Submission template: Review of KiwiSaver default provider arrangements

[Name of submitter]

Section 1: Your details

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Are you requesting that any of this submission be kept confidential? Yes/No

If yes, please let us know why the information should be kept confidential in accordance with the Official Information Act. Please also send us a redacted version of your submission for publication.

Reasons for withholding:

Section 2: Feedback on discussion paper

~~1.~~ **What is your feedback on the proposed objective for the review?**

All good

~~1.~~ **What is your feedback on the proposed criteria for the review? How should the criteria be weighted?**

I think these are very good. The first is most important, second is also a high priority. The third, no doubt, contributes to keeping fees low.

I'm very pleased to see the 4th option. As Kiwisaver will, in time, become a massive pool of investment money, some of it should be directed towards this purpose. Otherwise, we may end up with heaps of money flowing offshore into Vanguard Index Funds, which is great for low-cost diversification, but does not help to enhance and develop NZ's capital markets and economy. (Please note I did not mention "growth". Innovation and increase in productivity is fine, but we need to start living within sustainable limits.)

The 5th criteria is also pleasing to see and similar to (yet different) the 4th.

~~2.~~ **What is your feedback on the problem definition for the investment mandate? Is a move away from a "parking space" purpose justified?**

This is a serious problem as presumably those members who stay in the default funds are the least 'savvy' and therefore the most in need to a system that will deliver the best outcome for them automatically. A conservative mandate is probably not the best option for most of these Kiwisaver members.

~~3.~~ Should the investment mandate options (and other options, for example in relation to fees) apply only to default members who have not made an active choice, or should they also apply to members who have made an active choice to stay in the default fund? Why or why not?

It should definitely apply to default members who have not made an active choice. As for those who have actively chosen a default fund, they have demonstrated a higher level of engagement already. So they 1) want to be in a conservative fund because they are planning to use that money in the near-term (less than 5 years) or <u>they are under the mistake impression that conservative is always better which it actually guarantees an inadequate return.</u> It is hard to know which, so I would suggest an education campaign coupled with an 'opt-out' situation. So those members who have actively chosen a default (conservative) fund would get information (such as the sorted.org info referenced on pg 12) and notice that <u>they will be switched to the other option by a certain date unless they opt to stay in the conservative fund</u>.

~~4.~~ If a life-stages option is adopted, what "stages" should apply and to which age groups? Should there be a "nursery" period?

I definitely agree with the 'life-stages' option and with the 'nursery' period...with one very strong suggestion and this relates to investor education. Everybody should be taught the '3 buckets' idea. The money you anticipate needing in the next 5 years (say for a house deposit) should be in a conservative investment as you won't have time to recover if a big market correction happens during that time. Money that is needed 5-10 years from now should be in balanced and 10+ years should be in growth. It's a very simple concept and would help people enormously to choose where their money is allocated. It would also help for people nearing retirement as arguably some, but not all of their money should switch to conservative, but some should stay in balanced and even growth. So definitely set 'life-stages' based on averages, but they should also be capable of being tailored to individual needs.

~~5.~~ If a balanced investment mandate is adopted, what range for growth assets should be applied?

I agree with the narrow range. I wouldn't consider a 35% growth investment to be balanced; it is too low. 50-60% is much better.

~~6.~~ If a growth investment mandate is adopted, what range for growth assets should be applied?

I would be wary of a 90% level as this will be very volatile and when markets plunge (like in 2008) people can freak out. That is why, education idea #2, people should learn the famous Ibbotson/Morningstar charts showing that <u>over the long term</u>, growth investments way out-perform conservative ones, but <u>in the short term</u> they can be a gut-wrenching roller-coaster ride. This is why I object to the current BNZ add where the lady with the green face mask suddenly switches her *investments from conservative to growth. It is well established that lay-people do the wrong thing at the wrong time - plunging into, for example, dot-com stocks right before the collapse, then panic when markets plunge and turn a paper loss into a real one and then are frightened from going into such investments every again – missing out on all the later gains. Just look at the legacy of the 1987 sharemarket crash. Yet shares give the best long-term investment. Somehow we really need to educate people about this so they understand short term volatility is part of long term success.*

Education idea #3: teach people about 'dollar-cost averaging' and that when markets go down, it's like McDonalds, Coke and Apple shares have gone on sale. Every dollar buys more shares. Woohoo! Pity that the previous government (Sir JK and Sir BE) didn't understand that's what the Superfund does; missed one of the best 10-year bull markets in history.

