

Fund Level Disclosure from the APRA Superannuation Statistics Collections

ASFA Submission

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Association of Superannuation Funds of Australia

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ASFA Submission to APRA Discussion Paper: Fund Level Disclosure from the APRA Superannuation Statistics Collections

Introduction

The Association of Superannuation Funds of Australia Ltd (ASFA) is pleased to provide its submission to the Discussion Paper: Fund level disclosure from the APRA superannuation statistics collections (hereafter called the Discussion Paper).

ASFA is the peak superannuation industry association representing all sectors of the Australian superannuation industry. We aim to ensure superannuation fund members are engaged with their superannuation and have an understanding of the options available to them. One of the most important pieces of information for fund members is accurate, comparable investment performance information at investment option level, so that they can fairly compare the options available to them.

Executive Summary

Current statistics are aimed at trustees

APRA propose to expand their publications to include data on individual fund investment performance. Specifically they propose to publish a reference publication which contains the information necessary to construct fund level returns. APRA are asking for feedback on whether they should also publish compilation tables of fund level performance (i.e. league tables).

ASFA agree with the project's aim of providing accurate performance information for all superannuation funds across the whole industry.

Whilst it is important for trustees to have accurate information on which to gauge their performance, this information is already available to trustees from a number of sources, and trustees already use this information when reviewing their performance.

New statistics are also aimed at fund members

We understand that APRA is responding to a request from Government to provide statistics which are disaggregated at individual fund level. APRA has stated that the new statistics are designed to assist fund members.

Whilst it is important for members to have investment performance information, such information is already available to members from at least four different research houses.

Current statistics are an aggregation and are not at fund level

We understand the imperative on the Regulator to produce these statistics in a short time frame and the resulting desire to produce the statistics from data APRA has already collected.

However, the proposed returns based on the data APRA currently collect will provide figures for the Registered Superannuation Entity (RSE) which are an aggregation of different superannuation (and perhaps retirement) products and divisions. This is not information that will be relevant to or useful for a superannuation fund member.

ASFA is concerned that members could in fact be misled by such investment performance statistics as they will not understand that it is an aggregate figure, and not a return that they can expect to earn in a particular product or indeed a particular investment option.

ASFA's position

ASFA formally express our concern regarding the ability of APRA to provide information which will be useful to superannuation fund members based on the information already held. The reason for this is that the structures and practices of the industry mean that the data already collected is not at the right level to relate to individual superannuation or retirement funds. As such the data would be misleading for fund members.

If APRA determines that such figures must be provided, ASFA recommends that they are provided for the key (or largest) investment options within each superannuation or retirement product or division within the RSE. We recognise that new data would have to be collected in order for this to be achieved.

We further recommend that any technical issues with APRA's methodology be addressed, and have made some detailed comments in that regard.

The Purpose of the Statistics

Current statistics are aimed at trustees

The current statistics are aggregated for different sectors of the superannuation industry (Industry, Corporate, Public Sector and Retail).

In the covering letter (30th September 2008) to "A RESPONSE TO Review of APRA's Investment Performance Statistics of the Australian Superannuation Industry" Deputy Chairman Jones stated that "APRA's main focus in the relevant areas of our superannuation publications is to provide information on the long term aggregate investment returns achieved by trustees, *not to generate recommendations for individual fund members* as to which fund and what investment option they should choose."

Whilst it is important for trustees to have accurate data to gauge their investment performance against, this information is already available to trustees from a number of sources, and trustees already use this information when reviewing their performance.

New statistics are also aimed at fund members

However, with the publication of the new returns, the stated purpose has changed somewhat.

In the press release (20th November 2008) that accompanied the Discussion Paper, Deputy Chairman Ross Jones stated that 'The information in this new annual publication is intended to....*assist fund members, trustees and the wider industry*'.

We understand that APRA is responding to a request from Government to provide statistics which are disaggregated at individual fund level. APRA has stated that the new statistics are designed to assist fund members.

Is the aim to assist fund members to make financial decisions about their superannuation such as which superannuation product or investment option to select? It is very likely that any investment performance statistics aimed at fund members will be used in this way. Whilst it is important for members to have investment performance information, such information is already available to members from at least four different research houses.

We believe that APRA should be producing information that:

- increases transparency;
- provides comparable information on a like-with-like basis;
- enhances the understanding of members;
- encourages members to take a long term view; and importantly
- enhances confidence in the superannuation industry.

