AMP Wealth Management

Section 1: Your details

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Are you requesting that any of this submission be kept confidential? 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?**

   AMP strongly supports the objective of "enhancing the financial well-being of default members, particularly at retirement", and we believe that this should be the main consideration in design of the default provider arrangements.

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

   AMP supports the criteria for the review. We see better financial outcomes for KiwiSaver default members, trust and confidence in KiwiSaver, low administration and compliance costs, and innovation, competition and value-for-money as inextricably linked, but with the right combination of settings, should advance the interests of members.

   The KiwiSaver market is highly competitive, with a wide range of offerings. The basic design of one account per member and easy transfer of one's account between providers is a key design feature that promotes competition and innovation.

   We would down-weight criterion 4, as any arrangements that supported the development of New Zealand's capital markets at the expense of the other criteria would be detrimental to the objective to enhance the financial well-being of default members at retirement. We see development of New Zealand's capital markets as a positive and inevitable side effect of the inevitable increase, for the foreseeable future, of KiwiSaver funds under management. However, we do not think the interests of members should be compromised in advancing this objective. We would expect to see that in absolute terms the investment in the NZ market should increase in line with the growth of KiwiSaver, but this would be the result of asset allocation decisions and investment outcomes and not through regulatory requirements to set specific NZ market asset allocations.

A similar objective was proposed with the [now defunct] KiwiFund Bill, i.e.: "preferential treatment [be] given to New Zealand based investments". As the FSC noted at that time, Morningstar reports[1] indicated that existing KiwiSaver providers invested approximately 47% of their funds in New Zealand assets compared to the approximately 14% for the NZ Super Fund,[2] a government-owned entity. Increasing the proportion of domestic investment, including in infrastructure, is not necessarily positive for investors. As the NZ Super Fund stated: "A significant proportion of the NZ Super Fund is invested offshore. This strategy is consistent with global best practice. Investing globally gives us diversification and access to investment opportunities that are not available domestically." Legally mandating a bias towards New Zealand investments (especially if narrowly or directed towards sectors such as regional investment) risks: a) increasing market risk/market concentration risk, b) distorting the market by artificially inflating NZ asset values, and c) potentially increases illiquidity in KiwiSaver funds (e.g. if a NZ infrastructure minimum was mandated).

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

AMP agrees that a move away from a "parking space" purpose is justified. Our over-a-decade experience interacting with our default members tells us that many feel they have "done the job" in relation to KiwiSaver *just by joining*. Part of the challenge in engaging default members is getting beyond this mindset and helping them to realise they have *two other* jobs: (1) to contribute and (2) to choose a suitable fund, which, more often than not, isn't their default fund. Given default members not choosing an appropriate fund is now well-proven behaviour, AMP supports moving to a 'life-stages' approach so that members are automatically allocated a fund more likely to be appropriate for them given their expected investment horizon.

We note that a one-off switch into expensive markets (from a conservative mandate to a more graduated lifesteps approach) carries risk, especially for high member balances. Timing could make a significant difference to investor outcomes. It would be worth considering how the transition could be incremented, for example with default fund slowly getting more aggressive over time to lower investment risk and market impact.

4. **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?**

AMP's view is that the investment mandate and other regulations should apply to the fund or funds into which default members are placed when they arrive with their provider. Any member who selects that fund/s should be treated the same way – same investment mandate, same fees.

The default fund may suit a range of members and they should be able to choose to stay in it or to join it if that suits them at the fee level of the fund.

Members who have actively chosen the existing default funds as best for them should not be affected by any changes – they should stay in their low risk, low cost choice.

We do see an issue with "stranding" for members who have not made a choice if the investment mandate for the default funds changes. Our view is that existing default members

[1] https://www.morningstar.com.au/s/documents/KiwiSaver_Survey_Q4_2017_Final.pdf
[2] https://www.nzsuperfund.co.nz/sites/default/files/documents-sys/NZSF%20Annual%20Report%202017.pdf

who have never made an active choice to be in the default fund should be moved to a fund that has the new investment mandate. For example, for AMP, we would move existing non-active choice Default Fund members into AMP Lifesteps, so that the probable benefits from an age-appropriate fund, in the same way that new default members would. If this was not required, the current default members who have not made a choice would be “stranded” in the old conservative mandate funds and lose out on the benefits of the new default mandate. Members should of course be advised of this change and, as always, have the option to make a different choice and opt out.

We suggest that a government campaign around any changes would be an excellent idea, as it would create awareness for providers to capitalise on in their member education conversations around any such changes. A government campaign informing KiwiSavers in default funds to expect improvements would also support trust in KiwiSaver overall and help members have context for the changes.