~~7.~~ **If a conservative investment mandate is adopted, what range for growth assets should be applied?**

No. Locks in mediocre results for those who are less savvy.

~~8.~~ **If a life-stages, growth, or balanced option was adopted, how should we mitigate the potential issue in relation to first-home buyers and other people making early withdrawals?**

See above, I vote for a 'nursery' period where you can choose between the 3 buckets, then apply the 'life-stages' to anything not otherwise allocated by the member. Those who are passive are probably not doing any of their investments properly and need all the help they can get so they have a better outcome with their investments. Pushing them to growth (assuming they are young) will ensure that result.

~~9.~~ **What would be the administrative costs to providers of choosing a life-stages option?**

Well worth it. The people will be better off.

~~10.~~ **What is your feedback on the different options? Do you agree with our assessment of the costs and benefits of the option? Which option do you think is best and why? Is there another option that we have not considered that would be better than the options discussed?**

Regarding criteria 4 & 5, I think we would definitely see improvements in both these areas.

~~11.~~ **What is your feedback on the level of value that KiwiSaver default members get for their fees? What are the costs that are within and outside a provider's control? To what extent are fees too high?**

Ok, I just had a squiz at vanguard.com and what they charge institutional investors and most were under 0.10%. Most were under 0.08%. So there's most of your global diversification pretty cheap and easy.

Yes, fees are way too high for what most of these companies are currently providing. If, however, some of the default money goes into NZ investments, I can see where that bit could justify a higher fee component.

~~12.~~ **Is it a problem that fees disproportionately affect those on low income and under 18s? Why/why not?**

Absolutely. Low income people need even more help building a nest-egg instead of that being sucked off to (often foreign) company shareholders. For those under 18, getting more money working for them earlier means they'll have much more at retirement.

Education idea #4: The power of compounding, both when it is working <u>*for you*</u> *in terms of investing more and earlier, and when it is working* <u>*against you*</u> *in terms for fees, interest on debt, hidden charges, etc.*

~~13.~~ **If the government sets a fee, what should the fee be set at for the different investment mandate options? What considerations, methods or models could be used to determine the fee? What should be the balance between fixed and percentage fees?**

Don't like this idea – risks the fee is set too high or too low.

~~14.~~ **What fee arrangements would best promote the objectives of the review? What is your feedback on the fee options? Do you agree with the costs and benefits identified? Which option (or the status quo) do you prefer and why? What other approaches or models could be used to reduce fees?**

Regarding Option 2, I prefer the variation as the benefits would extend beyond the default funds to encompass all of a providers offerings.

Regarding Option 3, this should happen as a result of increasing scale, but apparently has not, so presumably it must be prescribed. So I agree with this.

Regarding Option 4, I agree with the variation proposed. I know of people who put $1000 into their child's Kiwisaver to get the government matching (before JK and BE stopped that), then watched as the balance was eroded by the fees outstripping the earnings. Not a good result. I'm quite happy to subsidise mokopuna to help them get ahead.

Also, Metiria Turei had the great idea that every child would get a Kiwisaver account at birth with $1000 in it. Generally the more well-healed folks help their kids save whilst poorer folks are unable to start their kids on a savings program, thus inequality becomes more entrenched.

Regarding Option 5, I agree with this idea for the same reasons as for the under 18s. Providers who coax unsuspecting members away from the default funds to the fee-charging ones should know they would face sanctions for not looking after their customers' best interests...there's been a lot of that lately, eh?

Re Option 6, I agree with this a fixed fees are harder on those with smaller balances. You could still consider tenders with low-cost fixed fees.