Issues

Before answering the questions in the Discussion Paper, there are a number of issues that ASFA would like to discuss in terms of the proposed disclosures.

1. New returns will still be an aggregated return

Currently APRA publishes aggregated returns for different sectors of the superannuation industry (Industry, Corporate, Public Sector and Retail).

The Discussion Paper states APRA's intention to expand these publications to include data at an "individual fund or trustee level". This is in response to a request from the Minister for Superannuation & Corporate Law, Senator Nick Sherry, to publish performance at an individual fund level.

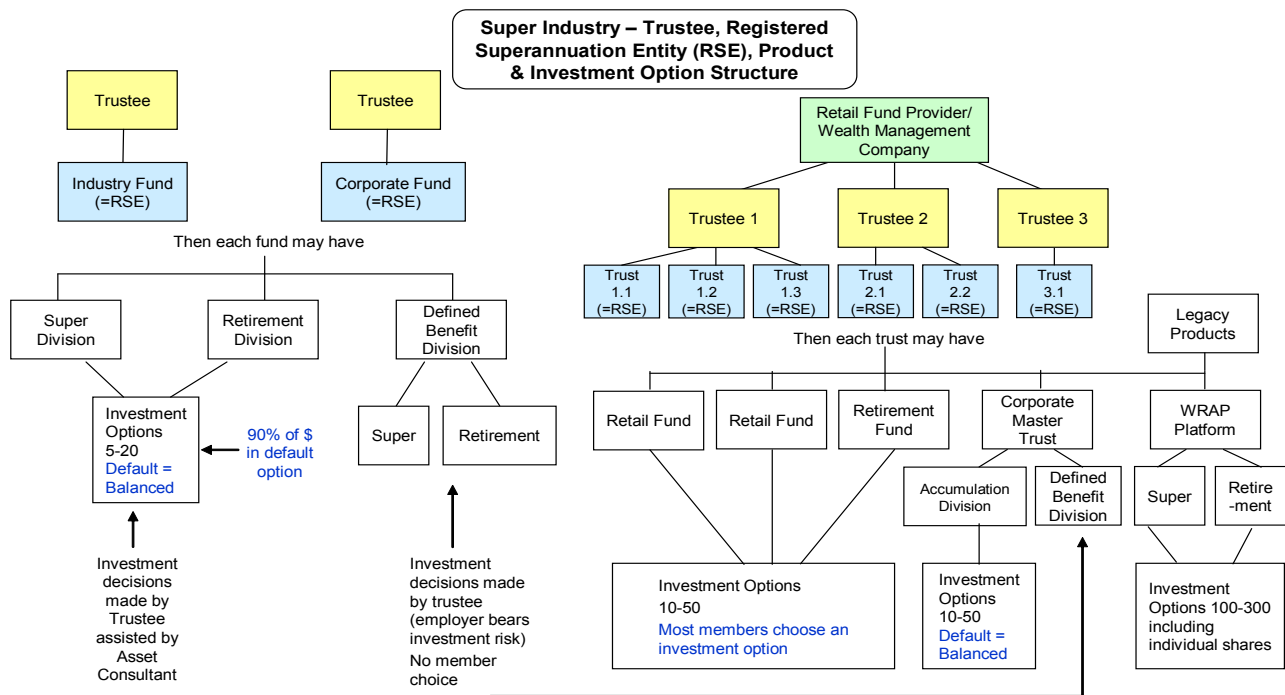
There are two issues here.

1.1 Returns will not be at "Fund Level"

Firstly the Discussion paper makes clear that the data that APRA will publish is based on APRA's current data collections. The data already being collected is for Registered Superannuation Entities (RSE's) i.e. for superannuation trusts. This data is collected for prudential purposes.

It's important to recognise that this does not achieve the aim of reporting at individual superannuation fund level for those providers (generally retail funds) where there are multiple superannuation funds within the one trust.

The following diagram of the superannuation industry illustrates this point. For three different sectors on which APRA reports (Industry, Corporate and Retail funds) the position of the Trustee is shown in the yellow box, and the RSE (or superannuation trust) is shown in the blue boxes.



The diagram shows that Industry and Corporate fund trustees generally only run one superannuation trust, which contains only one superannuation fund, however that fund will often include separate divisions (or products).

