ASIC

Australian Securities & Investments Commission

Superannuation: Assessing Efficiency and Competitiveness - Productivity Commission Draft Report

Submission by the Australian Securities and Investments Commission

7 August 2018

Contents

Overview

1 The Australian Securities and Investments Commission (ASIC) appreciates the opportunity to provide a submission in relation to the Productivity Commission's (PC) draft report released on 29 May 2018 (Draft Report) on the efficiency and competitiveness of Australia's superannuation system.

2 Our submission is particularly focused on four subject areas in the Draft Report: defaults, decision making, insurance and the regulatory architecture. In additon, we make reference to additional specific recommendations for ASIC to act.

A Defaults

3 The Productivity Commission has highlighted the importance of default super arrangements given that superannuation is compulsory for consumers. While the default settings are not regulated by ASIC, we agree that improvements should be considered around the design of default superannuation arrangements.

The current default system

4 Superannuation is a compulsory system, so a default will be a necessary feature of the system. Default arrangements are therefore an integral part of Australia's superannuation system and, as the PC notes, have worked well for the majority of default members

5 However, a 'sizeable minority' of consumers have ended up in underperforming default funds in ways that create significant long-term costs for those consumers. Defaults tend to be sticky, and the Australian data supports this, which highlights the importance of having the right default fund in place in the first instance.

6 Furthermore, exercising consumer choice in the superannuation context is inherently complex and involves assessing risk and uncertainty across a significant time frame. These factors, combined with relatively low levels of financial literacy in Australia, make informed decision-making in the superannuation space complicated. Given this, many consumers may benefit from clearer and stronger standards around default funds even if they do exercise a choice.

Employers and defaults

7 Currently, many default arrangements for an employee are driven by choices made by employers. For this system to work well, employers must have the knowledge, capability and motivation to make choices that promote good outcomes for consumers. There are harms for consumers (employees) if an employer chooses a poor fund.

8 In relation to employer knowledge and capability, employers are of varying sizes and sophistication and, as outlined above and in the Draft Report, comparing and choosing between superannuation funds can be challenging. Accordingly, even if an employer wishes to choose the best fund for employees the employer's knowledge and capability when it comes to the

superannuation system may inhibit good choices. A poor choice then has significant consequences for any disengaged employees.

9 In relation to employer motivation, employers currently have no obligation to select a default fund that is in the best interests of their employees, nor to put their employees' interests ahead of their own in selecting a fund. This naturally creates an environment in which conflicts can arise, and more generally where the employer may not place significant importance on the selection of a default fund.

10 Some employers do exercise choice carefully and endeavour to ensure employees receive a quality product, sometimes on better terms than if the employee sought to obtain the product in the market.

11 But these benefits can be transitory, and if the member leaves the employer and is transferred into a personal plan from an employer plan in the fund the member may find themselves in an expensive superannuation product. Consumer inertia and disengagement as well as the challenges of leaving an employer means that the member may not properly act upon revised terms and conditions disclosed to them about their superannuation. This has the result that the member may remain in the fund for the long term and find their retirement savings compromised.

12 There are some limited provisions regulated by ASIC that have the aim of ensuring that employers make good decisions by addressing possible conflicts of interest. However, in ASIC's experience (and as ASIC has publicly noted), these are of limited effect. In particular, the prohibition on inducements by RSEs to employers under s68A of the SIS Act does not result in the commission of an offence nor the subsequent imposition of a penalty, and only gives rise to the creation of a statutory right for an aggrieved individual to commence a civil proceeding for the recovery of losses.

13 Employers also have consumer protections as a result of being deemed to be 'retail clients' for the purposes of receiving financial advice in relation to choosing a superannuation default fund. However, it is the interests of *employees* not *employers* that is important in this context. That is, the protections relating to financial advice on default fund selection do not directly impact those most affected by the advice – the employees. Furthermore, many employers will not obtain financial advice.

14 As a result, ASIC supports improvements to the policy framework for default fund selection as a key requirement for better consumer outcomes over the longer term.

