the amended Class Order:

The definition of Factor 'F' in paragraph 10:

> F = the total in dollars of the administration fees (if any) deducted directly from the member's account with the fund during the year ending on the date of the estimate plus the total in dollars of indirect administration fees (if any) that are attributable to the member's account for the year.

The definition of indirect administration fees in paragraph 14:

> ***indirect administration fees*** means any administration fees that are not deducted directly from a member's account. The amount of indirect administration fees attributable to a member's account is calculated by

multiplying the member’s current balance (as defined in paragraph 10) by the ratio of the fund’s indirect administration fees to the fund’s total average net assets.

Attachment A: Profile of the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Large Law Firm Group, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Independent Bar
- The Large Law Firm Group (LLFG)
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of approximately 60,000 lawyers across Australia.

The Law Council is governed by a board of 17 Directors – one from each of the Constituent Bodies and six elected Executives. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive, led by the President who serves a 12 month term. The Council's six Executive are nominated and elected by the board of Directors. Members of the 2013 Executive are:

- Mr Joe Catanzariti, President
- Mr Michael Colbran QC, President-Elect
- Mr Duncan McConnel, Treasurer
- Ms Fiona McLeod SC, Executive Member
- Mr Justin Dowd, Executive Member
- Ms Leanne Topfer, Executive Member

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