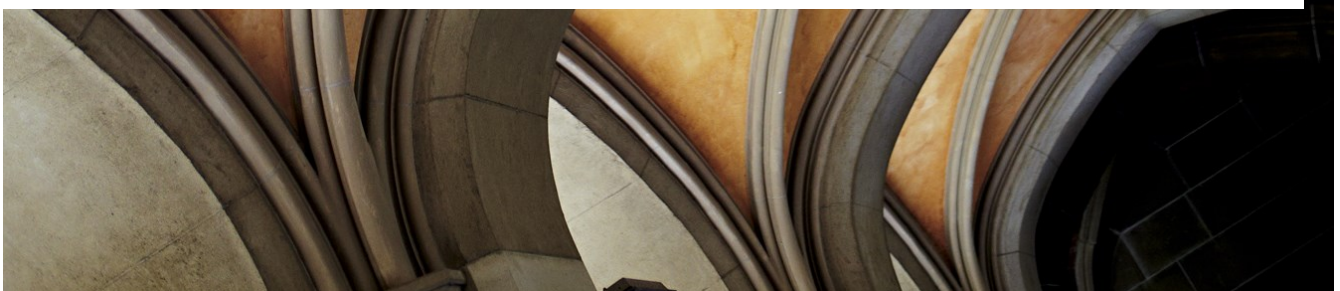




Extending superannuation choice to enterprise agreements & workplace determinations

Submission by UniSuper

20 January 2016



About UniSuper

UniSuper¹ is the superannuation fund dedicated to people working in Australia's higher education and research sector. With approximately 400,000 members and \$49 billion in assets under management as at 30 June 2015, UniSuper is one of Australia's largest superannuation funds and has one of the very few open defined benefit schemes.

UniSuper, established in 1983 as a defined benefit (DB) scheme, was modelled broadly on then contemporary DB schemes in the Australian public sector and overseas peer funds. The benefit design from its outset offered full portability of benefits across all participating employers and coverage of all permanent employees in the sector, including general, academic and professional staff.

The multi-employer nature of UniSuper led to some important distinguishing features from its commencement, in particular:

- a fixed contribution rate of 14% of salary p.a. for employers and 7% of salary p.a. for contributing members;
- by covering the whole university sector, members can maintain defined benefit membership when transferring between employers within the sector;
- members can defer their benefits (so maintain membership) through periods when not employed in the university sector;
- a formula-based benefit related to member's salary, tenure and employment experience.

Over its foundation years, UniSuper succeeded in obtaining broad coverage of permanent employees in the Australian university sector and "folded in" a large number of legacy DB superannuation and pension schemes from individual institutions on a successor fund and/or optional transfer basis.

Today, 37 universities and roughly 200 related bodies are participating employers. The Defined Benefit Division (DBD) remains funded by a 14% employer contribution and 7% default member contribution (which members can reduce with appropriate benefit adjustments). Many members also receive an additional 3% "award" contribution paid into an associated accumulation account, making a total employer contribution of 17%.

We also manage two defined contribution, accumulation-style accounts. Accumulation 1, is for members who are not entitled to DBD membership and Accumulation 2 is based on the same 14%/17% employer contributions paid by participating employers for those who opt out of DBD membership.

¹ This submission has been prepared by UniSuper Management Pty Ltd (ABN 91 006 961 799), which acts as the administrator of the Trustee, UniSuper Limited (ABN 54 006 027 121). This submission is endorsed by the Trustee.

UniSuper is proud to be recognised as one of Australia's most awarded super funds. Over the years we have received a string of awards and high ratings from independent ratings and research agencies. Most recently we were named 'Super Fund of the Year' and 'Best Fund: Investments, 2015' by Chant West and received 5 apples ratings for our Accumulation 1 and Accumulation 2 products. Our Accumulation products were also awarded a 10-year Platinum Performance rating by SuperRatings. These awards reflect our ongoing commitment to providing members with the highest quality products and services, along with our competitive investment returns.

UniSuper Management Pty Ltd would welcome the opportunity to discuss the submission further and to provide additional information in respect of the comments made in this submission. Should you have further queries, please contact Sean Hughes on (03) 8831 6513 or sean.hughes@unisuper.com.au.

