

INTRODUCTION TO FIRST DOLLAR™

First Dollar Software P/L has provided investment performance measurement solutions to retail and professional clients in Australia for five years as exclusive licensee of First Dollar™.

First Dollar™ has developed and markets a free downloadable application for retail investors which allows them to measure and monitor portfolios of investments. This provides individuals with the opportunity to compare their performance on a like-for-like basis with the market or professional funds or other investors.

Our performance measurement solutions were developed over a period of 20 years initially to address at an individual level the problem of longevity that plagues all developed economies' pension or superannuation systems - ie if or when the money would run out. We recognise the importance of investment performance to the maintenance of living standards through the decumulation phase of individuals' superannuation entitlements. Research suggests that on average approximately 2/3 of the total amounts paid out to beneficiaries from retirement funds is earned in capital and income accrued after the date of retirement. The importance of ongoing investment performance to the maintenance of living standards is therefore crucial.

We think there is an opportunity to put applications into the hands of retail investors of all kinds, including the 11.6 million superannuation fund beneficiaries, which allow them to measure and monitor the performance of their investment portfolios of all kinds through simple interfaces providing greater transparency and consistency than the current industry practice.

First Dollar Software management have worked in global funds management, and we provide ongoing performance measurement in Australia for Huntleys' portfolios and Morningstar Australasia P/L. We have hundreds of members and the First Dollar™ application has been downloaded thousands of times. We have experience of working directly and indirectly with retail investors and individuals who are looking after their family's long-term financial interests through their investments. Some of First Dollar's members' comments are included in the conclusion to this response.

We invite Committee members to visit our public website at www.firstdollar.com.au where more background and detail about this application is available, and if they have the time perhaps even to download and use First Dollar™ for themselves using the real life Samples provided.

First Dollar™ is currently free for retail users, potentially offering a costless improvement to existing industry processes. We will argue that third party applications have the potential to add value to all beneficiaries of the Australian Superannuation System.

LIMITATIONS OF EXISTING PROCESSES AND BENEFITS OF A NEW APPROACH

We identified some time ago the limitations of the existing static paper snapshots of investment portfolios which present a variety of information based on discrete dates (ref. the 31% of members who admit that their member statements are difficult or worse to understand). First Dollar™ evolved to provide investors of all kinds with a continuous moving picture of their investment portfolio. The benefits of this continuous approach include:

1. A User/Superannuant may select their own dates to review the performance of their investments/superannuation. Users do not have to rely on their adviser/fund to select dates for them, or on the somewhat arbitrary calendar dates determining the current reporting cycles.
2. Superannuation Fund Members ("Members") may compare their superannuation with other investments including their own and other portfolios and funds through a single lens and a simple interface with consistent output formats.
3. The ability to include or exclude the impact of Commissions, Tax, Management Fees or particular investment fund or asset allocation choices creates like-for-like comparisons that nevertheless capture each individual's different personal financial circumstances. These comparisons allow individuals to better assess whether their advisers and their funds are meeting their current needs and expectations or are likely to in the future, and whether the costs of implementing the choices made are justified by the benefits to be gained.

By creating impediments to Members comparing one investment option with another, existing superannuation and investment platforms create barriers to exit which allow them to continue to charge fees and other charges

which are not otherwise justified by the value that is delivered to the end user or Member.

We aim to extend a culture of performance measurement throughout the funds management industry, and that First Dollar™ and other third party applications which independently assess the performance of investment portfolios will be a helpful addition to the current industry model.

OUR RESPONSE TO THE ISSUES PAPER – OPERATIONS AND EFFICIENCY

There are a number of different questions in the Second Issues paper that we will address directly in our response, although our response is wide ranging and does not fit neatly into one section of the Issues paper. Our objectives in this response are to

- 1 Argue the merits of encouraging third party applications to help Members improve their understanding of the dynamics of their investment and superannuation performance
- 2 Demonstrate how such applications may help to break down barriers preventing individuals from understanding the impact of their investment choices on their superannuation outcomes
- 3 Encourage the Super System Review Committee to consider mandating measures to ensure that Financial Service Providers (FSPs) provide their Members with access to their core transaction information and enable third party applications to provide independent market driven solutions which assist Members to make more informed choices about their superannuation and investments.