Multiple accounts

15 As outlined in the Draft Report, significant consumer harm is caused by the proliferation of multiple accounts and associated insurance policies. The PC estimates that there are 10 million unintended multiple accounts - or 35 per cent of total accounts held by funds - costing members $690 million and $1.9 billion annually in excess administration fees and insurance premiums, respectively.

16 We note that the Government's recently announced 'Protecting your Super' package will help address this issue by enhancing the ATO's ability to more proactively consolidate lost or low balance inactive superannuation accounts, where a person has an active superannuation account.

MySuper reforms

17 ASIC notes that the Government has proposed reforms designed to improve standards of MySuper Products (Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Bill 2017), including by increasing APRA's powers in relation to MySuper products. The Draft Report identifies the outcomes test and stronger supervision of outcomes by APRA as having significant potential benefits for members.

Defaulting only once

18 Draft Recommendation 1 to have new entrants to the workforce defaulted only once and also allow choice of fund as a consumer changes employers would, if implemented, significantly reduce the incidence of consumers unintentionally having multiple accounts and insurance policies. As the PC highlights multiple accounts and insurance policies deplete those consumers' retirement savings.

19 It also strikes an appropriate balance between retaining the freedom for consumers to choose what to do with their superannuation, while also recognising and accepting the behavioural factors which are likely to drive the decision-making of many consumers with regards to their superannuation.

20 Defaulting only once would need to take into account performance issues over time. It is therefore important that default superannuation funds are designed and subject to oversight to ensure that quality outcomes will be delivered in the long term.

Arrangements for selecting default funds

21 The PC has identified some of the structural problems with current default selection arrangements. These include:

(a) The compulsory nature of superannuation means that competition drivers are, by definition, largely absent in the default space.

(b) The linking of default choice to employers places obligations on many employers that they are not well equipped to meet regarding the assessment and choice of funds.

(c) Employer interests may not be aligned with the interests of employees (members).

(d) Whether a consumer ends up in a better default fund (which many do) may be, in effect, an arbitrary by-product of where they happen to work.

(e) Some employees (members) have no choice at all.

22 While as noted above ASIC does not regulate the default settings, ASIC agrees that these issues could be addressed in a structural change to default selection. ASIC notes the PC's proposed 'best in show' list, if carefully designed, could help address many of these issues.

23 A 'best in show' list, or a similar proposal, would need to be carefully designed and implemented to ensure good consumer outcomes:

(a) (**Criteria**) The criteria for inclusion in any shortlist should cover consumer outcomes holistically to ensure there is not focus only on net investment returns.

(b) (**Choices**) We provide further comments in section B of this submission about consumer decision making in superannuation, which will be relevant to the 'best in show' model. We support the flexibility in the Draft Recommendations about the total number of funds on any such list and consider that any decisions by a Panel about the number of funds on the list should be supported by appropriate evidence about what is tractable for consumers and will drive the right outcomes in the superannuation industry longer term.

(c) (**Consumer testing**) We suggest conducting research to understand what consumers might understand a 'best in show' list to mean, particularly in the context of receiving financial advice.

(d) (**Material deficiency of shortlisted fund**) There would clearly need to be appropriate mechanisms for ongoing assessment of the inclusion of funds on any list, given that some may no longer be appropriate over time.

24 ASIC agrees with the PC that care would need to be taken to ensure that trustees with funds in the 'best in show' list do not seek to use the default arrangements inappropriately as a means to distribute more expensive products.

B Consumer decision making

25 The key Draft Recommendations relevant to this section of our submission relate to three key themes: dashboards, other disclosure requirements and guidance and support.

More useful information for consumers

26 ASIC supports efforts to improve information and disclosure for consumers, and this is a key area of focus for our regulatory work.

27 We note that while disclosure is important, given that superannuation is a long-term credence product which involves an assessment of risk and uncertainty over a long time frame, it will have limitations. There is a range of other regulatory tools that need to complement disclosure, especially in relation to issues such as the extent and impact of conflicts of interest.

28 Accordingly, disclosure-based approaches should include flexibility to provide individual consumers with information that meets their decision-making needs (e.g. through layering and tailoring of information). These approaches should also be regularly reviewed so they can be improved and revised as needed. These reviews may also suggest the disclosure tool is not achieving its objectives and an alternative approach (which may not involve disclosure) is warranted.

