



# ACTU CONGRESS 2006

## Superannuation and retirement incomes: A position paper

### INTRODUCTION

The focus of ACTU Congress 2006 is on industrial relations policy and the union movement's response to the Government's Work Choices legislation. Comprehensive policy on superannuation and retirement incomes was adopted at the 2003 Congress. The purpose of this position paper is to:

- (1) Reiterate the 2003 policy;
- (2) Set out key developments since 2003; and
- (3) Identify principles and priorities for the next three years.

<p>Congress 2003 Superannuation and retirement incomes policy - A summary of main points</p>
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### Adequacy

Congress noted that there is clear evidence that 9% SG is insufficient to fund an adequate retirement for workers on average incomes and proposed addressing this by:

- Increasing contributions to a goal of 15% through one or more of bargaining, legislative change or changes to the taxation system, with an objective of 10% contributions achieved through bargaining;
- Reducing the contribution tax;
- Restructuring all superannuation taxes to provide greater equity;
- Extending the SG entitlement to all workers, irrespective of age or minimum earnings;
- Requiring full disclosure of fees and charges and a ban on entry and exit fees and commissions charged on SG contributions; and
- Requiring equal treatment of same sex couples.



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## Superannuation funds

Congress confirmed its longstanding support for industry superannuation funds as offering the best combination of good returns, low fees and effective service to workers and their families.

Congress called for measures to enable industry funds to operate in a fair environment including:

- Providing for awards and collective agreements to collectively satisfy choice of fund legislation; and
- Controlling commission-driven financial planners.

## Investment

Congress called for a debate focussing on encouraging superannuation fund investment in economic and social infrastructure, and companies offering real growth over the long term.

Congress noted the evidence that company performance is assisted by good governance practices and by adherence to appropriate labour, social and environmental standards.

## Corporate governance

In a separate policy, Congress called for corporate governance standards to be lifted through a number of measures, including:

- Improving the composition of company boards through better disclosure, requirements to appoint a majority of independent directors and increased penalties and personal liability for breach of duties;
- Encouraging greater institutional shareholder participation, requiring voting of shares and enabling submission of resolutions to general meetings;
- Improving executive remuneration disclosure, restricting exercise of options and requiring expensing of all remuneration in accounts;
- Improving protection for whistleblowers;
- Accelerating audit reform to avoid conflicts of interest;



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- Removing corporate tax deductibility for salaries over \$1 million; and
- Legislating for directors' duties to be extended to include other stakeholders, including employees.

## Developments since Congress 2003

Since 2003 there has been substantial legislative and other change affecting retirement incomes policy, including:

- The introduction of choice of fund legislation;
- Very substantial growth in the superannuation industry, and industry funds in particular;
- The removal of the 15% tax on lump sums and income streams paid on retirement, and the removal of reasonable benefit limits (RBL's);
- The growth of the co-contribution;
- The introduction of Work Choices and the removal of superannuation from all awards (to be finalised by 2008);
- The encouragement of growth of independent contracting and consequent increased non-compliance with superannuation law;
- Introduction of licensing and consequent rationalisation of funds;
- Growing interest in infrastructure investment; and
- Greater corporate understanding of the requirements of good corporate governance.

## Future principles and priorities

The ACTU sees six principles as underlying a fair, efficient and equitable superannuation system:

- The collective provision of superannuation to maximise economies of scale through the nomination of not-for-profit funds as the default fund for all workplaces;
- The prohibition of upfront and trail commissions on SG contributions;



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- Ensuring adequacy in retirement incomes;
- A strong representative trustee system;
- A long-term perspective on investment; and
- Greater adherence to high standards of corporate governance.

## The collective provision of superannuation

### Background

The combined effect of choice of fund and Work Choices is a growing individualisation of superannuation.

By 2008, the link between awards and superannuation will have been abolished, although collective agreements will continue to be capable of specifying the fund into which employees' contributions are paid.

