Default super funds under review

A Productivity Commission inquiry is developing alternative models that could be implemented by government if a new model for allocating default fund members to products is desirable.

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The Productivity Commission's comprehensive review of the superannuation industry[1] continues with its release of a draft report into possible changes to how default fund members are allocated to products.[2]

The Productivity Commission was requested by the federal government to undertake a three-stage review of the 'competitiveness and efficiency' of the superannuation industry in response to recommendations contained in the Financial System Inquiry, which released its final report (known as the Murray Report), in December 2014.[3]

Stage one of the review focussed on developing criteria to assess the efficiency and competitiveness of the superannuation system and was completed in November 2016, while the current stage two is focused on possible changes to how default super fund members are allocated to products. (To clarify, employers are required to nominate a 'default' super fund into which they pay an employee's superannuation guarantee contributions if the employee has not chosen their own super fund.)

Stages one and two will then inform stage three—a review of the efficiency and competitiveness of the overall superannuation system—which the Productivity Commission will undertake following the full implementation of the MySuper reforms sometime after 1 July 2017.

Default super funds review

The Federal government issued Terms of Reference for the Productivity Commission to "develop a workable model, or models, that could be implemented by Government if a new model for allocating default fund members to products is desirable. The developed model(s) should enhance efficiency in the superannuation system in order to improve retirement incomes, including through optimising long-term net returns to members."

"In developing alternative models, the Commission is to consider international practice; costs and benefits of different mechanisms; the robustness of the process; efficiency and innovation over the long run; the effect on system stability and market concentration; who should run the process; and the extent to which the process promotes the interests of consumers."

Why default super fund arrangements exist

While it would be better for individuals to choose their own super fund which best suits their financial needs, the reality is that many Australians don't or simply forget to do so.

One consequence of this approach is that when an individual changes jobs, they may find themselves signed up to a new default super fund and, if they change roles again, signed up to yet another fund and so on.

As a result, individuals may end up paying multiple sets of administrative fees with different funds, which erodes their overall superannuation balance.

With this in mind, it is commendable that a key focus of the Productivity Commission's draft *Superannuation: Alternative Default Models* report, which was released in March this year, is an attempt to reduce the number of default super

funds that an individual may join or be joined by their new employer.

Four default super fund models are proposed: assisted employee choice (model 1); assisted employer choice with employee protections (model 2); a multi-criteria tender (model 3); and a fee based auction system (model 4).

Employee choice model

Employees would be required to choose a super fund themselves but would be assisted by a non-mandatory shortlist of selected super funds deemed, by a government body, to be 'good'.

Assisted employer choice with employee protections model

Employers would choose a default product for employees who do not exercise choice. In doing so, employers would have to select a list of super funds decided by a government body.

Multi-criteria tender model

Super funds would compete for the right to a share of the default pool by making proposals against a number of different assessment criteria.

Fee-based auction model

Super funds would compete for default fund status by out bidding each other on the cost of member fees.

Which model to choose?

According to the Melbourne Mercer Global Pension Index, Australia currently rates third out of 27 countries, behind only Denmark and the Netherlands in terms of the world's best retirement income systems.

This high ranking does not mean that there is not scope for improvement in superannuation in this country, including default super fund processes. However, it is clear that any changes must be supported by rigorous research and modelling to ensure any such changes result in positive outcomes for Australians.

One way to increase the likelihood of positive outcomes is to ensure that any amendments to default fund arrangements result in only high quality and consistently strongly performing super funds being selected as default fund options by employees or employers.

The Productivity Commission is scheduled to hand its final *Superannuation: Alternative Default Models* report to the federal government in August.

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1 See *http://www.pc.gov.au/inquiries/current/superannuation*

2 See *http://www.pc.gov.au/inquiries/current/superannuation/alternative-default-models#report*

3 See *http://fsi.gov.au/*