

# Submission: Legislating the objective of superannuation

30 March 2023

## Overview

The Responsible Investment Association Australasia (RIAA) thanks Treasury for the opportunity to comment on the proposal in *Legislating the objective of superannuation: Consultation paper* (the Consultation Paper).

Australia's superannuation sector plays a critical role in the way Australians plan for and live during their retirement. RIAA broadly agrees that the proposal to codify the objective of superannuation could bring clarity and stability to the superannuation sector. It can also complement existing obligations for superannuation funds to deliver the best outcomes for members.

We recommend that the proposal be strengthened in the following ways:

1. The definition of 'sustainable' should:
  - make clear that implementing responsible investment strategies is consistent with the purpose of superannuation, and
  - include investment with appropriate long-term time horizons in mind, considering the risks and impacts of sustainability challenges such as climate change, and how superannuation investments can help mitigate those.
2. The legislated objective should align with national and global sustainability goals, including combatting global warming.
3. Existing legal obligations for superannuation funds, including the Your Future Your Super (YFYS) performance test, should align with the objective.

Our views are detailed below.

## Response to consultation questions

### 1. What do you see as the practical benefits or risks associated with legislating an objective of Australia's superannuation system?

The Consultation Paper states that legislating the purpose of superannuation could provide clarity for regulators, policy-makers and Government.

Codifying the objective of superannuation in an appropriate manner (see below) could also provide:

- clarity for the sector itself and, as a flow on effect, for the millions of Australians who are saving for their retirement or drawing on their savings, and
- greater long-term stability for the sector.

## 2. Does the proposed objective meet your understanding of the objective of the superannuation system in Australia?

RIAA supports the proposed objective of superannuation being:

*‘to preserve savings to deliver income for a dignified retirement, alongside government support, in an equitable and sustainable way.’*

We broadly agree that superannuation must be ‘sustainable’, that is, ‘robust to demographic, economic and social change, and... cost-effective for taxpayers in achieving retirement outcomes’ (Consultation Paper, page 11).

It is important that superannuation is invested for the long-term future of Australians, and contributes to creating the world that Australians will retire in to. This is arguably as important as the direct financial returns on fund members’ retirement savings.

### Meaning of ‘sustainable’

Sustainable investment will ultimately result in maximising superannuation fund members’ financial returns over the long-term.

Anticipated changes in our society, environment and economy over coming decades are a critical considerations in ensuring the superannuation system is sustainable. This is why responsible investment approaches – which focus on long-term returns and mitigating environmental, social and economy-wide risks – are central to a sustainable superannuation system.

An obvious example that highlights the need to ensure that superannuation is more broadly ‘sustainable’ is the impact of global warming on the superannuation system. The risks and opportunities of mitigating global warming, and adapting to the impacts of climate change, are systems-wide and global. The direct impacts of climate change, as well as mitigation and adaptation efforts, will increasingly affect investee companies and the lives of superannuation fund members.

Impacts of climate change on the broader sustainability of the superannuation system include:

- **Valuation of holdings:** The valuations of particular sectors and companies are changing, as investor and consumer demand shifts away from some sectors – chiefly high emitters of greenhouse gases (GHGs) – and towards others, such as renewable energy. The same is true of investors shifting towards companies that are taking stronger action to reduce their GHG emissions.
- **Investment risks:** The risks of investing in sectors and companies which are significantly affected by the impacts of climate change (such as insurance) are increasing. This is true across various time horizons.
- **Impacts on communities:** Communities across Australia are increasingly impacted by climate change and/or efforts to reduce GHG emissions, particularly due to the destruction of homes and changes in employment. The social changes brought about by climate change will impact superannuation funds’ investment risks and returns, as well as personally affecting fund members.

Given these examples of systemic risks and impacts, the definition of ‘sustainable’ should be clarified to support responsible investment approaches over long-term time horizons.

#### **Recommendation 1:** The definition of ‘sustainable’ should:

1. make clear that implementing responsible investment strategies is consistent with the purpose of superannuation, and
2. include investment with appropriate long-term time horizons in mind, considering the risks and impacts of sustainability challenges such as climate change, and how superannuation investments can help mitigate those.