On the other hand, Retail fund trustees generally run multiple superannuation trusts (or RSE's), each of which can contain more than one superannuation product. For example data from three large bank's wealth management arms (in total with significant market share) indicate the following statistics:

- Bank 1 - 3 trustees, 8 RSE's and 51 superannuation products
- Bank 2 – 3 trustees, 12 RSE's and 30 superannuation products
- Bank 3 - 2 trustees, 4 RSE's and 12 open products plus legacy products.

Retail funds collectively account for more than 30% of the total superannuation funds under management, so this structure is common for a significant sector of the superannuation market.

The proposed APRA performance analysis will not be provided at an individual superannuation fund (i.e. product / division) level but at the RSE level. Whilst for some funds the trust and the product are the same thing, for others reporting at RSE level is merely an aggregate of many different superannuation and retirement products. This is true for most of the retail sector, but also for those industry and corporate funds that run separate divisions within their funds.

A number of funds across all three categories provide membership of one or both of the 'accumulation' fund or 'defined benefit' fund. Although many funds have ceased offering the latter for new members there is nevertheless significant membership for the foreseeable future in the defined benefit membership category of the fund. Aggregated reporting in relation to these funds is meaningless given the benefit promise basis of a large proportion of the aggregated funds.

As such the proposed publication will not achieve what has been requested by Senator Sherry i.e. publishing information at fund level.

1.2 Returns will only be useful to members at investment option level

The current data will provide a return figure across all investment options in a series of superannuation products within one superannuation trust. This is not a relevant figure for a particular member as no-one invests in the whole trust. Even where a trust contains only one fund (or product) there will be a number of investment options within the fund and it is unlikely that a member will invest in all of them.

When a member is considering superannuation returns, they are often looking to compare their current investment with another potential investment, to see whether they should consider moving to a new fund. The proposed performance information will not assist them with this decision.

ASFA is concerned that members could in fact be misled by the performance statistics as they will not understand that it is an aggregate figure, and not a return that they can expect to earn in a particular investment option.

The other important issue to recognise is that such an aggregate return will be impacted by a number of issues including but not limited to:

- The proportion of “superannuation” (i.e. pre-retirement) versus “retirement” money in the trust (noting that there are different tax regimes for returns on each); and
- The aggregate asset allocation of the accumulated assets of all the investment options in all the products in the trust. ASFA notes that asset allocations will vary between different trusts and between different categories, including the accumulation and defined benefits divisions of superannuation funds. As such it will be difficult to draw any meaningful inference from returns where the underlying investments are quite different.

If APRA’s intention is to provide information that is useful to fund members, then it must be provided at investment option level. APRA has committed to providing such data from 2011 – however we are concerned at a two year delay before such information becomes available. Superannuation funds already collect and report information at investment option level, so this information is available and ASFA believe that it can be provided to APRA (including information for the last five years).

Providing information on every investment option in every superannuation product in the market will result in an overwhelming amount of data which will be very difficult for fund members to use. As such if an investment option approach is taken, ASFA recommend that data is collected only for a small number of investment options.

For example, where an industry or corporate fund has a default option containing a large proportion of the assets, that option could be shown. If assets are spread over two or three main options, they could all be shown. For a retail fund with numerous investment options where the assets are spread broadly, their (say) three largest diversified investment options could be shown. This aspect required more thought. ASFA would be happy to work with APRA to come up with a method here.

ASFA formally express our concern regarding the ability of APRA to provide information which will be useful to superannuation fund members based on the information already held. This is because the structures of the industry mean that the data collected is not at the right level to relate to individual superannuation or retirement funds. As such the data would be misleading for fund members.

If APRA determines that investment return figures must be provided to members, ASFA recommends that they are provided for a small number of key investment options within each superannuation or retirement product or division within the RSE. We recognise that new data would have to be collected in order for this to be achieved.

Neither reference publication or any compilation tables should be published until data can be presented at this level.

2. Timeliness of data

Greater member awareness due to almost a decade of investment choice has engendered a greater awareness and vigilance amongst members. Likewise, the Global Financial Crisis has heightened interest in switching. The provision of timely, accurate and comparable data will significantly enhance member education. Indeed, the current circumstances provide the basis for some urgency in this regard as some fund members have rushed to exercise poorly informed investment switching decisions.

The timeliness of publication is crucial for the relevance of the data. The discussion paper proposes a first publication date of April 2009. For this, APRA will rely on data from June 2008. Since that time, most superannuation funds have experienced significant negative returns. The publication in April 2009 of comparison tables based on June 2008 data will, in our view, mislead as opposed to inform members.

