9 November 2022

General Manager
Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority

To whom it may concern,

Submission: Strategic Planning and Member Outcomes

We refer to the above consultation on APRA's review of SPS 515 Strategic Planning and Member Outcomes. We are pleased to see APRA's increased focus on member outcomes as opposed to the 'documentation-focus' of the implementation period for SPS 515. Importantly, the 'outcome' for a superannuation member is what income they receive to replace their salary in retirement.

We have focussed our comments on how to define outcomes in a way that can be regularly assessed against the outcomes that trustees intend to achieve for members. In particular, we focus on your Questions 2 and 12 – 14.

Quantitative measures are critical to design and deliver outcomes that align with the objectives of the Retirement Income Covenant. Having robust metrics will also assist with conducting business performance reviews. It is essential that a core part of a superannuation fund's framework is the end goal of providing retirement incomes, otherwise measurements of performance, fees etc will not be that relevant or will utilise the wrong metrics.

Optimum Pensions have partnered with Generation Life and Hannover Re and launched a new retirement income stream type that superannuation funds can use or white label. The product allows member investment choice whilst giving the benefit of longevity protection that ensures retirees cannot outlive their pension.

We would be pleased to discuss our comments further.

Your sincerely,

[redacted]
General Manager

Defining and measuring outcomes for members in retirement

In the accumulation phase the emphasis is on the member's balance. But 'balance at retirement' is not the member's 'retirement outcome' unless they take a lump sum withdrawal. Most Australians then spend two to three decades in retirement.

The purpose of superannuation has been agreed almost unanimously as being "To provide income in retirement to substitute or supplement the Age Pension".

The retirement products and strategies offered by an RSE licensee have a major impact on members' outcomes as framed by the Retirement Income Covenant. **The Australian Government Actuary estimated that retirement product decisions can improve a member's retirement income outcome by up to 30%[1].**

The methodologies used by each RSE licensee to develop and manage these products and services need to be dramatically different from those used in the accumulation phase.

- A bad member outcome in retirement would be if income runs out while they, or their spouse, are still alive. That outcome is a function of the fund's Retirement Income strategy rather than just relying on investment performance and fees.
- Another bad outcome would be to end up dying with a large remaining balance that should have been enjoyed earlier as income. Lump sum death benefits at older ages (e.g. for members in their 80s and 90s) represents a material 'leakage' from the superannuation fund - if the objective is to maximise retirement incomes and not generational wealth transfer.

Superannuation outcomes for members

During the accumulation phase, the main drivers of a member's balance are largely outside the control of the RSE licensee. These include the member's:

- Rate of salary over time and career pattern
- Length of time in this particular fund
- Voluntary contribution decisions
- Performance of the markets (equities, bonds, cash, property etc)
- Retirement age

[1] Financial System Inquiry Final Report page 26

In the retirement phase the RSE licensee has a much more material role to play. It is the RSE licensee's responsibility to select which retirement income product types to offer members and the RSE licensee is responsible for the efficient operation of these products.

The choice of retirement income product spreads the member's accumulated superannuation across their (and potentially their spouse's) remaining future lifespan. There are many different ways of doing this and the RSE licensee's decisions shape which members get what outcome

Annual outcomes assessment

Trustees need a separate strategic section within their business plans that relate to the outcomes of their retired cohorts.

The choice of retirement income product and strategy also has a material impact on the fund's projected funds under management (FUM), its projected demographic profile and its future income for a number of reasons:

- Having excellent solutions in the retirement phase is essential – given that superannuation is no longer compulsory when members retire
- Some retirement product types do not prevent a member's superannuation balance from running out while they are still alive (e.g. a 100% allocation to an account-based pension)
- Some product types 'leak' FUM in the form of lump sum death benefits to elderly members (e.g. in their 80s and 90s) that could have been used to provide higher income while the member was still alive

Because retirement products are long-term by nature, there is a time dimension and the exact outcomes for a member will not be known until the many years in the future. Assessing outcomes will require forward looking projections based on objective assumptions. They also need to take into account uncertainty.

Metrics for measuring member outcomes – in terms of retirement income

RSE licensees need to set up several separate, distinct techniques for defining and assessing the effectiveness of their efforts to manage outcomes for retired cohorts. We recognised that there are many ways to assess retirement income products. Listed below are some of the metrics that could be considered as appropriate:

- Metrics that assess actual observed benefits paid to retired members, including:
    - Starting income levels as a percentage of the member's balance
    - How many members are starting pensions at each age. For example, commencing prior to Age Pension Age, rather than at or after reaching age pension age.

- Income volatility observed. e.g. the number of times in a specified period that changes in members' income are negative or if incomes fall below the members starting income level (inflation linked)
  - Lump sum death benefits paid in retirement
  - The number of members whose balance ran out in a specified period

- Metrics to assess the pricing, charges and risk of products used (including longevity products):
  - The retirement income risk metric proposed by the Australian Government Actuary[2]
  - Explicit fees and charges
  - Implicit fees and charges e.g. using 'value for money' (present value) calculations done by actuaries. Metrics used in other countries (e.g. the UK's compulsory critical yield calculations)
  - Credit risk of external providers (such as longevity risk insurers)

- Demographic studies of how long the fund's retired members are living in practice against the assumed distribution of how many members are likely to live to each age and what tools are provided to assist members to obtain some degree of confidence about how long they may live (other than reliance on the Average Life Expectancy tables)

- Metrics to monitor retired member circumstances, behaviours and preferences:
  - Data (or surveys) on whether members have a dependant spouse, home, non-super incomes and savings, health status, desire to leave an inheritance and so on
  - Take up of each product type and product option
  - The level of take up of engagement programs (e.g. retirement seminars or planning appointments)
  - Surveys to assess retired members feelings of satisfaction, confidence, fear of running out, financial security etc

- Metrics to assess the experience of investment linked retirement products:
  - Returns of underlying investment options (including the relationship to CPI, given that it would be beneficial for retirees to maintain their income in real terms)
  - Fees and charges

Importantly, some of the above metrics require forward looking projections and some can be measured ex-post. Both are essential for retirement phase in Australia. We also refer to the Actuaries Institute paper "*A Framework To 'Maximise' Retirement Income*" published earlier this year [3].

Fund Data on payments from retirement products

In order to enhance the focus on measuring retirement incomes, APRA could require funds to provide data on payments from different retirement product types – for inclusion in APRA's Fund-level Superannuation Statistics report. Even simple data that shows lump sum payments and income paid from different pension product types in age bands would assist in considering how successful the fund is in achieving retirement income outcomes.

It could highlight how much was being paid out (i.e. is it just the minimum from an Account Based Pension, are members using products that quality for preferential means-testing, lump sums paid to members in their 80s and 90s). This would assist in understanding how retirement savings are being used.

At present there is considerable focus on contribution by age, which is important, but how these contributions are being used at retirement is becoming more important.

[2] https://treasury.gov.au/consultation/c2018-t347107

[3] https://actuaries.asn.au/Library/Opinion/2022/TheDialogue260422.pdf