State of Play: AE Experiences and Pro[illegible] in the UK and Ireland

Scoping Workshop

David Harris – Managing Director

TOR Financial Consulting

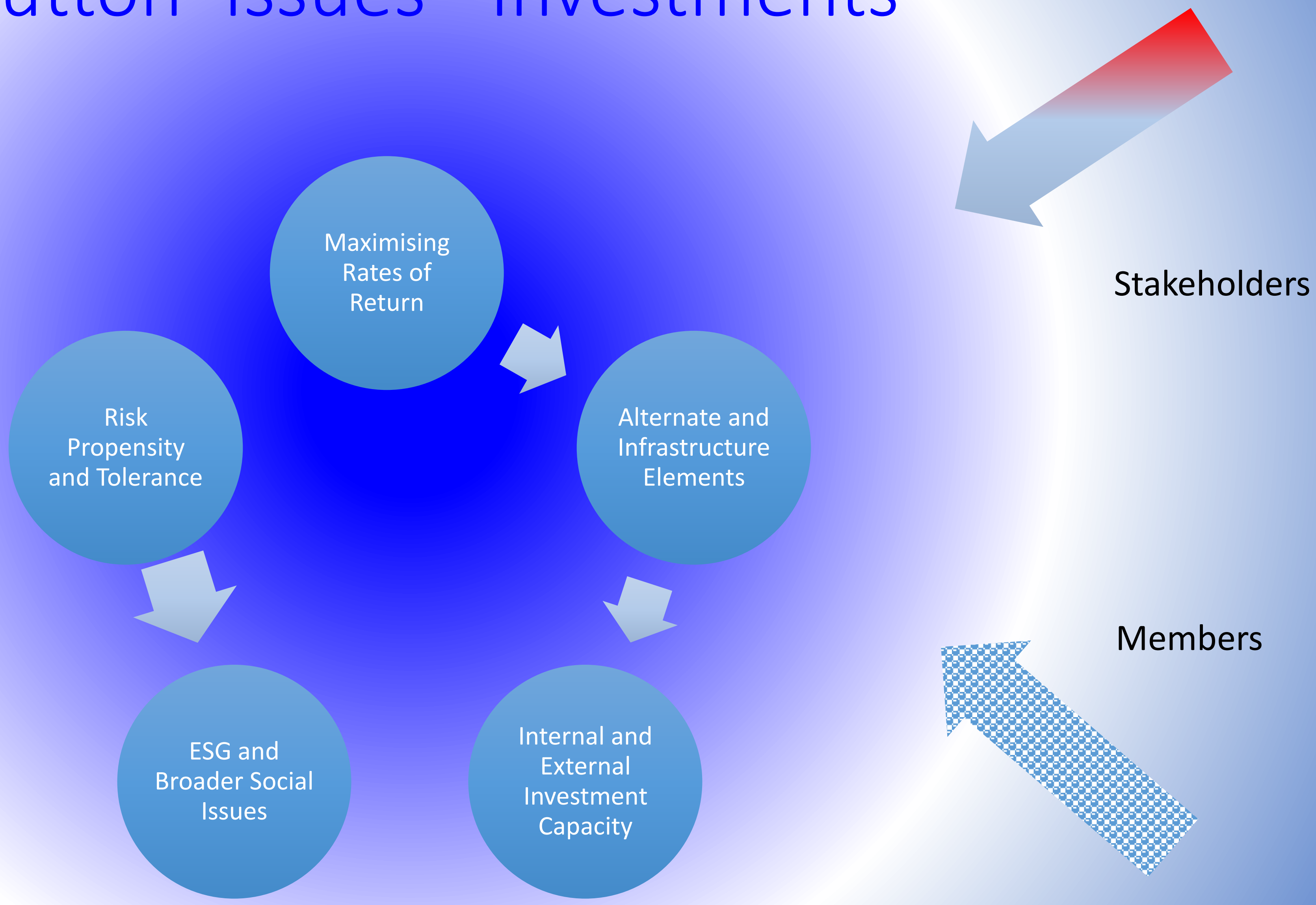
April 26, 2019

TOR Financial Consulting Limited

Global Drivers for Pension Reform

- 'People Worried More About Living Too Long than Dying Too Soon'
- Government Fiscal Crunch: Baby Boomer retirement and the demands on the first and second pillar pension solutions
  - Disruption and Economic and Social Cohesion
  - Hard Compulsion > Auto Enrolment > Tax Incentives
- Accelerated transition from DB to DC – PAYG Impact and Political Considerations and Support
  - Infrastructure held by US, Canadian and Australian pension funds
  - Australia and New Zealand – Sharp Decline
- Social Activism/Media Considerations – Member attitudes
- Political reactions to a low interest rate environment – long term impact
  - Infrastructure considerations
- Economic Impact – Brexit and Economic Slowdown in China
- Decline in paternalism – pensions seen as more transactional
  - Scale and Transactional/Operational Costs

Global 'Hot Button' Issues - Investments



UK – AE Backslapping But Really?

- Moved sharply to 5% employee contribution and 3% employer contribution – global and domestic uncertainty
- Minimal opt out rates but analysis on cessation of contributions are not clear. Coverage rates have surged pre and post AE.
- Price capping at 75 bps is promoting ‘vanilla solutions’ that generate profit margins. Smart default has not been widely accepted. Calls to lift price capping to encourage growth in UK infrastructure.
- NEST – State quango is due to have a loan balance of £1.29 billion providing DC schemes of last resort.
- Pension freedoms – corner stone of retirement income solutions – more government revenues and discretionary spending.
- Replacement rate – discussions around Collective Defined Contribution Schemes
- Dashboard Developments – appreciating your pots of retirement money.
- Number of providers is much smaller in number compared to New Zealand.

Ireland – AE and Its Strawman

- Brexit and the flattening of the Irish Economy + IORP II have slowed AE reforms
- Responses to the consultations – over 100 submissions have generated some political consternation
- The New Zealand KiwiSaver experience continues to provide the closest comparison with the likely Irish AE reforms
- Existing DC landscape + Newly created AE solutions.
- Price capping of 50 bps – economically sound to provide such solutions