5. **If a life-stages option is adopted, what “stages” should apply and to which age groups? Should there be a “nursery” period?**

AMP does not support a nursery period as it introduces complexity without any good reason.

By and large default members are young. They start with small/zero balances. If they are planning to use KiwiSaver to buy a first home and wish to have a more conservative approach than the life-stages default, a nursery period of six months in which their balance is commonly negligible will make almost no difference to their outcomes, be it the amount available for a first home deposit or their eventual retirement funds.

Further, for most young default customers, the time when they might use their balance as a first home deposit is commonly 5-15 years after they join KiwiSaver, so a more growth-focussed approach is appropriate for such members. Providers should be using this time to engage members around the topic of their first home and how this might affect their investment choices.

We suggest that real-world behaviour should influence the decision on stages and age groups, and that age 65 should not be considered the end of the average investment period. MBIE should find or commission research on the actual age at which people are likely to start using their KiwiSaver (often older than 65), and also take into account that most people will live for many years past 65. Targeting 65 as the end period for the investment and basing the life-stages on that assumption would imply a more conservative life-stages approach and be counter to improving financial outcomes for members in retirement. We note also that the recent projections formula assumes a life expectancy of 90, which means people at 65 still have a 25-year investment horizon.

AMP is currently reviewing its Lifesteps approach to take into account observed real-world behaviour of our clients and their projected longevity.

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

AMP’s current view on balanced is a target of 57% growth and 43% income Assets . The range would need to be determined in conjunction with the Default review. The FMA has issued its

Guidance note on risk indicators and description of managed funds[3], which provides guidance for growth asset ranges for balanced funds "generally representing 35% to 63%".

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

   AMP's current view on Growth is a target of 77% Growth and 23% income assets. The range would need to be determined in conjunction with the Default review.

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

   AMP's current view on Conservative is a target of 24% Growth and 76% income. The range would need to be determined in conjunction with the Default Panel.

9. **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 our comment under question 5 on first home buyers. Providers have a responsibility to communicate with all members and help them make appropriate decisions. This is especially the case for younger members who might have a first home in their future.

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

    For providers that don't operate life-stages it would require investment in development because it requires automated systems within the provider's registry/administrative systems. The cost would need to be factored by each provider.

    AMP has existing life-stages capability and the administrative cost will largely depend on whether it is simply a change to the Default fund in terms of income and growth levels or a fully prescribed life-stage solution that adjusts the members allocation to growth and income over the time to retirement and/or target retirement age in specified age bands.

    For AMP members in Lifesteps funds, the administration cost is the same as being in an active choice fund. However, if life-stages became the default, AMP would need to determine the costs (administration and investment management) as part of tender process. This is likely to be higher than the current Administration cost of 0.15% for the current Default fund. (Refer question 14 for the rationale.)

11. **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?**

    AMP strongly supports a life-stages mandate for default funds as it would increase the likelihood of the greatest net benefit for default members generally. It also fits best with the "opt out" design of KiwiSaver – that is, the generic design is what is likely to be in most default members' best interest, however, members can opt out if they have a different view.

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[3] http://www.fma.govt.nz/assets/Guidance/151124-Guidance-note-on-risk-indicators-and-description-of-managed-funds.pdf

12. **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?**

Fees need to cover investment management costs, provider administration costs, the costs of serving and educating members and a margin for providers. AMP's view is that all providers need to continue to work on member education and servicing, and that where this is working well and fees are fair, members are getting good value for their fees overall.

Specifically, AMP's KiwiSaver Default Fund fees are one of the lowest in the market with total fund charges of 0.34%[4]. Such low fees are only feasible, however, for a simply structured lower underlying cost fund. As noted in #10 and #14, this likely would need to be higher for a life-stages approach.

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

Fair fees that cover providers' costs are necessary for the operation of schemes. Given that all members create costs , we do not believe some members should not be charged fees. If public policy considerations favour lower income members or under 18s having low/no fees, a means of achieving that could be re-introducing the *annual fee subsidy* (which in the early days of KiwiSaver was a government benefit that subsidised members' fees up to $40 p.a.) in a targeted manner.

14. **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?**

Considerations in setting fees

The cost of funds management can be minimised in two ways: through passive management, and by holding higher proportions of cash and other low-cost conservative assets.

The relative value of active versus passive management can be debated. However, AMP's view is that default fees should not be set at such a level that entirely passive management is the only viable option for all default providers. Low cost passive providers should not be considered a fair benchmark for the default market as a whole. In particular, we note that low cost passive management could conflict with the desire to develop New Zealand capital markets as it leaves little leeway for investment in alternative asset classes, which tend to be more expensive.

