Submission template: Review of KiwiSaver default provider arrangements

Rob W M Dowler

Section 1: Your details

Name of contact person: Rob Dowler

Organisation (if applicable): Red Owl Consulting Ltd

Contact email address:

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

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: My only request for confidentiality is in respect of my contact e-mail, to reduce the risks of it being harvested for use by spammers and scammers. No other part of the submission is required to be held confidential and may be made publicly available in full.

Section 2: Feedback on discussion paper

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

   No submission

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

   It is correct to state that default members have not chosen to be in the default fund, but only at commencement of membership. Thereafter, this statement is incorrect, whether the member's decision to remain in the default fund after commencement of membership is a conscious or an unconscious choice.

   It is an inappropriate criterion to consider whether default funds should support the development of New Zealand's capital markets.

   New Zealand capital markets should stand on their own merits when default funds determine the extent to which to invest within the allowable parameters, in the same way that default funds consider any other prospective investment.

   The design of KiwiSaver should be focused upon giving priority to the investors in the scheme, not to other objectives, such as developing capital markets. Giving such priority to investors in considering scheme design is then directly in line with the policy objectives of the recent review of financial advice services whereby those providing such services are required under the legislation soon to come into force to give priority to the interests of the client.

It would be somewhat ironic if those providing advice and meeting the requirement to give priority to the interests of their clients were thereby required to recommend against investment in KiwiSaver because the design of KiwiSaver was instead focused on the priority of developing capital markets, or some other equally arcane objective, instead of giving priority to the interests of investors in KiwiSaver.

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

If, as many commentators state, the parking space in the default fund is seen as a problem, why is the money being directed to such default funds in the first place? If someone thinks that they know what the "right" answer is, why isn't that made the default option for new members, albeit noting that the "right" answer doesn't necessarily have to be the same for each new member.

Oops, doesn't that mean that someone, either a member, fund manager or an adviser, might have to assess what the best answer is for each new member?

Perhaps those default members that don't make an active decision to stay or change simply reflect the fact that, first, they are default members with everything that this implies about how proactive they are about KiwiSaver and, secondly, that they might simply be happy knowing that they are in the lower fee alternatives getting the benefit of employer and government contributions that they would not otherwise receive and they consider that is enough of a benefit without going to the bother of having to consider alternatives, even when others think that a better result might be achieved via a change.

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?**

A default fund is a default fund, so keep it simple, with its provisions applying equally to everyone in it, whether they are there by active or passive choice.

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

How do you balance an aggressive growth life stage investment fund for young KiwiSavers against the option that many have to withdraw at any time to apply the benefits of KiwiSaver to a first home purchase? I do not see these two scenarios as being compatible or able to be resolved.

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

It really doesn't matter, because the individual member can go elsewhere if the mandate doesn't work for them.

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

It really doesn't matter, because the individual member can go elsewhere if the mandate doesn't work for them.

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

It really doesn't matter, because the individual member can go elsewhere if the mandate doesn't work for them.

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?**

As noted above, I don't believe it to be possible to mitigate these potential issues but I await other submissions on this point with interest to see if anyone else has come up with a valid answer.

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

No submission

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?**

To the extent that the long-term benefits of being in a higher-growth fund are believed to be supreme, one can then question why KiwiSaver default funds are allowed to offer anything other than higher-growth funds. If all default funds were higher-growth funds, that would at the very least remove the constantly expressed criticism that KiwiSaver investors are missing out on maximising their returns.

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?**

No submission

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

Of course it is a problem, in the sense that those with less money will always be disadvantaged, which I regard as a natural outcome.

To the extent that this is regarded as a problem that needs to be fixed, which is questionable, the solution is for someone else to pay the fee, which probably means the government.

That is, if the inequity that naturally arises from those with wealth or higher incomes being able to contribute and take advantage of the benefits at a greater level than those with less wealth or lower income, then tax the wealthy and higher income individuals and redistribute the tax received to those with less wealth and lower incomes.

Wait a minute – That is pretty much what NZ Superannuation does in a very equitable manner, even after accounting for its universal nature.

Of course, the other alternative is to simply remove the vehicle that produces the inequity, which means wind up KiwiSaver.

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?**

    No submission

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?**

    No submission

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?**

    No submission

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?**

    No submission

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

    No submission

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

    No submission

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

No submission

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

No, because there are options that KiwiSavers can transfer to, if responsible investing is an area of interest to them.

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?**

If they do, they can transfer.

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?**

If an investor is concerned about the lack of information, they can transfer to another fund that provides what they want.

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

I have no idea, and I doubt that anyone else does either.

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?**

I await with interest the complete range of exclusions that other submissions will suggest, probably to the point that there will be no options left to invest in, if all of the suggestions that I expect to be made, are adopted.