ASFA recommends that both the reference publication and any compilation tables be published no more than one quarter after the end of the collection period, and show rolling five and ten year returns to the end of the period. Consideration would have to be given to how to handle key investment options with less than five or ten years of performance history.

3. What fees and costs should be deducted from investment performance?

The purpose of the new statistics is to measure investment returns. APRA’s current methodology deducted all fees and costs of the fund from the return.

It is important to be able to provide a comparable measure of the real costs of a superannuation or retirement fund. However there are different views amongst ASFA’s membership about how this should be done, in part resulting from the different fee structures of different providers.

Some superannuation products have all their fees as a percentage of assets. Some have a mixture of percentage and dollar-based fees. Still others have mostly dollar-based fees.

View 1

Some of ASFA’s members feel that fees and costs are a separate issue to investment performance and the two issues should not be inter-linked. As such only investment-related fees and costs should be deducted from the return of the fund, with other non-investment-related fees disclosed separately (in the same publication and perhaps next to the return).

The logic for this is that some fees are not related to investment options and are structured at a different level.

For example when a fee is charged on a dollar basis it is difficult for funds with assets spread over a broad range of investment options (eg. retail funds) to spread these fees across investment options. How does the trustee decide from which investment option a dollar-based fee should be deducted when determining performance?

Secondly where the level of a fee is dependent on the member's individual circumstances such as where fee discounts are given based on the size of a member's account or the total assets of their employer, how can this be allowed for at investment option level? In this case such funds usually deduct the maximum fee from their returns although the average member will pay a lower fee.

View 2

Other members feel that all APRA should continue to deduct all fees and costs from the investment return. Deducting from returns is the only way in which fund members will get a true picture of the costs of a fund.

If such fees are not deducted from the return, there may be a moral hazard as fund providers may be tempted to shift profit margins or change fee structures to minimise the fees that are included in the investment return.

ASFA commenced a project in September 2008 and has been working with members of the super industry with the aim of getting this approach adopted industry-wide in all investment performance reporting.

ASFA intends to consulting further with our membership to attempt to achieve an agreed common approach on this issue.

ASFA would welcome the opportunity to work with APRA on a project to collect and publish data showing where the real costs are across the industry. This would enable the industry to better understand where cost reductions can be targeted. In order to achieve this, data will need to be collected at a lower level than currently (i.e. at product level).

4. Technical issues with methodology

We have a number of comments of a technical nature on the proposed methodology which are detailed in Appendix A.

Answers to Discussion Paper Questions

Question 1: Which data items and calculations should be included in the comprehensive reference publication? How should these items be presented?

Which data items and calculations should be included?

ASFA formally express our concern regarding the ability of APRA to provide information which will be useful to superannuation fund members based on the information already held. The reason for this is that the structures of the industry mean that the data collected is not at the right level to relate to individual superannuation or retirement funds. As such the data would be misleading for fund members.

If APRA determines that such figures must be provided, ASFA recommends that they are provided for the key investment options within each superannuation or retirement product or division within the RSE. We recognise that new data would have to be collected in order for this to be achieved.

We further recommend that any technical issues with APRA's methodology be addressed, and have made some detailed comments in that regard.

We recommend that ASFA provides additional information to fund members on issues such as strength of management and cost, which will increase transparency, enhance the understanding of members, encourage members to take a long term view; and importantly enhance confidence in the superannuation industry.

We have the following comments and recommendations regarding the data items noted in Part 2 under "Reference Publication"

3. Fund business name(s) – APRA notes that item 3. is intended to provide the business name or names under which a superannuation fund is marketed to members. As illustrated by the diagram in Issues Section 1. above, the entity being reported to APRA is the RSE. For most retail superannuation providers, this is not a particular fund or product. As such it is not possible for such providers to give the name under which the superannuation fund is marketed, as in many cases this name belongs to the next level of detail under this – the product or even individual fund level. As such fund members will not be able to identify their product if data is collected at this level.

8. 9. and 10. Attachment 1 appears to require that both geometric and arithmetic returns are provided. We believe that it will be difficult for many superannuation funds to calculate arithmetic returns as most returns are reported to members on a geometric return. Also as discussed in point 2 of Appendix A, geometric means are more meaningful in comparing investment performance. ASFA recommend that only geometric returns are collected.