- Creation of the Central Processing Authority (CPA) – arms length government agency that will select four providers – 5 year contractual period – suggested 10 years.
- Processing hub to be built allowing employee rather than employer choice.
- Suggestion EET tax approach with TTE – inconsistent – tax arbitrage.
- 2022-2028 – 6% from employer and employees
- Intergenerational fairness, wealth gap and housing access in the post global financial crisis
- Gender issues – not well developed or understood - wage levels, divorce timings and longevity risk
- Political risk – the first pillar will provide in perpetuity – really?
- Political cost of IT system designs - Delays and Cost Overruns
- 70/30 – What is the ideal replacement rate?
- Employee Choice vs Employer Choice

Questions and Thought Leadership for New Zealand

- Does the country need to rethink retirement income policy and housing access and ownership?
- Is there a need for New Zealand to embrace financial wellness approaches – to better understand consumer needs eg. Lifecents (USA)
- Is gender issues and intergenerational fairness ideal for the future of New Zealand – wealth gap?
- Need for indigenous providers to create infrastructure for future generations.
- Political risk for maintaining static first pillar pension solutions
- Is the level of fees and charges appropriate for returns generated?

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New Zealand/Australia
Some Systems Comparison Nick Sherry

	NZ	Australia
Start date	2007	1987
Contributions	3,4 or 8%	3% 1997, 3 to 9% 1992-02, 9.5%, 2013, 12% 2021-25
Size	$34b, 2016; $40b 2017; 15% GDP	A$2.65t 2018; 140% GDP
Contributions, mechanism	Central via one platform	Decentralised via fund
Governance	Corps Law, FMA license	Trustee (best interest member test), Corps Law, APRA/ASIC license both NFP and retail
Default fund	Individual selects, if no, default	Default then individual may opt out usually “advised”planner or accountant
Default investment option	Provider determined	Provider determined, My Super

Comparison continued…

Contributing/ No. of members accounts	1.57m, 2.7m	15.5m,28m
Early Access	Hardship and first home	Hardship, first home (voluntary conts. only)
Retirement	Lump sum at 65/ little developed	Lump sum at 60, semi developed-mainly drawdown, transition to retirement, or term annuity

Note: New Zealand a simple system. Australian system has many other features, contributions type, insurance, estate, transition to retirement, tax, etc. Very complex. Admin cost 20 to 40 bp.