However, with annual labour turnover at around 20%, many industry fund members will change employment at least once within the next five years. The key issue is for employees to have access to industry superannuation at the workplace, whether by individual choice or as the default.

### The choice of fund agenda

The cost advantage held by industry superannuation funds is a result of the collective distribution of superannuation through industrial instruments. This system is efficient and cost-effective and has served working Australians well for nearly twenty years.

The purpose of the Government's choice of fund legislation is to shift the provision of superannuation from collective (wholesale) arrangements to individual (retail) arrangements more suited to the financial planning, banking and insurance industries. This "retailisation" of the superannuation sector adds cost to individual members and reduces their retirement income.

If elected in 2007, a Labor Government will scrap much of the industrial relations legislation. The ACTU believes the choice of fund legislation also needs significant amendment. The ACTU believes the "retailisation" of superannuation provision is inimical to the public policy objective of mandatory superannuation; that is, to maximise the retirement income of retirees. Reform of the choice of fund legislation would address its inherent weaknesses:



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- The risk of mis-selling by financial planners seeking to earn a commission, ignoring inherent conflicts of interest and the effect of high fees on retirement income;
- Inadequate fee disclosure;
- The ability of employers to choose the default fund; and
- Low levels of financial literacy and lack of interest and knowledge about superannuation among employees.

## Collective choice of fund

The ACTU believes that employees should be able to continue to access low cost superannuation funds at their workplace through:

- A requirement that a not-for-profit funds be the default fund in all workplaces; and
- A greater effort by unions to ensure the inclusion of industry funds (or appropriate not-for-profit funds such as public sector or corporate funds) either exclusively or as a choice in all workplace agreements and employment contracts.

The ACTU believes industry funds are the most appropriate vehicles for this purpose on the basis that they:

- Are not for profit;
- Do not pay commissions to financial planners;
- Have lower than average fees; and
- Have an equal number of employer and employee/union directors on the trustee boards.

## Superior investment returns

In addition to the lower average fees and not-for-profit structure, industry funds have delivered their members investment out-performance when compared to retail funds run by banks and insurance companies and sold by financial planners.



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For the five years to 30 June 2006, the top ten performing balanced funds (where over 80% of workers choose to invest their superannuation) were industry funds.<sup>1</sup> These were MTAA, AMIST, CARE Super, ARF and STA (now AustralianSuper), HESTA, HostPLUS, REST, EquipSuper and Westscheme, representing well in excess of three million working Australians.

## The prohibition of commissions on SG contributions

### The effect of commissions

The ACTU has strongly advocated the prohibition of the payment of commissions on SG contributions on the basis that commissions for advice on choice of fund are not warranted for mandatory contributions. Financial planners remunerated by commission have a direct conflict of interest which affects the quality of advice provided to their clients. Further, commissions have an erosive effect on a member's final account balance, as demonstrated by the "net benefit" analysis (see below).

In a recent Government submission, the consumer organisation CHOICE included research undertaken by Rainmaker which estimated that in the nine months to March 2006, over \$850 million was paid to financial planners in upfront and trail commissions on SG contributions.<sup>2</sup>

The recent ASIC Shadow Shopping survey revealed widespread systemic problems in the financial planning industry arising from the commission system. The findings included that advice was six times more likely to be non-compliant where the adviser had a conflict of interest, and that in many cases the advice would leave the consumer worse off.

### The effect of fees

In recent years, two research houses, SuperRatings and Rainmaker have undertaken research commissioned by Industry Funds Services. Both organisations have consistently found there is a significant "net benefit" for industry fund members when compared to their counterparts in retail funds.

The "net benefit" research demonstrates the dollar amount of growth in a member's account, where growth is measured as contributions plus investment earnings less all fees and taxes.

<sup>1</sup> Source: SuperRatings 50 Balanced Index, 30 June 2006

<sup>2</sup> CHOICE submission to the Joint Parliamentary Inquiry into the Structure and Operation of the Superannuation Industry, September 2006



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SuperRatings found that over the five years to 31 March 2006, an average industry fund member received \$12.30 for every \$1.00 taken out in fees, while master trusts over the same period, had on average, given back just \$4.50 for each \$1.00 in fees.