Additional data to be collected:

Rather than the proposed volatility measures to be calculated using data in 8. 9. and 10., ASFA recommend that asset allocation information (such as percentage of growth vs. defensive assets) is collected and used as a proxy for risk. Please refer to Appendix A issue 4 for a more detailed discussion of this recommendation.

ASFA recommends that the additional investment expense information be collected so that funds are compared on a like-with-like basis (please refer to Appendix A issue 1).

Additional categories

APRA currently classifies funds as corporate, public sector, industry and retail, and is seeking views on any other sub-groups which might be separately reported.

ASFA recommends that APRA distinguish retirement money from superannuation money in these statistics, as the investment performance is subject to different tax regimes. We acknowledge that this may require collecting data at a different level to the RSE level at which it is currently collected (refer diagram in Issues section 1 above).

In addition we recommend the differentiation between 'accumulation' funds and 'defined benefit' funds be made given that investment performance of the latter is relevant only insofar as the trustee must ensure the fund will meet its liabilities of the benefits promised. Our recommendation is that defined benefit monies are excluded from these statistics.

Outliers

Rather than identifying asset allocation outliers as proposed, ASFA recommends that the proportion of growth and defensive assets be reported alongside to the returns for all funds. Where compilation tables are presented, the key investment options being reported should be sorted into categories according to their asset allocation.

Other outlier funds that should be considered separately are Defined Benefit funds. ASFA recommends that Defined Benefit monies be excluded from the analysis as it is the employer and not the member who bears the investment risk. Members often cannot elect to join or leave a defined benefit arrangement. We acknowledge that data may have to be collected at a different level to that proposed in order to achieve this, as defined benefit assets are often a part of a larger trust that includes accumulation monies.

Question 2: Should APRA publish compilation tables, in addition to the reference table?

ASFA recommends that neither the reference table nor the compilation tables be published until the concerns raised by the industry have been addressed. Such a compilation table should be produced at key investment option level.

Question 3: If APRA publishes compilation tables, what should be included in the compilation(s)?

If APRA publishes compilation tables, ASFA recommends that:

- returns be collected and provided for the key investment option(s) within each superannuation product;
- returns be shown on an after-tax basis;
- asset allocations are provided for each key investment option shown;
- results are grouped by asset allocation ranges;
- results are shown on both a 5 year and a 10 year rolling time horizon; and
- results are provided on a timely basis.

Summary of Recommendations

In order to provide the industry and the public with real information about the health and status of superannuation funds, and in order for that information to be useful and relevant to superannuation fund members, ASFA makes the following recommendations:

- that return statistics are provided for a small number of the key (or largest) investment options within each product or division within the Regulated Superannuation Entity (RSE), rather than at RSE level;
- that when calculating the returns:
 - all relevant investment expenses are captured to ensure like-with-like comparisons
 - either the current method of deducting all fees and costs from returns is retained, or alternatively only investment-related expenses are deducted from the returns and a measure on the non-investment related costs of the fund be shown alongside the investment return (we have divergent views amongst the membership);
 - returns are calculated post tax (as is currently the case);

- returns are calculated using the geometric (not arithmetic) mean;
 - returns are calculated on a time-weighted (not money-weighted) basis;
 - the planned volatility measures not be published, but that the proportion of growth assets be used as a proxy for volatility;
 - retirement money be separated from accumulation money; and
 - defined benefit assets be excluded from the analysis.
- that the return statistics be categorised according to asset allocation ranges; and the asset allocation (or proportion of growth assets) be shown for each key investment option displayed;
 - that data be published no more than one quarter after the end of the collection period;
 - that the rolling five year and ten year returns be shown; and importantly; and
 - that neither the reference table nor the compilation tables be produced until the concerns of the industry have been addressed, and until information can be collected and provided to members at a key investment option level.

ASFA would welcome the opportunity to meet with APRA to further discuss these issues, and we are willing to offer our assistance with the aim of getting the right result for both superannuation fund members and the industry.

ASFA would also welcome the opportunity to work with APRA on a project to collect data showing where the real costs are across the industry. This would enable the industry to better understand where cost reductions can be targeted. In order to achieve this, data will need to be collected at a lower level than currently (i.e. at product level).

Appendix A

We understand the imperative on the Regulator to produce these statistics in a short time frame and as such understand the reason for the desire to produce these from data APRA has already collected.