New Zealand/Australia Providers

New Zealand

Provider no.	Default	Employer selected	Complying super funds
31	9	20,000	16

Australia

Number of Funds	2002	2012	2018
Corporate (WFP)	2484	119	22
Industry (NFP)	134	56	38
Public (NFB)	76	38	18
Retail	254	131	116
Self managed	.250 m	.500 m	.600 m

Funds with more than $20b; 2 corporate, 7 industry, 8 public sector, 6 retail. 86 MyS

Assets $b

	2012	2018
Corporate	58	54
Industry	292	630
Public	237	461
Retail	397	589
Self Managed	478	727

New Zealand/Australia
Returns and Fees

New Zealand -Best 10			
	Return%	Average	Fees%
Conservative	4.17 to 5.76	4.18	.81 to 1.48
Defensive	2.49 to 6.39	2.51	.74 to 1.19
Balanced	5.86 to 9.29	5.48	.81 to 2.10
Growth	6.78 to 12.59	6.42	.84 to 2
Aggressive	7.93 to 11.55	7.07	.77 to 2.11

Australia -Best 10	Return	Average	Fees %
Conservative	6 to 8.6	n/a	.5 to .52
Defensive	6.9 to 7.4	n/a	.4 to .52
Balanced (My Super) growth in NZ	9 to 11.2	n/a	.58 to .72
Aggressive	11.6 to 13.6	n/a	.67 to .77

All industry, public or corporate funds. All $10b plus in size. The majority of members in.

A 2% fee rather than 1% reduces final balance by 20% over 30 years.

Number of Lost Accounts $b

	2015	2016	2017
Number	6.2m	5.7m	6.3m
$b	$16.2	$14.8	$18

The Clean Up

33m multiple/lost accounts in 2010. Now 28m.

- Changes – ATO removal of lost or inactive accounts and SuperMatch – fund campaigns – Single Touch Payroll – Superstream and Tax File No. use buy funds.
- Auto consolidation of accounts less than $6000 from July 1, 2019 – 5m consolidated.
- $340m in duplicate administration fees removed.

Productivity Commission

Evidence

Structural flaws including - multiple accounts, underperforming funds/products, excessive fees.
Multiple accounts 28m for 13 m in the system - Retail, most poor performing; Industry, some poor performing (smaller under $10b funds); Self Managed poor performance under $1m assets (revised to $.5m).

Major recommendations only

- “Best in show” shortlist of 10 funds to **new members** to choose from or auto allocated for life
- Exiting underperforming funds
- Multiple accounts consolidation – increase over $6000
- Enquiry into Retirement Incomes – suspend increase in SG

No political policy announcement on from either major political party.

The Hayne Royal Commission

Royal Commission into misconduct in the Banking, Superannuation and Financial Services Industries

a salutary lesson in corporate governance

Calvert J Duffy & Associates
Governance Risk & Compliance Consultants
April 2019 ©

Hayne Royal Commission

In 2014, a Senate Committee recommended a Royal Commission into the Commonwealth Bank of Australia (CBA), following a multi-million-dollar financial planning scandal.

In 2017, more wrong doing was uncovered at the CBA's insurance arm and other misconduct by the other banks, namely ANZ, NAB & Westpac.

Add to that, the federal Opposition was pushing for a Royal Commission for 18 months - stating that it would make the sector stronger.

When even more pressure (cross benchers, media etc) was put on the Government the PM then relented.

Enter the Hayne Royal Commission 14 December 2017!

corporate governance

“GREED IS GOOD”

was there a culture of greed?

could it infiltrate NZ?

- conflicts of interest – Trustees & representatives

- KPIs – realistic?

corporate governance
changing the regulatory culture

- remuneration typologies

- punishment to fit the crime?
  what ‘crime’?... see “Downs Syndrome” matter from Insurer

- legislative remedy?

- consequences – political, economic, social and criminal

corporate governance
the future?

for New Zealand ….. where to from here

- trustees – obligations vs actions
  - does this mean that Trustee Duties in NZ will need to be tightened up in some way?

- trustees in Australia – did they just fail?
  - If so – how do you mitigate that possibility?

