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Submission to Treasury on the Objective of Superannuation

The Responsible Investment Association Australasia (RIAA) welcomes the opportunity to make this submission to the Treasury regarding the Objective of Superannuation.

RIAA is the industry body representing responsible and ethical investors across Australia and New Zealand. RIAA has 165 members who manage well in excess of \$1 trillion AUM globally. Our membership comprises superannuation funds, asset consultants, fund managers, financial advisers, dealer groups, researchers and analysts, and others involved in the industry, across the full value chain of institutional to retail investors.

Our work aims to see more capital being invested more responsibly, working to shift capital into sustainable assets and enterprises, and shape responsible financial markets, to underpin strong investment returns and a healthier economy, society and environment.

Importantly, our work also connects us on many fronts with consumers - the underlying beneficiaries of much of the activity in the financial system. Importantly, this submission is informed by our experience across the organisations we represent as well as our experience dealing with the underlying beneficiaries of the superannuation system whose interests the system should ensure it is effectively representing.

Key factors for consideration regarding the objective of superannuation:

At the highest level, the recommendation by the Financial System Inquiry that the primary objective of super be *“to provide income in retirement to substitute or supplement the Age Pension”* forms an adequate starting point but remains excessively narrow in a world where our superannuation system contains some of the largest economic actors within our economy and in combination are managing capital at a huge scale with broader system wide impacts.

Broadly we are in agreement that the objectives recommended by the FSI do capture important elements of what the objectives of superannuation should entail, and in particular that this should be focused upon providing means for a comfortable retirement, and not for wealth accumulation and estate planning.

However, for this submission, we would like to highlight a broader set of objectives for superannuation that we feel are not adequately reflected in the FSI recommendations or the Discussion Paper.

The objective of superannuation as a system:

With projections that the superannuation system will be managing \$9 trillion in 2040, it is critical and essential that any definition of the purpose of superannuation considers broadly the implications that the allocation of that capital will have in terms of shaping our nation, economy, society and environment. With or without intention, the way superannuation capital is invested is shaping and will continue shape our nation.

When considered in this light, superannuation has both an individual purpose to deliver each of us income in retirement, as well as a system wide purpose, of choosing the shape of the world into which we will all retire.

From this perspective, it becomes clear that to simply provide income in retirement is an inadequate purpose for such a substantial and influential pool of capital. Indeed, with an excessively narrowly defined purpose, we risk the sector competing to solely maximise returns for an individual, at any cost, which at worst risks an outcome where superannuation fund members could retire into a world with sufficient income, but low quality of life, due to the external costs (social, environmental and ethical) imposed in the narrow pursuit of income maximisation.

Pleasingly, the evidence indicates that we can consider such broader material factors and that these can in fact enhance our ability to make prudent investment decisions, that can be linked to long term, sustainable financial returns.¹

In this way, it is important that the objective of superannuation looks beyond only providing income to an individual in retirement, and additionally considers a notion of the type and quality of that retirement, and the role superannuation will have impacting on that.

For example, if superannuation plays no role in providing capital to build the infrastructure our economy needs, or the medical technologies, retirement homes, affordable housing, hospitals etc., if it supports companies who pollute, erode natural capital, exploit workers, etc. then it risks its beneficiaries retiring into a world where even with a strong income, quality of life could suffer.

In this regard, and directly responding to the issues raised in your Discussion Paper, we view the concept of standard of living as a more useful objective than retirement income.

Consumer primacy:

In addition, it is important that consumer primacy is elevated as a critical objective of superannuation. This has a number of implications, including giving consumers choice as to how their superannuation is invested, enabling transparency so that consumers can clearly understand where and how their retirement savings are invested, and taking efforts to understand what are the beliefs, needs, objectives and values of those consumers and reflecting these in the products being offered.

¹ See for example: RIAA (2015), *Responsible Investment Benchmark Report 2015*; Oxford University and Arabesque

To deliver this means a greater prioritisation of engaging superannuation members in investment decisions by better understanding their values, beliefs and expectations (through regular surveys of members for example) to ensure the superannuation system is indeed serving its clients and acting in their best interests.