~~15.~~ **How has the number of providers in the default market affected innovation, competition and value-for-money in the default market and in KiwiSaver more generally?**

Given that a large number of default members are passive, I wonder if too many providers is just overwhelming without really providing a benefit as these members obviously aren't comparing *different providers. Do we have more innovation - or just more complexity? Sadly, many members go to their bank for advice and you can guess what advice they get. I have friends like that. They are chefs, teachers, hard working folks who are incapable of evaluating the different options, so they go to someone they 'trust'. If we use the 'nursery' and 'life-stages' coupled with the '3 buckets' idea, most people will fit in a pretty standardised set of options which will then minimise costs, enhance scale and probably give better outcomes for the vast majority of people. Five providers could do that, I reckon, but government would really need to monitor...no more AMI Insurance or ANZ/ING frozen funds or Ross "Investments" debacles, thank you.*

All this complexity reminds me of how busting up ECNZ and creating the gen-tailers was suppose to create a more efficient energy market. Didn't that work a treat? Again, savvy people can try (I emphasis 'try') to figure out their best option, but a lot of people are getting hosed.

~~16.~~ **Do you agree with our assessment of the costs and benefits of the different approaches for the number of providers? Can you provide us with evidence that might help us quantify the size of the costs and benefits? What option do you prefer and why?**

The only concern I have with the idea of fewer provides, is that they will have a big advantage in the market compared to other funds...however, I think default members are likely the most vulnerable Kiwisaver investors and need protection – from their own ignorance of handling money and from rapacious financial companies. There will be enough active investors in the Kiwisaver realm for non-default providers to go after.

~~17.~~ **If a "minimum requirements" approach is taken should this be on a period-based or rolling system, and why?**

This whole thing seems like a bad idea to me. Too difficult to monitor, lower economies of scale, high costs to implement and turnover. What's the benefit?

~~18.~~ **Are there higher investment costs for responsible investing? If so, how likely are these costs to contribute to lower net returns?**

It is simply too early to tell, these funds have not been around long enough to give a statistically robust indication one way or another. However, this is clearly how investments will be defined in the future and it's coming fast. There are already numerous international bodies (such as Sustainability Accounting Standards Board and Aviva Investors to name a couple) who will increasingly signal which companies are good, neutral and bad, then capital will flow accordingly. It is delusional to not see where this is heading and get with the program sooner rather than later. I have not doubt that in time, the responsible investments will outperform.

~~19.~~ **How does responsible investment affect returns? Does it increase or decrease returns, and to what extent?**

See above. Also, we also need to consider more than just financial returns. People have indicated they don't want to invest in cluster bombs and such. I think you can have a conscience and get a good return too.

~~20.~~ **Should the default provider arrangements be used to achieve objectives in relation to responsible investment?**

The main objective is a good return for default members, I don't think responsible investment will compromise that objective and more likely will enhance returns. It will likely ensure that this practice will become standard across all Kiwisaver funds.

~~21.~~ **Would default members want their funds to be invested more responsibly? If yes, is the same true if responsible investment means potentially limiting future returns?**

I doubt the last of uptake of responsible investments is due to lack of interest, but rather the other reasons mentioned – uncertainty, credibility, complexity, lack of time to figure it all out. It's difficult for the professionals! That why the SASB and Aviva are doing their work. We don't all have to reinvent the wheel. There is the fear of a lower return, but I think it will be the opposite. We can't wait 100 years for robust data, we've got to get on with it.

~~22.~~ **To what extent is it a problem that default members do not have information about whether their investments are made responsibly? Would having more information make a difference to the behaviour of default members? What alternatives might there be to more/standardised information to address responsible investment concerns?**

See above.

~~23.~~ **Do providers' current responsible investment exclusions meet what default members would expect?**

I think there is a clear indication that members want responsible investing to some degree. Option 1 (a) seems like a reasonable step and is what the Superfund is already doing. It is probably a cost-effective way to start this process.

~~24.~~ **If this option is adopted, what industries or sectors should be excluded? Should the government instead adopt an international exclusion standard or certification regime? What would be the costs associated with an exclusion or certification regime?**

I think this should be done across all funds offered in NZ, not just default Kiwisaver. Look what happened a couple years ago when people learned their money was going into cluster bombs...my understanding is that Vanguard created an index for NZ that excluded those companies and also a few other areas as well. So our change prompted their innovation and it's high time too. Vanguard is just now getting around to some basic ESG options; they are well behind the times.

However, I suspect the passive default investors will also not actively inform themselves on this aspect either, but we should do it anyways.

~~25.~~ **If this option is adopted, what form should standard disclosure take? For example, should all providers be required to provide a statement listing all excluded companies by sector?**

See above, yes, everybody, all funds – not just default.