Executive summary

UniSuper welcomes this opportunity to provide comments on the exposure draft legislation to expand the coverage of the Choice of Fund regime to include more Australian workers.

UniSuper makes three main suggestions to improve the draft legislation and policy process.

1. Exemption from Choice when an employee is a DB member

The policy principle stated in the Explanatory Memorandum (EM) for the original Choice Bill should be restated in the EM for the proposed Bill to clarify that the exemption applies to both existing and future newly eligible DB members: *“This bill prescribes a class of employee who cannot choose a fund into which their superannuation contributions are paid. This will ensure that employers are not required to fund additional superannuation benefits for employees.”*

Also the proposed heading for section 20(3A) should also be changed to clarify the basis for the exemption and we suggest the following wording: *Employer is obliged to contribute to defined scheme and member’s benefit not affected.*

2. The proposed transition timeline to Choice – multi-employer arrangements

An alternative transition plan for multi-employer schemes should be developed to ensure that employees and employers in the relevant sector continue to have consistent superannuation arrangements. This could be done by a uniform transition date linked to the finalising of all new agreements across the relevant sector after 1 July 2016. This would ensure that all employees and all employers know exactly when Choice will take effect.

3. Joint consultation

Choice and default superannuation are related issues, and have the potential to affect the viability of DB schemes and other collectively-pooled arrangements. These issues need to be considered together and there should be further consultation on how to deal with the issue of those who receive employer support in excess of the Superannuation Guarantee (SG) minimum level.

Extending choice to employees covered by enterprise agreements

UniSuper is the default superannuation fund in numerous enterprise agreements across the higher education sector² and Choice of Fund — as envisaged in the current law — does not widely apply. Arguably, the current exemption of DB schemes from Choice of Fund legislation is because the choices of individuals could have a detrimental effect on a group of people.

We believe that, under the draft legislation, all of our members in accumulation options (two-thirds of our active members and \$31 billion in assets under management) would have choice, while members in the DB scheme (one-third of our active members and \$18 billion in assets) would not. There are very strong reasons why DB schemes were exempted from the Choice of Fund rules over ten years ago and these reasons remain relevant.

Our DB scheme has been in operation for over 30 years. Under current legislative arrangements, we have been able to establish a successful, well-funded, innovative and *open* DB scheme. In contrast to accumulation products (which are directly exposed to investment volatility) DB schemes aim to deliver a more predictable formula-based benefit. The DB structure offers members far greater certainty in planning for their retirement, achieving this through pooling members' assets to smooth investment experience, ultimately providing a stable (formula-based) benefit that is not directly exposed to the volatility of investment markets. Over three decades, and many economic cycles, no UniSuper DB member has had any reduction to their accrued defined benefit. Even after the financial crisis in the last decade, defined benefits accrued by members have not been impacted. Many Australians have not been so fortunate.

We note that future directions for product development across the superannuation industry suggest a return to many of the principles of collective-risk sharing. The proposal for a Comprehensive Income Product for Retirement is likely to involve some risk-pooling to address longevity risk. While an extension of Choice — along with any changes to default arrangements — would not necessarily preclude collective-risk pooling, it is easier and more efficient to pool risks between a well-understood and readily definable class or group of members in a particular sector, particularly where a trustee has a long-established relationship to a sector and has deep and extensive data on employment patterns, resignation and retirement ages, along with reliable mortality and life expectancy data.

² UniSuper is named in the two higher education awards and in a third award on post-secondary education. Despite having default status in awards and EBAs, many new employees can still “opt out” of being a member of UniSuper. We have established rules, supported by enterprise agreements, that allow new employees the choice to join another fund and not UniSuper, particularly where an employee is already a member of another similar defined benefit scheme, such as the CSS or PSS, or is a visiting academic from overseas. These rules were also established to prevent members having duplicate superannuation accounts.

Exemption for *existing* DB members – should continue

Even though the exemption from Choice for *existing* DB members is being maintained, it is important to highlight that if it were removed, there would be significant consequences. In UniSuper's case, if existing DB members were able to redirect their SG contributions to another fund, there would need to be significant rule changes and deed amendments because our current defined benefit design requires a level of employer funding (typically 14%) well above the current SG rate.