29 Against this background, we note that there will need to be:

(a) more evidence-based and consumer tested development of comparison tools

(b) an outcomes-based approach to evaluating comparison tools (e.g. are they easily navigable and does consumer use of them lead to “better” outcomes?)

(c) steps to ensure integrity of included data

(d) financial capability support for consumers using comparison tools.

Dashboards

30 Dashboards can provide one form of comparison tool to help guide decision making and we support evidence-based measures to make dashboards and other comparison tools more usable and useful for consumers.

31 We support the proposal to have all superannuation product dashboards available on a single website, and readily accessible to consumers at critical

decision-making points in time, such as when they are contemplating consolidating their accounts.

MoneySmart and dashboards

32 It is our view that MoneySmart is the appropriate place for product dashboards to be hosted. In this regard, we note that the Government has previously identified MoneySmart as being the primary channel for communicating consumer information regarding superannuation, and that MoneySmart can provide guidance and context to assist consumers in understanding product dashboards. With appropriate resources, ASIC would work with the ATO and myGov to ensure relevant information is readily and seamlessly accessible to consumers through those sites and services.

33 In relation to providing dashboards to consumers when they switch from a MySuper product to a choice product, the PC may wish to give further consideration to how ASIC's MoneySmart website can facilitate this proposal.

34 ASIC anticipates doing further work in relation to dashboards and comparison tools for superannuation.

Dashboard development

35 Any development process for dashboards should also consider how best to ensure that dashboards are provided at an appropriate time in decision making processes.

36 Previous research to understand how consumers engage with and use dashboards demonstrates the complexity of consumer behaviour when engaging with comparison tools. We outline some of this research below.

Dashboards research

ASIC has previously sought to understand how consumers engage with product dashboards, and how different designs and approaches to presentation influence consumers' understanding of key information.

In this regard, ASIC engaged Latitude Insights to undertake consumer testing of MySuper product dashboards in 2013. Report 378 *Consumer* *testing of the MySuper product dashboard*, released in December 2013, sought consumer feedback from 55 participants.[1]

Following on from this, in December 2015 ASIC published further consumer testing undertaken by Latititude Insights in relation to choice product dashboards. Report 455 *Consumer testing of the Choice product dashboard* sought feedback from 120 consumers.[2]

The consumer testing found:

- Many consumers said they were confused by superannuation and had not taken action in the past due to its complexity
- Support for the dashboard(s) varied: some said they would use them, some disengaged from them and some were supportive of the material they viewed during the testing but admitted they would not be likely to use the dashboards in 'real' decision scenarios (e.g. because they wouldn't think to look it up/timing factors or because the dashboard wasn't sufficiently personalised to their circumstances and needs)
- Consumer preferences for information presentation varied significantly
- Small design details impacted whether and how individuals noticed or understood information
- Fee information was considered important but difficult to understand
- Understanding of risk was superficial and risk information was found to be very difficult to simplify.

Importantly, a group of academics who subsequently independently tested the recommended dashboard in a controlled choice experiment discovered a key element, the *investment mix pie chart*, was highly relied upon but subject to a visual bias that caused participants to prefer options with more segmented pies (lower concentration) and with equally sized segments (lower deviation from what is known as a '1/n allocation').[3]

This and other, unexplored visual biases could cause consumers to select options that conflict with their own risk preferences and be exploited by motivated fund managers, leading to poor outcomes. This research also underscores the need for consumer testing to consider not only the look, feel and sentiment towards consumer disclosure tools – their 'user friendliness' – but also whether they *actually* aid better decision-making or outcomes.

37 Revising and simplifying dashboards may require legislative change as the core requirements to be included in MySuper and choice product dashboards are set out in s 1017BA of the Corporations Act.