However, ASFA itself has raised some issues with the proposed methodology and we add some concerns to the list as follows.

In the Discussion Paper and the previous document “A RESPONSE TO Review of APRA’s Investment Performance Statistics of the Australian Superannuation Industry” (we will refer to this as the Response paper), APRA outline a number of issues with the methodology of the performance information.

These issues are as follows:

1. In Part 1 of the Discussion paper, point 2. notes that “the current collection does not capture all investment expenses for some entities and therefore gross income is not consistently measured”. This means that funds are potentially not being compared on a like-with-like basis. ASFA recommends that any relevant additional investment expense information be collected before returns are published.
2. In the Response paper on page 7 under “The calculation of returns using arithmetic means” APRA stated that they would consider using geometric not arithmetic means to calculate returns. In Attachment 1 of the discussion paper both methods are discussed and it is not clear which method APRA intends to use.

We note that the majority of returns in the industry are calculated using geometric means. The purpose of geometric returns is to show the change in the value of any amount invested at the start of the period over the course of the period – this reflects the compound interest nature of how investment returns are allocated to members. Arithmetic returns do not do this and may make comparisons of investment performance misleading.

ASFA recommend that APRA direct that the new “ROA” figures to be collected at items 8, 9 and 10 of Part 2 of the Discussion paper should be calculated as a geometric and not the arithmetic mean.

However, it appears that arithmetic volatility measures are to be used, and as such perhaps both geometric and arithmetic returns are planned to be collected. This will be an issue as the industry uses geometric means and would not have the systems capability to calculate arithmetic means. We suggest in point 4. below an alternative proxy risk measure that would not require the calculation of arithmetic means.

3. In the Response paper on page 8 under “Performance measurement of asset allocation of superannuation funds” APRA stated that their next data revision would enable APRA to calculate benchmark returns based on asset allocation. However the data proposed to be collected does not include asset allocation information. The only asset allocation information to be collected is where the allocation is outside a 50-75% range.

However, the expected investment performance for a fund with 50% growth is markedly different to that for a fund with 75% growth.

ASFA do not recommend that the compilation data be released until it can be provided at key investment option level. However if the compilation data is released and investment option level returns cannot be displayed, ASFA recommends that the funds in the table should be grouped according to asset allocation ranges. Sufficient data should be collected to allow this.

4. In the Response paper on page 10 under “Suggested reporting formats” APRA stated that in their consultation on fund level data, “*selecting risk measures (such as Sharpe ratio) is likely to feature prominently*”.

The volatility measure planned to be used is an arithmetic measure using arithmetic returns collected from the industry. As outlined in 4.2 above ASFA do not believe many funds have this information available as their systems calculate and report geometric returns.

We are also concerned that the Sharpe Ratio formula in Attachment 1 may not calculate a true measure of excess return per unit of risk taken. The standard definition of the Sharpe Ratio is as follows:

$$S = \frac{E[R_1 - R_{1f}]}{\sigma} = \frac{E[R_1 - R_{1f}]}{\sqrt{\text{var}[R_1 - R_{1f}]}}$$

where R is the asset return, R_f is the return on a benchmark asset, such as the risk free rate of return, $E[R - R_f]$ is the expected value of the excess of the asset return over the benchmark return, and σ is the standard deviation of the asset excess return.^[1]

However, the denominator of the formula proposed in Attachment 1 is the volatility of the excess return over the fund’s average return over 5 years. A Sharpe Ratio requires the denominator to be the volatility of the excess return over the risk free rate. As such we do not believe the formula in Attachment 1 will accurately measure of excess return per unit of risk taken.

ASFA recommends that (as per 2. above) instead of using the version of the Sharpe ratio in Attachment 1, that asset allocation (or proportion of growth assets) is used as a proxy for risk. If compilations are published, the returns should be grouped according to asset allocation ranges as suggested in 3. above.

5. Time Weighted vs. Money Weighted returns

APRA’s current approach for prudential data relies on audited information and uses a money-weighted return (MWR) basis.

APRA could consider calculating investment performance on a time-weighted return (TWR) basis rather than MWR basis. In this case it could be done using unit prices/crediting rates for the relevant periods, which should be available much sooner than information provided through APRA returns and audited financial statements.

APRA return information for the key investment options would then be consistent with the returns reported to members (in statements, PDSs etc.) by the superannuation funds for that investment option.

Letter sent on 23 January 2009 to:

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