First Dollar™ has already developed and markets a series of standardised portfolio measures for individuals and beneficiaries of self managed super funds (SMSFs) and other investment portfolios. Similar solutions could immediately be available for all customers of FSPs, in particular for the millions of Superannuation Fund Members. We think that a key mechanism to improve efficiency in the Superannuation System is through comparability between portfolios of different sizes, of different composition and subject to different regulatory and taxation requirements.

We have a commercial interest in promoting First Dollar™. We are unaware of any other application on the Australian or any other developed market which tries to achieve the objective of transferring control over the investment portfolio measurement process to the end user. There may be many different ways to provide applications to Members to improve their control over their investment outcomes. We would welcome the potential competition that will appear if an independent market can be successfully developed in third party applications which provide investment performance measurement.

Our response to the second Issues Paper addresses the broad topics of:

Transparency – Members should be able to directly analyse the transactions they have undertaken or which have been undertaken on their behalf

Consistency & Comparability – Different Members of different superannuation funds should be able to review their outcomes consistently and to compare their performance on a like-for-like basis

Accessibility – Solutions responding to market needs should be readily available automatically to everyone who wants to use them, not just those solutions authorised or recommended by their particular FSP

Improved financial education - Independent third party solutions developed in response to market demands will address unmet needs for information in forms that members understand and want

Market solutions – An “open source” approach will ensure that incremental improvements emerge to embed a culture of continuous improvement in the provision of performance measurement information to members. Improving investment performance measurement will improve financial outcomes.

Giving power to members to understand the dynamics of their own investment performance and the outcomes that they may expect will necessarily reduce ambiguity and increase accountability through transparency and comparability.

There is an opportunity to create a culture of continuous performance measurement throughout the industry, driven by the retail investor and Superannuation Fund Members who will expect daily performance measurement on demand. Similar tools could be available for trustees of superannuation funds and for beneficiaries and the diverse holders of managed funds and superannuation funds based on varying degrees of access to the detail of underlying transactions. These tools could use clearly defined parameters as the Committee has suggested in its Issues Paper in relation to the naming conventions of different types of fees and charges.

It is astonishing that trustees of large superannuation funds and other investment vehicles have not yet insisted on these sorts of tools to allow them to dig deeper into the performance of their investments and their outsourced investment managers in a way that gives them control over the reported outcomes rather than relying on the manager and/or other third parties to provide this information in a heterogeneous form.

BENEFITS OF THIRD PARTY APPLICATIONS BASED ON UNDERLYING TRANSACTIONS

We think that the best interests of members may be served by giving individuals access to a level of detail about their transactions and the transactions that are undertaken on their behalf which is currently not universally available. Transaction based third party applications can address the inadequacies of the static snapshots of investment portfolios including those provided for the millions of superannuation accounts. We have noted the unwillingness of existing service providers to provide information that can be relied on to reflect the entirety of the investment experience rather than a series of discrete pictures.

First Dollar™ measures investment performance on a pre and post commission basis, pre and post management fees, pre and post tax and we calculate for our users measures of the cost of different asset allocation decisions made by the investor or on their behalf by their advisers and funds. The First Dollar User Guide (available online) describes in detail how these are calculated.

By providing standardised results which reflect the actual cost to an investor of the particular investment decisions that they or their advisers make, investors of all kinds including the 11.6 million super beneficiaries are able to compare and contrast their investment experience at the hands of their advisers with the experience of other individuals and of the average and median investor or super fund beneficiary.

Each investor's particular investment experience will be different. Even where a deliberate attempt is made to maintain an identical portfolio, it can be difficult to maintain the necessary close nexus between two differently constituted income streams and investment options. These different experiences, and the reasons behind them need to be communicated clearly and effectively to all Members.

