



Institute of Actuaries of Australia

# 4th Financial Services Forum

*Innovation in Financial Markets*

19 and 20 May 2008 – Melbourne

## **Benefit Projections and Online Calculators - Discussion Paper and Current Issues**

### **Benefit Projections Working Group**

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## Outline

- Background
- April 2008 Discussion Paper
- Revision of GN 466
- What next?



## Background

- Importance of projections/ calculators in a DC world
- Actuarial involvement GN 466
- ASIC Class Orders (05/1122)
- ASFA assumptions paper
- IFSA Best Practice Guidance
- Parliamentary Joint Committee recommendations:
  - further consultation with funds about calculators
  - provide additional regulatory relief
- April 2008 Discussion Paper
- Sydney and Melbourne forums (with ASFA, IFSA, ASIC, AIST and ISN representatives).



## Uses of projections

- a) Potential amount
- b) Planning/budgeting contribution levels
- c) Impact of fees and costs
- d) Relative impact of different fee and cost structures and levels
- e) Impact of different investment strategies, assets and managers on likely outcome
- f) Impact of different investment strategies, assets and managers on variability of outcome

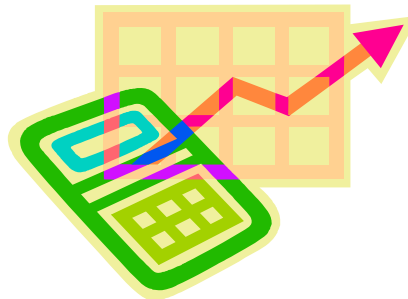


Few Printed  
Projections

PDS fee  
disclosure may  
mislead

Age Pension  
ignored /  
Lump sum focus

Calculators  
differing results  
- “today’s” dollars/  
assumptions



Inadequate info  
about risk /  
sensitivity

Some online  
calculators are of  
poor quality

Universal  
Retirement  
Forecast

Unclear  
regulations,  
“stalemate”,  
“pre-population”

## Issues



## Issue #1

Few Printed  
Projections

- Not exempt from FSR Advice Provisions
- “reasonable inquiries” into personal circumstances

### Suggestion:

- Class Order exemption for Printed Statements for existing members
- Exemption given if Standard Assumptions used
- Standard Assumptions set by Australian Government Actuary



## Issue #2

Calculators  
differing results  
- “today’s” dollars/  
assumptions

- Different approaches to deflating results
- Different default assumptions

### Suggestion:

- Standard default Assumptions set by Australian Government Actuary
- Terms like “Today’s dollars” be defined and standardised
- “Today’s dollars” = Salary based deflator
- Minimum standardised disclosure
- Comments on ASFA, IFSA, FIDO assumptions



## Issue #2 Standardised assumptions gross or net ?

- **Gross** example (ASIC):
  - Growth: 8.5% gross (of tax and fees and costs)
  - Balanced: 8% gross ( ..... )
  - Cap stable: 6% gross ( ..... )
  - Cash, Cap G: 5.5% gross ( ..... )
- **Net** example:
  - maximum* of 7% net of tax and net of investment fees and costs





## Issue #2 Section 3.4

“ ... with a gross basis it is necessary to make different assumptions for different asset classes (or else, because the projection [explicitly] includes both administration and investment costs, cash based [and passive] products with lower investment costs will be favoured). This adds greatly to the complexity.”



## Issue #2 Why net?

- Simplicity of **one** maximum (not four, or more)
- Consistent with IFSA and IAA standards
- Corporations Reg 7.9.01 *net earnings*
- Accepted common practice
- Sharper focus – administration fees and costs will not be swamped by investment fees and costs
- Choice of an investment option seldom requires a projection of investment fees and costs



## Issue #3

Some online calculators are of poor quality

- Studies show varying results
- Explanations are often inadequate

### Suggestion:

- Minimum disclosure to include who reviewed calculator and which professional standard was used to review it
- Projections/calculators should have standardised minimum disclosure explanation items – with consumer testing