In its implementation, it also could involve the ability of consumers to have more control over how their retirement savings are invested, with adequate and prudent constraints. For example, there are examples globally where members can direct their pension fund savings to be invested to contribute to shaping a better society through sound financial investments with a social impact. In particular, the French have a system of Solidarity Investment Funds, whereby consumers can choose to allocate up to 10% of their retirement savings to social impact investments. Consistent with the previous point about the superannuation system contributing to the future shape of society within which members will retire, it follows that members may wish to explicitly direct their own savings towards this end.

Considering the high levels of disengagement by Australians in their superannuation choice and management, this consumer primacy objective necessitates superannuation funds working to better understand the average member's values, beliefs and expectations to then ensure that these are being accurately reflected in the way their superannuation is being managed.

Take for example the fact that a number of surveys have shown consistently that Australians have an interest in ensuring that their retirement savings are invested in a way that does no harm, for example by avoiding tobacco investments.² This mounting body of evidence and consistent findings across a large number of polls indicates that at a default fund level, to be accurately reflecting the expectations of Australians, that these core values and beliefs should be reflected in these default superannuation products. To this effect, it was recently reported in the press that the former CEO of AMP Capital suggested that all superfund trustees and asset managers should consider putting in place a base moral standard implemented across all investments to better reflect the fact that the average Australian does indeed care about the impact that their retirement savings are having.³

For the superannuation system to be truly functioning in the best interests of the underlying beneficiaries, it is essential that steps are taken to better reflect this consumer primacy.

Supplementary changes required to support a more systemic view of superannuation:

It is important, in the context of this ever-growing pool of superannuation capital, that the objective of superannuation reflects the systemic level impacts that this capital will increasingly have in shaping the world into which the underlying beneficiaries retire. In this light, it is essential that we look beyond merely the narrow objective of maximising income for an individual at the point of retirement, as the

² See for example: RIAA polling Nov 2013 here <http://www.responsibleinvestment.org/wp-content/uploads/2014/08/RIAA-press-release-Nov28.pdf> where 69% think its important for super funds to make responsible investments by for example investing in companies that build clean energy infrastructure or avoiding investment that harms the community like tobacco; Essential Research, *The Essential Report*, 21 April 2015 where 59% said superannuation funds should consider social and environmental impact of the companies they invest in; The Australia Institute (2013), *Time to get engaged with super* where 40% believed that superannuation funds should consider ethical and environmental implications.

³ The Sydney Morning Herald, *Super Fund Members Lack Ethical Investment Knowledge*, 4 September 2015

quality of life afforded by this income may be put at risk if we don't adequately address the system wide impacts of superannuation.

This ultimately goes to the core of what is in the best interests of superannuation fund members. In this light, superannuation has a higher purpose or positive duty to act thoughtfully in the best interests of members in order that their retirement is not impacted upon detrimentally, and that members retire into a world where they can achieve a high quality of life.

In order to achieve this, there are a number of supplementary changes that are necessary to allow the superannuation system to fully acknowledge and proactively manage the role it has in shaping the economy and society in which members will retire (through the companies and assets it invests in) in a manner akin to a stewardship approach.

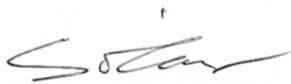
Setting the objective of superannuation in isolation will not shift the way our superannuation system operates. As such, supplementary changes that are worthy of consideration include:

- a focus on clarifying trustees duties, in particular taking a closer look at the sole purpose test under the SIS Act to ensure that in its implementation, the concept of providing benefits for the member's retirement is considered in this broad manner;
- providing updated guidance around the way fiduciaries ought to consider these broader systemic impacts (environmental, social, governance and ethical) as both material risks to be managed, but also issues that members want action on.
- In this light, acknowledgement of a positive duty of trustees to consider broader obligations to act to avoid systemic risks and/or support capital deployment to companies and assets that will contribute to future sustainable economic activity
- A better understanding of what is the nature of best interests in the emerging understating we have of the way members want their retirement savings invested
- A clearer guidance on stewardship responsibilities by owners in this context of system wide implications of capital allocation by superannuation funds

In conclusion

With our superannuation system growing to a scale where investment decisions will have implications on the type of world members retire into, it is essential this is acknowledged and recognised in any legislation that seeks to clarify the objectives of superannuation.

RIAA would be happy to discuss this submission further with The Treasury.



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