- trustees – is it 'profits at all costs' or something else?
  - perhaps we should look to Australia for an answer

corporate governance
the future

- what else is in store for NZ …. in terms of governance?

  especially given that the ANZ holds 25% of KiwiSaver
- are there going to be issues in NZ such as the *clash* between Industry funds and not-for-profits as is the case in Australia?

New Zealand conduct & culture review findings and future focus

Scott McMurray

RPRC Summit| 26 April 2019 | University of Auckland Business School

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Hayne Commission

"…the Final Report can be seen as a 'once in a lifetime' opportunity to drive future success for the Australian financial services sector though a renewed focus on the areas of trust and governance. The same is true for New Zealand."

MinterEllison

Hayne Commission themes

- Primary responsibility for misconduct lies with those who managed and controlled the entities
- Six norms should underpin conduct
- Connection between conduct and reward
- Asymmetry of power and information
- Conflicts associated with intermediation

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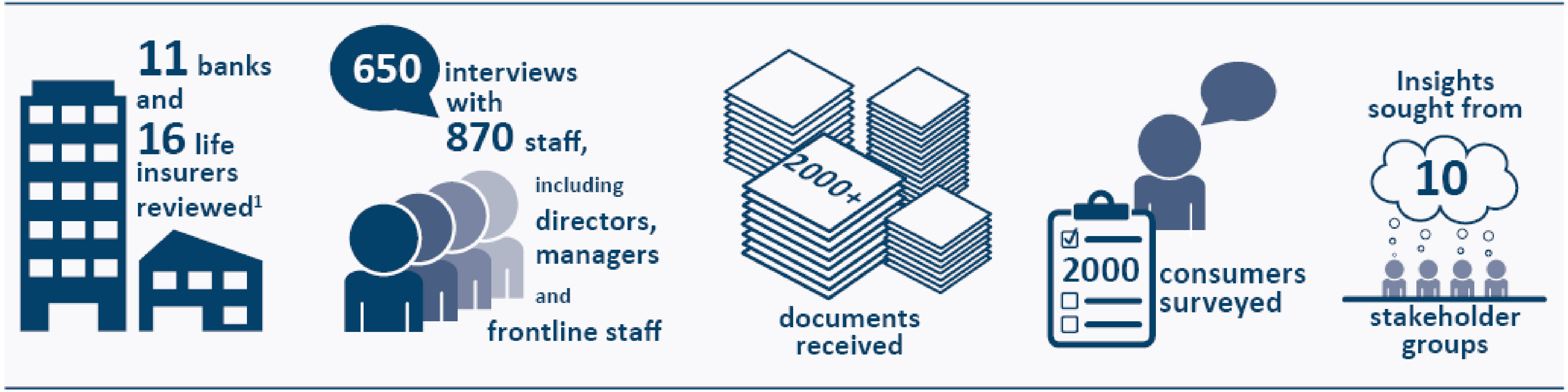
FMA/RBNZ conduct & culture reviews



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FMA/RBNZ conduct & culture reviews

Assessed the state of conduct maturity under four key areas:

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Conduct & culture review – bank findings

- Small number of instances of poor conduct – not widespread
- Weaknesses in management and governance of conduct risk
- Weaknesses in reporting of complaints and measuring customer outcomes
- Risk of poor customer outcomes heightened by sales based incentives
- Overall, insufficient board ownership and accountability

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Conduct & culture review – life insurer findings

- Several examples of poor conduct and some cases of potential misconduct – not widespread
- Extensive weakness in the governance, and systems and controls for managing conduct risk
- A lack of focus on conduct issues and good customer outcomes
- Remediation of conduct issues generally poor
- Lack of oversight of advisers and intermediaries

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Regulator expectations

- Boards to take ownership of conducts risks and culture
- Responses and actions plans
    - Invest in systems and controls
    - Identify and remediate conduct issues
- Review all incentive structures – internal and external

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Key recommendations and outcomes

- Transform firms approach to conduct risks and customer focused culture

- Rebalance focus between shareholder and customer interests

- Government to address regulatory gaps

Future focus

- Work on changes to the FMA's regulatory remit
- Conduct and culture recommendations apply to all financial service providers
- Strategic risk outlook and sector views
- KiwiSaver default providers review
- Investor engagement