INCREASED ENGAGEMENT BY INDIVIDUALS WITH THEIR SUPERANNUATION OUTCOMES

By giving retail investors and superannuation fund beneficiaries the tools to become as well if not better acquainted than their advisers with the detailed ups and downs of their own investment performance and financial returns, the playing field will be a little bit more even. In an ideal world, Financial Advisers would be required to provide to new clients details of all their existing clients' previous investment performance and financial returns on a global and individual basis. This would allow an adviser to demonstrate that it has delivered to existing clients the sorts of investment outcomes that it says it will be providing to the prospective new client.

The availability of tools and applications which encourage retail investors or superannuation beneficiaries to be as involved as they choose with their own investment performance and financial returns could contribute towards a dramatic improvement in their understanding of their overall financial situation and the delivery of their investment outcomes, thus raising the general level financial education over time.

We also think that it is likely that as standardised applications are developed and become more widely used, one of the important issues identified by the Committee - the problem of lost accounts – could be substantially improved. This improvement could come from providing members with an opportunity to identify themselves and their lost super through easy online (one click) consolidation options which eliminate a time-consuming process which has not proved to be easy enough for individuals to identify their lost super accounts in greater numbers. We think that application providers could supply a mechanism for individuals to take immediate easy steps to consolidate their lost accounts with their active accounts in order to improve their understanding of their overall situation. This would have the collateral benefit of reducing the number of orphaned lost accounts as well as potentially ensuring that a beneficiary may reduce the overall level of fees being paid across all their accounts.

WHY ISOLATING THE COMPONENTS OF INVESTMENT PERFORMANCE AND FINANCIAL RETURNS MATTERS

The detailed mathematics behind the calculation of investment performance and financial returns starts from the internal rate of return of a series of transactions in shares or funds or other investment instruments. These raw returns are then altered by dividends and distributions, bonus issues and other structural changes which are reduced to a stream of cash flows (or potential cash flows) valued daily which ultimately lead to a financial return to the superannuation beneficiary.

Individual contributors to the same large superannuation fund will have slightly or substantially different experiences in terms of their long-term financial returns.

For instance, if a Member invested substantial additional voluntary contributions in the period leading up to 30 June 2007 into a Super account (whether an Industry fund, a Retail fund through a Superannuation platform or an SMSF) – not merely an academic issue based on the results of the SMSF review released last week by the Review Committee – then the relative performance of the financial returns across their entire invested funds vis-a-vis the performance of the superannuation funds into which their money was invested would be substantially impaired due to the relatively poor performance of most funds since mid-2007. Looking at the five-year returns for the individual investment fund vs the five-year returns for the individual investor in an individual investment fund choice, the individual investor would have substantially underperformed in terms of the overall financial returns measured as the internal rate of return of the cash flows from their investing activity (in this case a stream of the regular and irregular contributions together with the current realisable value of the units that individual purchased, ignoring the effect of tax for the moment). Over time this may become significant in either direction as an indicator of the individual's ability to judge relatively good and bad times to put money into particular asset vehicles.

It is therefore critical to ensure that returns are measured at the individual level as well as at the fund level and that the connection between the two may be analysed and reviewed by the particular individual to identify the impact of their own decisions on their overall financial returns.

A LATERAL AND CREATIVE SOLUTION FOR THE SUPERANNUATION INDUSTRY

The Chairman of the Review Committee has asked for participants to think laterally, with vision and creativity. First Dollar™ is a lateral solution founded in Members' needs which provides steps towards a vision of an industry dedicated to maximising performance for beneficiaries.

A VISION FOR THE FUTURE

We see a future where individuals have access to a range of platforms or applications through which individual investors and superannuants control and manage a variety of assets which are held in accounts across a number of different financial institutions.