We further note that tax efficiency can be an important factor that affects returns to members but does not show up in total fund charges. Most managers buy shares and hold them locally in NZ PIEs they can then get a rebate for foreign tax paid (foreign tax credits). AMP's analysis indicates this adds about 30bps to the returns of the global equity component of our fund. Some low cost passive providers buy exchange traded funds in Australia and forego this

[4] https://www.amp.co.nz/content/dam/ampnz/documents/kiwsaver/quarterly-fund-updates/default-fund/AMP-KiwiSaver-QFU-DefaultFund-2019-June.pdf; NB: the Discussion Paper, page 19 (Table 1), illustrates AMP's comparatively very low fees. Furthermore, for members with balances over $26,000, AMP's fees are the lowest in the default market.

tax efficiency. This reduces their total fund charges, but the tax inefficiency with a c.30bps return impact is not visible to members.

Default funds under the current settings are conservative (and therefore lower cost) in their mandates, and most have a heavy passive component to their management. Even under this scenario, current default pricing provides a very slim margin. A change in mandate to balanced, growth or life-stages will increase underlying fund management costs as the cost of management for riskier asset classes is usually higher. This change in underlying costs should be reflected in the fees, with the fees for a default fund with a non-conservative mandate being higher than current default fees.

Methods and models to set fees

Regarding fees, the public policy imperatives are to balance:

- fair costs to default customers
- value for money/service
- a sustainable market (that is, fees are allowed to be set at a level where a range of providers can make a margin, maintaining competition and efficiencies over the long term)
- equal outcomes for default customers (that is, default members paying roughly same amount whichever provider they are with)

To balance these outcomes, we suggest a five-step procurement process as follows:

1. Call for bids including fees

2. Panel assesses bids for service and non-fee criteria. There is a yes/no gate based on quality.

3. Assess the range of the fees offered by bids that pass the quality gate. Using this information, select an appropriate cap for fees (e.g. median fee bid, or the 66th percentile fee bid)

4. Release the new fee cap to all bidders who met quality criteria and call for new bids

5. Appoint all re-bids that meet quality criteria and new fee cap.

The benefit of this process is that it gathers some market information about a sustainable level for fees through the initial process. Most re-bids will come in at the new cap, which means some providers will earn more than the minimum they could have from their default product. However, overall, members will receive the default service at a reasonable price which the market has indicated is sustainable.

Fixed and percentage fees

There is a need to have both fixed and percentage fees. With the average balance of KiwiSaver at around $20,000 and Default balances at a much lower level, the fixed fee is an important element to cover costs and create a sustainable offering. Over time the percentage fees will have a larger impact in terms of the amount deducted. In mature retirement markets the set fee component has reduced over time as has the percentage fees as result of increasing

FUM/economies of scale. This will be for each provider to consider as part of periodic reviews of fees and is in keeping with current review process.

15. **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?**

    See question 14.

16. **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?**

    Competition in the KiwiSaver market is strong, with new entrants and incumbents offering different approaches and marketing their various points of difference to consumers.

    Default providers are part of the general market and need to compete well to retain default and active choice members.

17. **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?**

    AMP supports a regime with clear quality criteria (e.g. around stability, capability, service, education and advice) and a clear fee cap for default funds, as explained in #15. Under these conditions, we believe any provider that meets prescribed criteria should be eligible to become a default provider.

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

    We would support providers being able to join the default provider group any time if they meet the requirements.

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

    AMP's view is that "responsible investing" is a very broad term and the answer to this question would vary depending on how exactly how it was interpreted. Specific impact investments will come with a higher management cost, but overall, investing responsibly should have similar costs and returns to "standard" investment practices.

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

    See question 19.

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

AMP believes that standardised reporting on responsible investment policies would provide a benefit in encouraging thoughtful and customer-focussed policies. Responsible investment is contextual, and the landscape can change quickly. An example is the change of sentiment towards civilian weapons after the events in Christchurch. While we strongly support responsible investing, we believe it would be inappropriate and impractical for the government to mandate specific policies and keep these relevant and broad-based.

22. **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?**

AMP believes most customers want more responsible investment, but research would be required to determine at what point their view changes if the settings would materially reduce their returns.

23. **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?**

Default members and all other members should be able to easily compare responsible investment policies through standardised reporting.

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

AMP has no specific view on this.

25. **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?**

We do not support government mandated RI policies.

26. **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?**

Standardised reporting should include at least:

- Exclusions (sectors and companies)
- Impact investments (sectors and companies)
- Accreditations
- Full statement of the policy
- Policy on engagement and voting record

27. **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?**

See question 19 and 20.