## Member expectations of funds

Superannuation fund members increasingly expect their money to be invested in line with their own values, in addition to returning strong financial returns. RIAA's study, [\*From Values to Riches 2022: Charting consumer demand for responsible investing in Australia\*](#) found:

- **High expectations that funds will invest responsibly:** 83% of Australians expect their bank account and their super to be invested responsibly and ethically. For over 80% of the population, this means that their investments deliver a positive impact to the world,
- **Belief that responsible investment performs better:** 64% of Australians agree that responsible and ethical superannuation funds and investments perform better in the long term,
- **Demand for action on climate change:** The vast majority of Australians believe it is important their superannuation fund or bank commits to reducing GHG emissions (84%) and sets targets for emissions reductions (83%). 81% want to see them pledge to achieve net zero by 2050,
- **Interest in investing more to make a difference:** 61% of Australians would be motivated to try to save and invest more money if they knew their savings and investments made a positive difference in the world.

There are significant differences between the views of older and younger superannuation fund members. For example, different generations responded very differently to the question of whether they would be more motivated to try to save more if their savings and investments made a positive difference in the world:

- Gen Z: 83%
- Millennials: 75%
- Gen X: 57%
- Baby Boomers: 39%

We note that some Gen Z fund members today will retire in the 2070s. This time horizon should be considered closely when defining what is 'sustainable'. The goal of net zero GHG emissions by 2050 is one (significant) step along the path towards a sustainable future for younger Australians.

## Alignment with national and international goals

Responsible investment approaches can also support our national and international sustainability goals, in particular, Australia's efforts towards UN Framework on Climate Changes Conventions Paris Agreement commitments, and the Sustainable Development Goals. For example, some funds may invest in line with a net-zero emissions trajectory, or in social outcomes.

In RIAA's view, based on the available science, it will not be possible for Australians to have a 'dignified' retirement if global temperatures exceed the Paris Agreement targets. Therefore, aligning the objective of superannuation with Australia's national objectives and global commitments to combat climate change would be consistent with providing a dignified retirement.

Superannuation funds that are contributing to these broader goals through responsible investment approaches are ultimately contributing to a more sustainable social, environmental and economic future for Australia and for their fund members.

**Recommendation 2:** The legislated objective should align with national and global sustainability goals, including combatting global warming.

### 3. Is the proposed approach to enshrining the objective in legislation appropriate? Are there any alternative ways the objective could be enshrined?

In RIAA's view, the approach proposed in the Consultation Paper covers the most important elements of superannuation, and recognises the critical role of responsible investment.

We do not have any views on alternative ways to achieve the same objective. However, we may comment on the details of any future Exposure Draft amending legislation.

### 4. What are the practical costs and benefits of any alternative accountability mechanisms to the one proposed?

It is important that the legislated objective of superannuation aligns with existing measures aimed at ensuring superannuation funds are accountable to their members. In particular, the Government should consider the current formulation of the YFYS performance test.

In RIAA's view, the proposed legislative objective of superannuation, which requires funds to generate retirement income in a 'sustainable' way, could conflict with the current YFYS performance test for superannuation products.

This is because the indices currently underlying the YFYS performance test do not utilise negative screens or other sustainable investment approaches. For example, the YFYS test's Australian equities index is the ASX/S&P 300, which is heavily weighted towards resources companies and other stocks which may not be considered sustainable investments. Indices like this are not necessarily aligned with Australia's climate and sustainability goals, or with sustainable long-term financial returns.

Two ways that funds can show they are investing responsibly and sustainably are by meeting the requirements of RIAA Responsible Investment Product Certification and the UN Global Compact Controversy (UNGCC) exclusion screens. However, research by the Connexus Institute and London Stock Exchange Group has found that products which met the minimum criteria for RIAA Certification and UNGCC screens face an unstable tracking error against the YFYS performance test benchmark ([Your Future, Your Super Performance Test: Constraint on ESG, Sustainability and Carbon Transition Activities](#), 2022, pages 8-10). This uncertainty – and the prospect of a fund being penalised for failing the YFYS performance test – could deter some funds from robust investment approaches which are geared towards long-term sustainable returns for members.

RIAA looks forward to working with the Government to address these and any other inconsistencies or barriers, to ensure that the objective of superannuation provides clarity and stability for funds and their members' benefit.

**Recommendation 3:** Existing legal obligations for superannuation funds, including the YFYS performance test, should align with the legislated objective.

## About RIAA and our members

RIAA champions responsible investing and a sustainable financial system in Australia and Aotearoa New Zealand, and is dedicated to ensuring capital is aligned with achieving a healthy society, environment, and economy. With more than 500 members managing more than USD29 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across Australia and Aotearoa New Zealand. RIAA's membership includes superannuation funds, KiwiSaver default providers, fund managers, banks, consultants, researchers, brokers, property managers, community trusts, foundations, faith-based groups, financial advisers, financial advisory groups, and others involved in the finance industry, across the full value chain of institutional to retail investors. RIAA represents 58% of all managed funds in Australia.