SuperRatings concluded that over a 40 year working life, Australians could be more than 28% better off in an industry fund, based on existing fee structures. This is equivalent to having \$143,906 more (in today's dollars) or \$386,397 more (in future dollars) in their superannuation account at retirement.

Rainmaker Information found the industry funds' out performance was due to lower fees and investment performance, but also because they tend to use higher levels of growth assets in their diversified default options than master trusts.

According to Rainmaker Information, the overall performance advantage in the workplace market meant that industry fund members saw their super account balances outgrow master trusts by \$486 over the past year, \$2,283 over the past 3 years and \$5,411 over the past 5 years.

Of greatest concern is the personal superannuation market, where members don't have access to employer discounts. Industry super funds delivered \$99 more dollars over one year, \$2,165 more over three years and \$15,173 more over five years.

## Financial literacy and member education

The ACTU does not accept that disclosure of fees and commissions is sufficient protection against commission selling. Many consumers are likely to struggle to make sense of complex fee arrangements, let alone fully comprehending the compounding effect of high fees and trail commissions.

Research has consistently shown that employees are not sufficiently engaged with their superannuation. A recent survey commissioned by the Investment and Financial Services Association (IFSA) and undertaken by Newspoll found that:

- 43% of respondents did not know that their employer was legally required to make contributions to their superannuation; and
- 36% did not know the correct amount. <sup>3</sup>

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<sup>3</sup> 'Newspoll confirms need for improved financial literacy', IFSA Media Release, 27 July 2006



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This research adds to a considerable body of evidence that reveals the poor levels of financial literacy among the Australian population.<sup>4</sup> The push by many financial planning groups to repeal elements of the Financial Services Reform Act (FSRA) and reduce the requirements to disclose fees and commissions is strongly opposed by the ACTU.

The ACTU supports the work being undertaken by Members Equity Bank to develop a workplace based financial literacy program, in particular the inclusion in agreements of a clause to provide for limited paid leave for employees to undertake the training.

## Adequacy of retirement incomes

The debate surrounding choice of fund, the recent federal government superannuation changes and the industrial priorities of unions has reduced the emphasis on the adequacy of retirement incomes. There remains, however, ongoing consensus that increased contributions are required for all sections of the workforce, particularly workers who have not had access to superannuation for the whole of their working lives, particularly women, casuals and part-time workers.

The introduction of the co-contribution, and more recently the proposals to remove the tax on lump sums and removal of RBLs, have comprised the primary response of the Government to the issue of adequacy.

The Government's current policy is clearly skewed to benefiting high income baby-boomers rather than providing for ordinary Australians, including those on low incomes, approaching retirement. In particular, the removal of the "exit" tax only assists those with higher account balances (over \$130,000 upon retirement).

The Government has repeatedly missed the opportunity to divert surpluses to savings through superannuation, preferring to offer tax cuts. While this may be electorally popular, it is short sighted and, as the recent rise in interest rates proves, can be counter-productive.

More direct policy options need to be adopted to provide for the desirable target of 60-65% of gross retirement income for most workers and higher for those on low incomes.

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<sup>4</sup> See for example, the ANZ Survey of Adult Financial Literacy, November 2005, [www.anz.com.au](http://www.anz.com.au)



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To achieve this, the ACTU retains the view that employees, employers and Government will need to make a contribution to providing a sustainable adequate retirement incomes strategy. The following options need to be explored:

- The extension of SG entitlement to all employees irrespective of age or minimum earnings and the requirement for 9% super contributions to be made for all “independent contractors”;
- Removal of the contributions tax for all employees earning up to \$70,000;
- The introduction of a requirement for all employees commencing employment after 1 July 2007, unless they specifically choose to opt out, to make a contribution of 1% which would be matched by their employer increasing contributions to 10%; and
- Continued efforts by unions to increase contribution rates through bargaining.