Even if members were able to redirect their SG contributions and UniSuper received the difference (i.e. 4.5%) there would still be potential problems.

Firstly, the defined benefit accruing under a 4.5% contribution would be very small and made even smaller after taking into account provision for contributions tax, insurance and administration. Secondly, there could be considerable difficulties in determining and implementing an appropriate Minimum Requisite Benefit for DB members where employer contributions are made across different schemes, particularly to a scheme not connected to UniSuper.

In all likelihood, were existing DB members able to redirect their SG contributions to another scheme, we would have to introduce new rules that would exit them from the DBD, crystallising their defined benefit, and then direct their residual contributions to an accumulation account.

Any such move could have consequences for those who remained in the scheme, having the potential to put pressure on the funding viability of the scheme because there could be:

- Material numbers of exits of DB members who choose to leave the DB and crystallise their defined benefits, which could lead to significant funding and asset valuation and liquidity issues
- A fundamental shift in the remaining membership profile, creating future funding concerns
- Increased anti-selection risk, exacerbated by a lower proportion of members remaining within the scheme

Such unintended consequences could lead to perverse effects and moral hazards which might, quite possibly, prompt an actuarial review of funding and potentially require appropriate actions to ensure the ongoing viability of the scheme. Whilst it is an issue for the Fund (UniSuper) itself, this could negatively impact many individual members as possible reductions in benefits could be required because the Fund has neither a government guarantee nor recourse to additional employer contributions.

We believe the very strong reasons why DB schemes are exempted from the Choice of Fund rules will continue to remain relevant into the future.

Exemption for *future newly eligible* DB members – should be clarified and confirmed

The draft legislation is not clear on how (or if) the exemption from Choice would apply to *future newly eligible* DB members (i.e. future new employees to the sector who are eligible to join UniSuper's DBD), or existing accumulation members who may become newly eligible to join the DBD.

We believe there needs to be an exemption for both *existing* and *future newly eligible* DB members for a number of reasons, including the following:

1. If a lower proportion or fundamentally different profile of members were to join the scheme, over time, this could lead to the unintended perverse effects and moral hazards foreshadowed above.
2. There could be situations where employers are exposed to potentially being obliged to contribute to a defined benefit scheme under the scheme's trust deed or participation agreements as well as being obliged to make SG payments to a scheme of the employee's choice under the Choice legislation.
3. There could also be inconsistencies across employers, particularly where their pay cycles are different (e.g. fortnightly or monthly). For example, under the existing law, a new employee could become a DB member within 14 days of commencing a new job because the obligation to make superannuation contributions to the DB scheme could fall due before a Standard Choice Form has been issued (generally within 28 days of commencing employment and with the employer having up to two months to act upon the choice request).
4. Where employers are obliged to provide superannuation support in excess of the minimum SG requirement, typical of DB schemes, members who are able to exercise Choice would end up having two accounts: one, the default for their current employer and the other in a separate fund of their choice. The Financial System Inquiry's Recommendation on Choice was seeking to avoid that very issue of proliferation of accounts.

As the policy intent is to avoid each of these outcomes, we believe the DB exemption needs to be clarified through a clearer exemption from Choice for both *existing* and *future newly eligible* DB members.

Specific comments on the draft legislation

The draft legislation includes an exemption from Choice when an employee is a DB member. Proposed section 20(3A) of the Superannuation Guarantee (Administration) Act 1992, the “member benefit unaffected” test, mirrors closely other exemptions previously codified in sections 32F(3) and 32NA(9) of that Act. These exemptions are hard to follow and, as we understand it, the policy basis for the DB exemption is to ensure that employers are not required to make contributions both to a DB scheme as well as SG contributions to another scheme of an employee’s choice.

