Exorbitant super fees must end

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FANCY earning $20,000 for a couple of hours' work? Most readers easily could. There is a strong chance that you are unwittingly (and probably foolishly) paying exorbitant fees to teams of highly paid fund managers to look after your superannuation, dramatically sapping your ultimate balance in the process.

Basic economics says it is extraordinarily difficult for fund managers to get a better return than the market they are trying to beat, and it becomes even harder when they charge royally for the privilege of trying.

About three-quarters of all Australian equity fund managers did worse than the benchmark ASX 200 index over the past year, for instance. More than 90 per cent of fixed-interest fund managers did worse over a five-year period.

This is mainly why fees are high at Australian super funds and why many people are fleeing the "managed" sector to set up their own self-managed funds where typical costs are lower.

The super industry, largely underpinned by banks, extracted about $17 billion in fees from people's savings last year, equivalent to about 1.2 per cent of the total $1.4 trillion pool.

The bulk of those fees are investment management fees, which are close to zero for passive or index fund management.

Yet only 16 per cent of super savings in Australia track an index, far less than in the US and Britain, for instance, which do not have a compulsory retirement saving scheme like Australia's.

For an average account of $25,000, reducing the annual fee by one percentage point over a 35-year working life saves about $20,000 in today's dollars -- unless one strikes it lucky with a particularly prescient fund manager.

Since 2005, Australians have been free to switch their super savings into low-cost funds that track indices and thereby save many thousands of dollars.

But few have. Most pay scant attention to their future income as people naturally discount the future heavily.

It is not satisfactory for politicians in these circumstances to argue that people are free to optimise their super settings: nobody asked for 9 per cent of their wages to be siphoned off and gouged in the first place.

In the absence of the super system, people would save in different ways for their retirement: more in their home, for instance, and less in financial assets such as shares. In any event, they certainly would have paid vastly less in fees.

The government's MySuper regime begins next July, giving tacit recognition that existing fees are far too high.

The new regime will force basic super funds to be simpler and more transparent, but it will put little downward pressure on fees; it will introduce no hard limits.

The super industry will remain immune from normal competitive pressures because it will continue to lack price competition.

The compulsory nature of super makes it very difficult to introduce prices, but the government could try by making it illegal for funds to take fees of any sort from their members' accounts or their earnings.

Super funds would then have to charge members directly out of their after-tax current income, in the same way that private health insurers collect their premiums or gyms collect their membership fees.

People would surely choke on the massive funds management bills, prompting massive efficiencies in the industry.

Fees would tumble as fund managers shifted to passive management.

Only the small minority of superannuants with keen interest in investing would make use of "active" fund managers.

Government could also crack down on super funds that charge fees as a percentage of assets. It is a mystery why it costs funds twice as much to manage $100 million as $50m.

It is shameful that the supposed party of the ordinary worker, the Labor Party, and the so-called party of small government, the Liberal Party, not only endorse the existing framework, but they are in agreement to increase by one-third the torrent of money flowing out of workers' pockets in fees.

The Superannuation Guarantee will rise by a third to 12 per cent over the coming decade, despite the Henry tax review's explicit recommendation in 2010 not to increase it.

Both sides of politics appear to be beholden to the financial services industry, which profits enormously from the existing arrangement.

A large and profitable financial services sector is a good thing but not when it arises unfairly from the earnings of ordinary people.