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?**

No submission

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?**

No submission

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?**

First, note my opposition to amending the settings for KiwiSaver default providers to support the development of NZ capital markets. My submission under this question consists of extracts from submissions made to the Capital Markets 2029 review, identifying limitations or problems existing in relation to NZ capital markets.

Focusing first on NZX as a key part of NZ capital markets, I submitted as follows:

Barriers to NZX delivering to its key purposes:

- *Small number of brokers/sponsors – costs and risks of being one*
- *The range of competing platforms or opportunities available to entities to raise capital.*
- *Direct and indirect costs of listing and remaining listed*
- *Risks of listed entities getting things wrong with resulting costs*
- *Investor access to the trading platform is limited, principally via an NZX Firm*

Then I commented on the place of retirement savings policies in relation to capital markets as follows:

The concept of introducing mandated, compulsory or incentivised retirement savings policies, justified on the grounds of providing support to capital markets (among other reasons) consistently raises its head from time to time, unsurprisingly from those, such as fund managers, most likely to benefit from such policies.

Note my opposition to such policies, particularly those involving individual accounts such as is applicable in KiwiSaver, being justified on such grounds as supporting capital markets. My view, held strongly, is that capital markets should stand or fall on their own merits and that individuals should have freedom as to whether, how and how much to support capital markets, be it by direct or indirect investment.

Further, if it is felt to be in the national interest that government develop policies to support capital markets (and I certainly think that it is), to the extent that it is determined that this should involve some form of direct or indirect investment, then let government be transparent in what the objectives are, and how government intends to use its own tax-payer funding to support those objectives, always then subject to review by the electorate. I believe that the establishment of the NZ Venture Investment Fund and Callaghan Innovation are examples.

Then I commented on the regulatory environment as follows:

I do have a concern that the constant regulatory creep that is occurring, designed to better protect consumers and investors, is resulting in significant barriers to development of formal capital markets. These very barriers have the perverse effect of potentially encouraging individuals to engage in a range of activities that expose them to scams, as they seek to take up options or opportunities that seem easier to complete, many based overseas and accessible online.

Further, the regulatory changes relating to financial institutions and particularly advice services proposed or being put in place again are at risk of limiting access to legitimate *support, increasing risks that consumers take up what appear to be easier opportunities without support that result in inappropriate outcomes. I have always held the view that regulation should never preclude consumers from being able to access support or advice that they might reasonably expect to be available to them. I remain to be convinced that the current and proposed settings will meet this objective.*

I do not have an obvious answer to this conundrum, but we need to consider how to provide access to innovative developments to support capital markets. To that end, it is encouraging to see NZ leading the way in introducing regulated peer to peer lending and crowd funding platforms. Then, as outlined in my brief notes at the start, consideration might be given as to how to facilitate secondary market trading of the financial products and securities arising through such platforms.

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?**

They should not be used to develop NZ capital markets.

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?**

Default funds should not be required by law to take an active role in helping develop the NZ capital markets. Once made, the contributions belong to the member, and government should not therefore introduce compulsory requirements or objectives as arcane as supporting the NZ capital markets.

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

No submission

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?**

No submission

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)?**

Again, I oppose government dictating in such a way where monies belonging to members should be invested.

KiwiSaver is meant to be about building financial capacity in retirement, not delivering to social engineering objectives, or any other arcane policy objectives that someone might dream up.

If the managers of KiwiSaver schemes are currently making appropriate decisions for the investment of members' funds, it is clearly wrong for the government to direct them to do anything else.

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?**

There are lots of better options than involving KiwiSaver default funds. I refer you to the Capital Markets 2029 review.

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?**

No submission

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

No submission

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?**

No submission

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?**

No submission

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

No submission

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?**

This question provides the opportunity to highlight a much larger problem with the default fund system. This review has the opportunity to address this issue, thereby improving the design of the KiwiSaver regime in total, not just for default funds.

First, as I understand from a family member who is an "active default" member of a default scheme, he advises that there is no option to switch to another default scheme. Hence, if he decides that the default provider that he is with is no longer delivering to his objectives, the only choice he has is to switch to another KiwiSaver fund that is not a default fund, thereby losing the benefits that he has actively chosen to receive by staying in his default fund.

It seems fundamentally wrong to preclude transfer from one default fund to another. Further, why should KiwiSaver members of non-default funds be precluded from switching into a default fund? Where is the harm that is being addressed by precluding both of these actions? If KiwiSaver members could switch as outlined, wouldn't this enhance competition and keep pressure on the fee levels of the non-default funds?

I strongly submit that consideration be given to investigating the benefits of allowing switches between and into KiwiSaver default funds that I am suggesting be permitted, with a view to amending the provisions to allow for this.

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?**

No submission

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

No submission

43. **Any other feedback?**

No submission