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?**

Changing the investment mandate to a life-stages approach will inherently shift the investment profile from cash/bonds to other asset classes and should help develop NZ capital markets. All other options create distortionary interference with investment decisions, asset allocation and the operation of the market, to the potential detriment of retirement outcomes for default members.

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?**

See question 28.

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?**

See question 28.

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

See question 28.

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 question 28.

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)?**

See question 28.

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?**

Both options are admirable goals but also both feel challenging. Ideally the early stage market would slowly build up and become professional and easily investable by having high quality well-diversified managers running funds. Such funds would be naturally desirable to invest in by KiwiSaver funds with appropriate risk mandates. Given this, the status quo of no specific requirement on KiwiSaver default providers in regard to New Zealand capital markets is the best option.

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?**

AMP believes that the FMCA regime provides rigorous protections for investors, including for default KiwiSaver members. Given this, we do not see the need to transfer customers from default providers who lose their status if this loss of provider status is due to a government desire to reduce provider numbers.

However, if all providers who meet the quality and fee requirements are appointed, as we support, we agree that members should not be left with providers who do not meet the quality or cost provisions for the default fund. We note that, provided these requirements are reasonable, we would not anticipate existing providers losing their default status unless they choose not to bid.

If a need to move members eventuates, there will be significant costs associated with moving members, including liquidating the underlying funds and the transfer of data to new providers.

Under no circumstances would AMP support transferring any customer who has made an active choice to be in a default fund with their current provider. These customers have made a choice with their provider, and that should be respected.

We note that the transfer of members between providers without consent would probably erode trust in KiwiSaver and promote the view that the government has control of members' individual KiwiSaver accounts.

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

AMP does not support this action as we do not see the benefit for members.

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?**

The government should undertake to contact all affected default members and provide an easy way to opt out of moving, e.g. by texting "no" to a dedicated text number. These members should then be removed from the government's reallocation process.

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?**

Reallocating members involves unnecessary costs and causes confusion for members. We believe it should be avoided. If it is deemed necessary, the government should manage the logistics, including the informing and opt-out process. The complexity of managing this among multiple providers would have the potential to create confusion and inefficiencies and erode trust.

Under option three, providers who are not re-appointed could be required to comply with the same standard as default funds yet retain their members. This would minimise costs, disruption to markets and confusion for members. New default providers would still have the incentive of gaining new members.

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

If a transition were to occur, transition costs such as transaction costs and out of market exposure (and who incurs these transition costs) would need to be considered. It would require potentially significant funds to be liquidated and, depending on scope, could also impact liquidity and pricing in some asset classes, such as New Zealand equities (if this formed a substantive part of the asset allocation).

Transitioning members in tranches could mitigate this, however would need to be weighed up against members receiving different outcomes due to timing difference of assets being liquidated and invested. From a transitioning member perspective it would probably be most effective to execute on a target date but that would need to be weighed up carefully with the interests of non-transitioning members, to ensure they do not share in any costs created by the transition.

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?**

Active default members have made a choice regarding a) their risk level and b) to stay with their provider. AMP's view is that there is no justification for cutting across their decisions and that they should be active members of the scheme they are currently with. We believe moving these members would reduce trust in KiwiSaver as it would create a scenario where government had over-ruled individual member choice.

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?**

Member engagement is important and should be measured by outcomes, e.g.:

- number of members who have actively engaged with the provider to understand their fund
- number of members making contributions or more than the minimum contribution
- number of members on the correct tax rate
- provider NPS (or other satisfaction rating system)
- number and responses to member communications
- tools and guidance available and used.

Providers' member engagement programmes should be assessed as part of the tender process and measured by KPIs that reflect real outcomes for members.

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

AMP has no specific view on this.

43. **Any other feedback?**

We feel that it should be acknowledged that many default investors are not engaged and have proven challenging to switch. They should, however, be prudently looked after by providing a default option suitable for retirement savings. This would be in the form of a higher/risk return investment (as outlined in the discussion paper). This would likely greatly outweigh the sum of all other initiatives and getting this right should be the main aim of the review.

AMP's view is that the government should take more responsibility for establishing contact with default members. As a provider we use phone, email and postal contacts to get to our default members when they first arrive and as they continue with us. However, we do not always receive adequate or accurate contact details from IRD. Further, members who have not responded to our communications or who are "gone no address" are very hard for us to reach. Government has several ways of reaching people with up to date contact details and could deploy things such as myIR or other government communication channels to encourage default members to contact their providers or, indeed, to actively direct members to their provider's website. Once contact is established providers are able and willing to service, educate, and help their members.