This policy principle was stated in the Explanatory Memorandum (EM) for the original Choice Bill: “This bill prescribes a class of employee who cannot choose a fund into which their superannuation contributions are paid. This will ensure that employers are not required to fund additional superannuation benefits for employees.”³ We think this principle should be restated in the EM for the proposed Bill to clarify that the exemption applies to both *existing* and *future newly eligible* DB members,

The proposed heading for section 20(3A) could also be changed to clarify the basis for the exemption and we suggest the following wording: *Employer is obliged to contribute to defined scheme and member’s benefit not affected.*

The proposed transition timeline to Choice – for multi-employer arrangements

One of the strengths of the existing system, and one of the key drivers behind the creation of UniSuper, is that employees can – and should be able to – move between participating employers, typically the 37 universities, seamlessly and continue to receive the same superannuation arrangements. Under the proposals, this may no longer be the case.

Transitional issues could create complications and confusion for employers, employees / members and super funds. Currently, roughly 50 EBAs cover the higher education sector and they expire at different dates. These agreements, under the *Fair Work Act 2009*, will continue to operate after their nominal expiry date until they are replaced or terminated by application to the Fair Work Commission.

EBAs in the higher education sector typically have a duration of three or four years. Some EBAs take significant time to negotiate. Consequently, Choice within the higher education sector could come into effect in a staggered manner over a number of years. Whilst it would notionally start on 1 July 2016, the full effects would not likely be seen for number of years, potentially as late as 2019 or 2020. While this might be manageable for a single employer with one (or possibly two) EBAs, it becomes more complex with multiple employers.

We are concerned that the transition period will lead to uncertainty and will likely create complexity for employers and confusion for employees as university staff move between different institutions over a four year period (2016-2020) with their superannuation

³ Revised Explanatory Memorandum, Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill 2003, p. 10 para 1.23

transitioning in and out of the new Choice environment. Indeed, some part time staff work across three or more universities simultaneously. Such a scenario implies significant administrative complexity.

We are also concerned about the potential for labour market consequences during the transition period. For example, some employees might choose (or not choose) a job with another employer because of differing superannuation arrangements across the sector. This would be a disadvantageous outcome for our members because UniSuper was specifically established as a multi-employer scheme designed to ensure that members could move seamlessly from one employer to another and receive consistent superannuation arrangements within the sector, albeit with different employers.

We suggest consideration of an alternative transition plan for multi-employer schemes to ensure that employees and employers in the relevant sector continue to have consistent superannuation arrangements. This could be done by a uniform transition date linked to the finalising of all new agreements across the relevant sector after 1 July 2016. This would ensure that all employees and all employers know exactly when Choice will take effect. Under the current proposals, this is completely unknown.

Choice and Default are closely related issues – joint consultation is appropriate

Choice and Default superannuation are closely related issues, particularly for DB schemes because both matters have the potential to affect the on-going viability of collectively-pooled arrangements. The issues raised in this submission are specific to the DB sector and include matters that we believe should be addressed in a separate and targeted consultation. The consultation we seek would complement the work on default superannuation currently underway at the Productivity Commission because it would address the issue of default arrangements for those employees who receive employer support in excess of the SG rate. UniSuper would be happy to participate in such consultation.

Conclusion

The problem, as we see it, is that the existing focus of the Choice legislation on directing SG contributions does not readily translate to the superannuation entitlements of employees in the higher education sector. This creates challenges and uncertainty for employers, employees and UniSuper's Trustee over the destination of the remaining superannuation contribution i.e. in addition to the SG contribution. Choice, as it stands, fails to address the circumstances of schemes such as UniSuper which has a DB option to which employers and employees can contribute at a rate in excess of 250% of the SG level in a bid to build better retirement outcomes, reducing the likelihood of reliance upon government support as members age.

The proposed legislation could also undermine the ways in which UniSuper's current and proposed products support emerging policy around, for example, provision of a Comprehensive Income Product for Retirement.

The framing of Choice in these circumstances may lead to unintended consequences, perverse outcomes and the potential for moral hazard. Consequently, it could create

uncertainty, confusion and the possible duplication of obligations, with significant administrative complexity.

Given that the draft Choice provisions do not adequately deal with DB schemes such as UniSuper, we argue that, along with the existing exemption for current DB members, there should be an explicit exemption for schemes such as ours in which new members (and, shortly, existing members) have the choice of moving into a DB arrangement.