~~26.~~ **What is your feedback on our assessment of the costs and benefits of the responsible investment options identified? Which option (or the status quo) do you prefer and why?**

~~27.~~

The costs are likely exaggerated, the benefits will likely come. I prefer both options really. If I have to choose, then Option 1.

~~28.~~ **What limitations or problems exist in relation to New Zealand's capital markets? How could the settings for KiwiSaver default providers be amended to support the development of New Zealand's capital markets? How do the liquidity and pricing rules affect default provider investment in alternative New Zealand investments?**

I'm very pleased to see this idea being explored and fully support it. Good on ya! However, why do we want to encourage companies to list domestically? To my mind this comes back to the various capital markets reviews that tend to be about propping up the NZX. Selling interests in the power companies and Air NZ was supposed to fix that, right? Look at how much of the NZX is former SOEs. When NZ companies go on the NZX, they go into partial of complete foreign ownership (via a buyout offer)

I would prefer the development of something like a venture capital fund, run by the guardians of the Superfund or similar. This could support early stage companies development <u>*and*</u> *fund infrastructure projects with an income stream – like the proposed toll road to Whangaparoa that Auckland can't afford so it is contemplated that a chinese company would build it and collect the tolls for 30 years. I should think this would be comparable to a AAA-rated bond and be suitable for little old ladies to put some of their nest-eggs into. There are heaps of these projects that need to be built and I'm sick and tired of hearing that we need foreign investment – what we need is investment products that people have confidence in that will direct the capital to these opportunities instead of them going to offshore interests.*

I would trust the guardians of such a fund to judge if a company has grown to the point that it's best to sell, then do an IPO onr a private placements sale, ok. But please, no more selling off basic infrastructure or strategic assets. I would want those held in trust for all NZers; outside the control of government ministers.

As for the liquidity problem, just as with a hedge fund, you can suspend withdrawals for 90 days during market volatility (see above about stupid trading behaviour and teaching people about market volatility).

~~29.~~ **How could the default settings be used to develop New Zealand's capital markets? What parts of New Zealand's capital markets are most in need of development?**

Isn't there a Quebec pension fund trying to buy into the light rail project in Auckland? Couldn't we do like Singapore and Japan and buy the land around the stations before these rail projects are built and build/own the development around these stations so that we, the people, capture the capital betterment created by these government projects? Instead of speculators? Couldn't we also then provide affordable housing, just like those countries do? Couldn't we own the revenue producing part of the project as well as the part you should subsidise (the transport corridor)? Again, that would be a AAA-rated income stream.

I'm not talking about something bigger than the Kiwisaver default funds...I'm talking about a sovereign wealth fund. Sort of like the old Superannuation Corporation we used to have before Muldoon canned it. Brian Gaynor figured it would be worth half a trillion now.

https://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=11940232

~~30.~~ **Should default funds take an active role in helping develop the New Zealand capital markets? Would this support the purpose of the KiwiSaver Act and the accumulation of retirement savings by default members?**

I think the rant above covers this. I think it would provide both growth and conservative options for Kiwisaver members (both regular and default).

~~31.~~ **To what extent is the management of default funds currently located in New Zealand or carried out by New Zealand entities?**

I don't know about that, but I have suspicions regarding the foreign owned banks.

~~32.~~ **What is your feedback on a New Zealand-based management option? If this option is adopted, which part of the investment process do you think should be based in New Zealand to help develop New Zealand's capital markets? What type of mechanism would best give effect to this requirement?**

See above about how to do it. Rather than each Kiwisaver provider trying to figure this out (which would be pretty expensive) make a great big fund to increase diversification and lower costs to everybody. It will definitely need very good and trustworthy managers. If it is like the Superfund, it can operate at break-even cost structure. Who would we hire outside NZ? Why would we need that for this part?

As for developing the capital markets, here's an idea: In addition to the Kiwisaver fund, we create a parallel copy that is discretionary investment. If you look at how the Superfund has performed since inception (including the dark days of the GFC), it's been one of the best investments around. Why can't Kiwis get a piece of that? Why can't we get the guardians to invest our money for us? There's something like $165 billion languishing in bank accounts – some is needed for transactions, but the fact is Kiwis put their money into bank accounts and property investment because they're afraid of everything else. Because they or someone they know has been burned badly. That's the real problem with our capital markets. We have plenty of capital, it's just in the wrong places. Create a product people can trust and they'll put their money there. Especially if they are taught:

Teaching Example #5 (I think, I've lost track) Ta-Dah: Diversification! Remember the oldies who said, I'm diversified, I'm in 5 different finance companies. Well now their in a couple of rental properties. Oh that's much better (sarcasm). Or a farm or two or three. Kiwis need diversification, big time!