## A strong representative system

With the establishment of the licensing system and the “fit and proper” test for trustees, there had been some concern that the system of representative trustees would be destabilised.

To date this has not been the case, with APRA confirming that it is the corporate trustee as a whole, including staff and external consultants, not each individual director, who must meet education and technical requirements.

However, the ACTU remains concerned that the Government is intent on undermining the legitimacy of representative trustees, particularly in the case of union nominees.

The current parliamentary inquiry into the structure and operation of the superannuation industry, with its focus on industry fund trustees, highlights that concern.

Representative trustees have proven, in practice, to have delivered honest, diligent and competent leadership resulting in successful administration of the funds under their stewardship. The record of representative trustees could be usefully compared with the self-selection system of many public company boards, exposed during the recent imbroglio over Telstra board appointments, which has lain behind corporate scandals such as HIH.



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The ACTU remains completely committed to continuation of the representative trustee system, including the ability of trade union organisations to nominate employee representative directors to trustee boards.

The ACTU also strongly supports increased efforts to ensure that superannuation fund directors receive sufficient training and have adequate time to carry out their duties to the highest standard. Responsibility for resourcing of directors must be shared between funds and their nominating organisations, particularly in respect of ensuring that other duties do not impede their capacity to carry out their superannuation responsibilities.

## Superannuation investment

Superannuation funds are continuing to grow at a significant rate: industry funds' assets increased by 29% in the 12 months to June 2006 compared to 20% for all funds. While increased retirement savings is unreservedly positive, there are growing challenges in finding appropriate investments for these funds to ensure reasonable returns and avoid the creation of asset bubbles.

Consideration needs to be given as to whether growing investment in private equity and hedge funds contributes to encouraging long-term value-driven corporate growth.

Underinvestment in economic and social infrastructure remains one of the key impediments to Australia's successful long-term economic performance.

Superannuation funds are committed to investing in Australian infrastructure and have done so, generally consequent on privatisation of existing assets or the development of new ones through public-private partnerships (PPPs).

The key issue for Australian infrastructure is not shortage of public or private finance, but the lack of a process for identifying potential infrastructure projects, giving these a priority rating and developing effective mechanisms for project execution.

The ACTU has called on governments to finance infrastructure development through a combination of current expenditure, the creation of infrastructure bonds and appropriately structured private finance models, such as PPPs, subject to transparent cost-benefit analysis.

The ACTU welcomes the increasing involvement of Industry Funds Management (now part of Members Equity Bank) in raising funds for infrastructure investment, including in social sectors. Over time, it is



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expected that the active participation of industry funds will assist in bringing down the level of fees charged by those involved in putting deals together and in ensuring greater transparency and public benefit.

## Corporate governance

The need for high standards of corporate governance continue to be underscored by scandal - since 2003, for example, the events involving James Hardie and AWB.

The ACTU continues to press for the key elements of good corporate governance, including director independence, transparent and accountable remuneration policies and better enforcement of directors' responsibilities.

These issues are critical in ensuring that company directors and management have incentives directed towards longer term growth and performance, rather than short-term share price increases.

Good corporate governance should also include corporate social responsibility, with an emphasis on environmental and social sustainability.

Superannuation funds can strengthen good corporate governance by:

- Insisting that their shares are voted at company meetings in accordance with a fund policy and that details of the voting are made available to fund members;
- Requiring fund managers to engage actively with investee companies to ensure that they meet the highest standards of governance and social responsibility;
- Positively and publicly supporting companies which exhibit good governance;
- Requiring fund managers to consider governance issues in their assessment of companies' risk profiles and management;
- Being prepared to initiate and/or support resolutions at general meetings addressing issues related to corporate governance;
- Lobbying for legislative change to enable resolutions on a greater range of subjects to be put at general meetings; and
- As a last resort, being prepared to support legal action, where possible, to enforce companies' governance obligations.