## Minimum information – Section 6.1

1. Member account balance at start
2. Contributions and contribution increases
3. Fees and costs (and increases allowed for)
4. Investment earnings and whether net or gross
5. Salary or price deflation
6. Death and disablement costs deducted
7. Contribution (and excess) tax allowed
8. Government co-contribution allowed for
9. If lump sum – benefits tax allowed
10. If income benefits – basis and split/interaction with social security



## Issue #4

Age Pension  
ignored /  
Lump sum focus

- Major source of retirement income is ignored
- Lump sum results are not meaningful

### Suggestion:

- Encouragement to show results as income
- Rule of thumb for converting lump sum into income
- Encouragement to show Age Pension income
- If Age Pension included, must be separate



## Issue #5

Inadequate info  
about risk /  
sensitivity

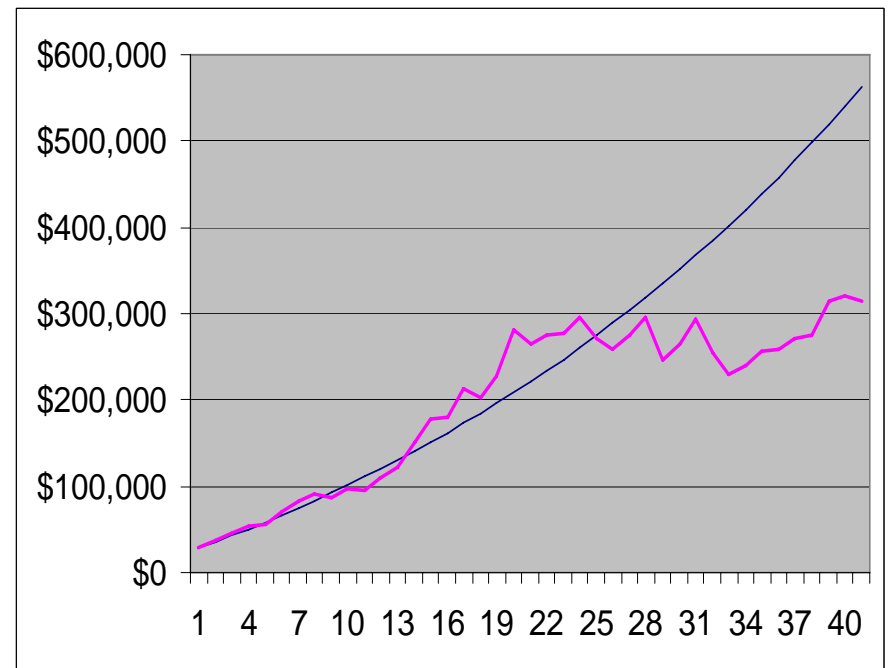
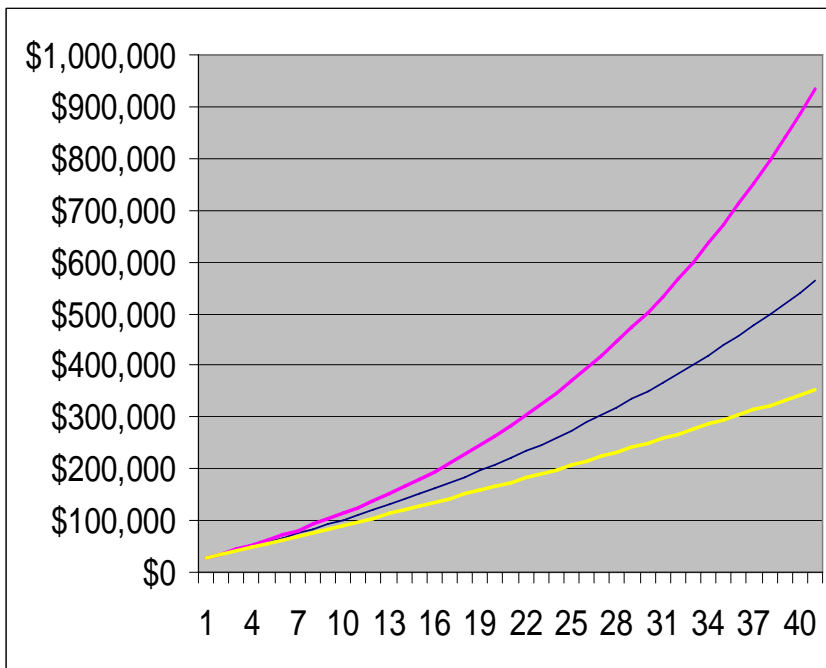
- Often no sensitivity shown / impact of uncertain outcome
- 3 deterministic forecast misleading