Each component of this vision statement addresses Member needs as follows:

"a range of platforms or applications"

Increasingly individuals are controlling aspects of their communication and day-to-day financial management through online means (eg online banking, online broking, Facebook etc). If the market for the provision of portfolio measurement applications was opened up in the way that we suggest in this Submission, we anticipate that a number of different applications would emerge quickly. Some of these would come from existing proprietary platforms who want to participate in both the proprietary and the third party market. Some of the new competitors would include existing software companies including providers of financial software applications, and others would be new entrants to the financial software market who bring particular skills or a perspective that was fresh and sufficiently innovative to gain a market presence.

"through which the individual investors and superannuants control and manage..."

Currently, Superannuation Funds deliver to superannuants a hardcopy statement some three months after the end of the financial year giving a series of numerical snapshots of the details of their portfolios and entitlements. Individuals are also supplied with various pages of figures which provides some linkage between the statements

for the beginning of period (which are the same as the statements that were sent to a superannuant one year earlier) and the end statement which of course will be the same for the package that you will receive next year. Apart from the carbon impact of all this paperwork, this methodology allows no easy comparisons between funds or between individuals' experiences, and serves to protect existing industry participants from robust competition for Members and their Superannuation assets.

"a variety of assets..."

We do not think that either the Member's or the industry's interests will be served by allowing instant changes to asset allocation or fund choices. It would be sensible to combine the analytical and educational benefits of independent third party performance measurement solutions such as First Dollar™ with extended lock-up periods for certain types of funds (to allow funds the flexibility to invest for the long term) and more informed decision-making by end users of superannuation fund services, based on better understanding by Members of the impact of their decisions.

"... across a number of different financial institutions"

It is currently an expensive option for individuals to maintain their superannuation investments across more than one Financial Institution. But after the damage wrought on individual financial institutions by the global financial crisis, we suggest that individual investors and superannuants should be able to diversify their investments across a number of different FSPs efficiently and effectively.

At the same time, the need for adequate competition in the provision of platform and investment fund services demands that a range of large and small FSPs are in a position to provide their different services efficiently and cost effectively. We recognise also that the benefits of scale demand that some FSPs be able to grow to sufficient size to participate appropriately directly and indirectly in investment markets.

We believe that by transferring control over the performance measurement process to individual Members and beneficiaries, competitive forces will ensure the best FSPs thrive whatever the optimal size of their individual business. Crucially a process of "open source" evolution will not favour FSPs who seek to use their existing scale to lock other providers out of their proprietary distribution networks.

CONCLUSION

Investors using First Dollar™ are already reaping rewards:

Keith from NSW who "spent 30 years in the IT industry, the last 15 in selling/marketing software" said the User Guide is "pretty outstanding". Keith provided some helpful suggestions on how we can improve First Dollar™ and concluded "I just want to say I think this is an excellent piece of software and I hope you are successful in getting it used widely"

After she had built up her own First Dollar™ portfolio, Wendy from Victoria found that "...I need time to study and understand (her First Dollar™ charts) but an initial glance is very impressive." She explained that she had also "successfully completed the download and run process on ... a much bigger portfolio." She continued "We are both really excited about your software - it is what I have been looking for for quite a while... We manage our own super fund and all the investments in it ourselves - so your program is ideal for us... Thanks again for a wonderful product"

Information is power. With better information provided by independent market based solutions, trustees and beneficiaries of Australia's superannuation funds in all sectors will be able to see clearly what is currently happening, and use that information to improve their outcomes. These improvements may be achieved through cost reductions, investment allocation and individual behavioural changes, critically including a process of continuous future monitoring to ensure that more optimum results are in fact achieved by individuals for their own circumstances as they change over the course of their lifetime.

We would welcome an opportunity to demonstrate First Dollar™ in person for members of the Super System Review Committee or other interested parties, which would give us a chance to answer questions which may arise from this Submission and expand on some of the fresh concepts we have introduced.

*We appreciate the opportunity presented to explain how First Dollar Software might make a contribution to the future of the Australian Superannuation System, and we look forward to participating further as appropriate.
(Net) Performance Counts*