

2 May 2023

Shibani Iyer – Director
Member Outcomes and Governance Branch
Retirement, Advice and Investment Division
The Treasury (via email)

Dear Shibani,

Superannuation Performance Test Regulations 2023

Ethical Super Australia welcomes the key changes proposed to be made to the Your Future, Your Super performance test, namely the extension of the lookback period to ten years and the increase in the number benchmarks. These changes will help to partially address a number of the unintended consequences of the current performance test framework.

As outlined in the Assistant Treasurer's media release of 4 April 2023, *"[t]he existing test may not reflect the diversity and objectives of choice products. At the same time, it remains important that funds are held accountable for underperformance in the choice sector. Values-based products were a key example where the investment strategy may deviate from the benchmarks, increasing the risk of failure and constraining the trustee's ability to meet its members' objectives."* In other words, this competitive disadvantage for values-based products remains.

However, one relatively simple way for values-based products to be better accommodated in the performance test is to increase the minimum years of investment history a product requires before being subject to the test from five to eight years. Such a change only requires an amendment to the Superannuation Industry (Supervision) Regulations 1994 and would result in a differential of two years to the test's ten-year lookback period, which would remain consistent with the lookback differential the test had when it was first implemented (five-year minimum history required to be included in the test, which was based on a seven-year lookback period).

We note that an eight-year minimum performance history would also align to the timeframe APRA focuses on in its public analysis of Heatmap outcomes (out of the three, five and eight-year investment return timeframes, APRA highlights investment underperformance at the eight-year interval only). This approach is outlined in APRA's December 2022 MySuper Heatmap Insights Paper: "[a]ssessing performance over longer time periods is most relevant as this is more consistent with the long-term nature of most members' investment in superannuation."¹

Further, maintaining the two-year lookback period differential would minimise the unintended skew towards or away from newer products, many of which are values-based, that can arise from short term shocks. This occurs due to each quarter's returns having a larger impact on newer products as they have less quarters of performance history. An extreme example of this distortion is the recent shock to global energy prices arising from the invasion of Ukraine. Many values-based products explicitly exclude investments in fossil fuel-related companies as they are not aligned to their members' values. However, these types of investments have outperformed due to the invasion and are reflected in a number of the benchmarks utilised in the performance test. As a result, many values-based products have been detrimentally impacted by the invasion of Ukraine, which the current calibration of the performance test is unintentionally exacerbating.

In summary, maintaining the two-year differential between the minimum lookback period and the new ten-year lookback period of the performance test would go some way towards the test better reflecting the diversity and objectives of choice products, while still ensuring all Choice Trustee-Direct-Products are captured by the test.

¹ <https://www.apra.gov.au/superannuation-heatmaps>: Insights paper - MySuper Heatmap 2022, see page 7.

About Ethical Super Australia

Ethical Super Australia Limited (ESA) is a not-for-profit trade association whose membership includes high-conviction ethical and faith-based superannuation funds. These funds include, Future Super, Verve Super, Cruelty Free Super and Crescent Wealth. ESA advocates for a greater understanding of the ethical superannuation movement in Australia, which is growing at over 2.5 times the industry average as a growing number of people living and working in Australia choose to align their super fund to their personal values.

Yours sincerely,



Fahmi Hosain, Chair