### Suggestion:

- Showing sensitivity of results is important
- Showing +/- 1%pa may be misleading (level and shape)
- +/- 2% at end point only
- Shape



## Issue #5





## Issue #6

Unclear regulations,  
“stalemate”,  
“pre-population”

- Can calculators be pre-populated with data?
- What is a product specific calculator? (does using a fund’s own fee structure as default make it product specific)?
- Are Risk Profilers exempt?

### Suggestion:

- Pre-population be allowed (under class order)
- Clarification of product specific default assumptions required.
- Clarification of status of risk profilers required





## Issue #7

Universal  
Retirement  
Forecast

- Compulsory Benefit Projection Statements
- Government Policy

### Suggestion:

- Enumeration of issues for Govt to consider, including
  - Standard Assumptions etc
  - Liability
  - Consistency with funds' web calculators & new business fee disclosure
- IAA in UK provided assistance in drafting Technical Memorandum & setting assumptions (now with Board of Actuarial Standards)



## Issue #8

PDS fee disclosure may mislead

- Standardised fee disclosure is for one year only
- Doesn't show impact of asset or contribution based fees and costs over time

### Suggestion:

- PDS's showing standardised projection of administration fees and costs (for say two contribution levels) is a powerful way to illustrate their impact



## Guidance note 466

### PROJECTED SUPERANNUATION BENEFIT ILLUSTRATIONS

- 3.5 The actuary should describe or illustrate how the result will differ if the assumptions used are not borne out. Possible approaches to illustrating volatility **and assumption uncertainty** include:
- 3.5.1 providing multiple illustrated benefits **at retirement** with variations in the key assumptions, for example different investment return assumptions and annuity rates;
  - 3.5.2 quoting the effect **at retirement** of an addition to and a deduction from the key assumption, for example investment return;



## 3.5 continued

- 3.5.3 stochastic **or historical** analysis, for example, a demonstration using scenarios over a range of reasonably possible future investment returns.
- 3.5.4 stochastic analysis, for example, illustration of a ‘funnel of doubt’ from a specified probability distribution based on scenarios from a wide range of reasonably possible future investment returns.

The use of two or more deterministic illustrations showing year-by-year projected benefits should be avoided, because such illustrations may give the misleading impression that any variation from say the assumed investment earning rate will be constantly higher or lower than the assumed rate and/or always within the limits of the two or three deterministic results.



## New section

### 3.9 The terminology:

- **“in Today’s Dollars”** should be reserved only for adjustments which include both inflation and rises in community living standards – thus the terminology “in Today’s Dollars” would be used when projected amounts are deflated using salary-based, AWE-based or AWOTE-based assumptions,
- **“in Future Dollars”** should be used for situations where there are no adjustments, and
- **“in Deflated Dollars”** should be reserved only for adjustments which include only price inflation.



## Other

- Corporations Act and Regulations
- account-based pensions
- fees and costs
- income amount to be expected over the member's lifetime **or other specified period**
- Delete references to surcharge and excessive benefits.



## What next?

- Practice Note **or** Professional Standard?
- Discussions with ASIC
- Universal Retirement Income Forecasts
- *Actuary Australia* articles
- PDS fee and cost disclosure?
- IFSA Standard?
- AFSA, AIST, ISN, FPA, FEAL (others?)
- ACA and Consumers