~~33.~~ **What is your feedback on a targeted investment requirement? If the option is adopted, what market should be targeted by an investment requirement (eg early stage companies)?**

I would keep it small to start. It'll take time to do anything, but please consider what I've written above. Look at Singapore. We can do that here and it time it would be huge and everybody would be much better off.

~~34.~~ **What is your feedback on our assessment of the costs and benefits of the options to develop New Zealand's capital markets? Which option (or the status quo) is best and why? Is there another option that would be better than the options discussed?**

My suggestion basically solves all these problems.

~~35.~~ **What is your feedback on the problem definition for the transfer of members? What other problems are there in relation to the transfer of members?**

Yes, big issue.

~~36.~~ **If default members are transferred from providers with more members to providers with fewer members, how should we decide which members are transferred?**

I prefer Option 1, otherwise the earliest providers have a significant advantage. New broom even though it will initially cost more. There's a huge risk that passive members will stay with deleted providers and not get the benefits of the new changes and would lose the protect of the old regime. If an existing default provider is reappointed, they will lose a portion of their default members, enough to rebalance with the newly appointed members. Deleted providers will lose all existing members unless they choose to stay. It will cost more, but provide much better incentives to the providers and ultimately results for the members.

Options 2 – existing providers still have the benefit of previous rounds, not as good for investors.

Options 3 – nope.

~~37.~~ **If transfer option 1 or 2 were adopted, how should default members be given a choice to remain with their current provider for this option?**

Notice (email and letter) of what's coming, that they will be automatically re-assigned, that they can choose to stay with their current provider, but if that provider is is not a default provider, then they should be made aware of the consequences, i.e. likely lower life-time returns and higher fees. These letters come come from the current provider but match a standard format so they aren't misleading.

~~38.~~ **What is your feedback on the transfer options and the costs and benefits of the options? Which option (or not transferring at all) do you prefer and why? Is there another better option we have not considered?**

I think members will be better off with Option 1 and to a lesser extent, Option 2.

~~39.~~ **What factors should the review consider in deciding transition timeframes?**

1 July 2012 is a fair way off. Perhaps start the information campaign 3 months before that so people are aware of what's happening, then another letter when your default provider is delisted or that you are about to be switched to another provider. If you go for Option 3 (I don't know why you would) then a 3rd letter to those who were passive investors and still are in a now delisted provider.

~~40.~~ **Should active defaults be considered default members for the purposes of transfers? How should active defaults be treated and notified of any changes to default provider settings?**

Yes, my partner is in this position. Even if a person has made an active choice, they should still be made aware of the changes and why they've been made, so they can made an informed (or better informed) choice about something so critical to their long-term well-being.

~~41.~~ **What is your feedback on the member education requirements that default providers should have in relation to default members, and how these should be enforced in the instruments of appointment?**

I'm with Superfund, and I've been very pleased with their annual seminars and the information they give. My partner is with Simplicity and Sam Stubbs and Shamubeel Eaqub have come to Christchurch for an information avo, so that was good. I don't know what the others do.

But here's the thing, we wouldn't think that someone can read a book and do their own root canal, why do we think a teach, a painter, a dentist, can do their own investment planning? People need to learn a few basics – se the Education Examples above – and that's about it. The rest is too confusing. I've looked at the MFA and Sorted.org websites. I think most people's eyes will glaze over or they won't understand it. I understand it because I've spent my life on this stuff. Most people are sheep to be shorn or geese to be plucked (just enough so they don't bite or flee). And the more they need help, the less likely they are to understand what you're saying. Keep it simple. Teach the bedrock basics. Provide people with products run by managers they can trust.

~~42.~~ **What is your feedback on the other requirements that should apply to default members?**

I'm interested in the bit about "Compliance and regulatory" - a couple of the present default providers have run foul of that with the RBNZ and FMA of late, haven't they? Will there be a consequence to that?

~~43.~~ **Any other feedback?**

Apologies for messing up the bullet points; I always have trouble with that.