[1] https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-378-consumer-testing-of-the-mysuper-product-dashboard/
[2] https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-455-consumer-testing-of-the-choice-product-dashboard/
[3] Hazel Bateman, Isabella Dobrescu, Ben Newell, Andreas Ortmann and Susan Thorp (2013) *As easy as pie: How retirement savers use prescribed investment disclosures*: https://www.uts.edu.au/sites/default/files/qfr-archive-03/QFR-rp326.pdf

38 In relation to choice product dashboards, ASIC has deferred the commencement date for choice product dashboards a number of times – currently deferred through to 1 July 2019 – as necessary supporting regulations have not yet been made for choice product dashboards. Again, the formal requirements should be carefully consumer tested before implementation. Notwithstanding this, we are of the view that upon implementation, choice product dashboards will provide consumers with a valuable comparative tool that is not currently available for choice products. Nevertheless, given the sheer number and diversity of choice investment options, implementation may also require consideration of pragmatic exclusions or necessary flexibility in the requirements.

39 ASIC agrees with the PC without a centralised location dashboards will not best fulfil their purpose of enabling consumers to compare products. Similar insights were highlighted in *Report 581 Review of ASIC Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements*, an external expert's report released in July by ASIC.

ASIC's MoneySmart

40 MoneySmart, ASIC's consumer facing website, is a vital tool through which ASIC disseminates information to the general public, and one which we constantly seek to leverage. We consider that there is significant scope within the Draft Recommendations for MoneySmart to play a major role. We refer to our comments on dashboards above.

41 In addition, ASIC supports Draft Recommendation 11 that would lead to all superannuation members at age 55 being guided to consider the 'Retirement and Superannuation' section of ASIC's MoneySmart website.

Other disclosure requirements and tools

42 Following the release of *Report 581 Review of ASIC Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements* referred to above, ASIC is currently considering next steps to provide meaningful information to consumers in relation to superannuation fees and costs.

43 In ASIC's view simple, comparable and easily understood information for consumers, as articulated in Draft Recommendation 21, is important. However, currently disclosure requirements are set out in legislation and regulations. ASIC has some ability to modify these requirements by legislative instrument, but there are limits to these powers. In extreme circumstances, the proposed product intervention power may enable ASIC to

set specific disclosure requirements for a type of product where there is a risk of significant consumer detriment.

44 Where ASIC is empowered to do so, ASIC will consider setting further standards for disclosure requirements, having regard to the net regulatory benefit, including the likelihood of meaningful improvement to consumer outcomes. Wherever possible, ASIC endeavours to consumer test these requirements to ensure they are evidence based.

45 However, as we have already stated simplified and standardised presentation of information as prescribed by ASIC or the legislature will not address barriers to better consumer decision making. Nor can it alone ensure effective competition.

46 Draft Recommendation 16 proposes that trustees provide calculators on their websites to assist consumers in determining the impact of insurance premiums on their balances at retirement. We support this proposal as a simple way of providing consumers with information to assist them in their decision-making. Our policy on the use of calculators is well articulated in Regulatory Guide 167 *Licensing: Discretionary powers*.

Financial advice

47 Directing consumers approaching retirement to MoneySmart, as proposed by the PC, is a good first step in trying to provide consumers with information about their retirement. It is also a good opportunity to encourage consumers to seek out financial advice at a time when they are making complex decisions with long term implications, particularly in light of recent proposals concerning products such as comprehensive income products for retirement.

48 We note the Draft Report's comments around the importance of quality financial advice in guiding consumers through complex decision making.

49 In line with our earlier comments regarding benchmarks, we envisage that the 'best in show' concept would if implemented provide a useful baseline around which financial advice in respect of superannuation can be formulated.

Trailing commissions

50 Trailing commissions were banned under the FoFA reforms going forward, but those already in place continue to be paid under transitional (grandfathered) arrangements.

51 ASIC's position is that grandfathered commissions should cease as soon as reasonably practicable and to the maximum possible extent.

52 Short of a more rapid phase out of trailing commissions, we support the PC's (Draft Recommendation 13) that there be more transparency about the extent trailing commissions are still paid by members of a fund and that any trailing commissions paid are disclosed periodically to the member. ASIC would explore ways to make this information public in a comparable manner.

C Insurance

Insurance in superannuation - a focus for ASIC

53 Approximately 70% of all life insurance in Australia is held within superannuation funds and is therefore an area of significant interest to ASIC.

54 ASIC agrees with the PC that many members benefit from default group insurance arrangements in superannuation. This insurance can provide cover at lower cost to many Australians.

55 However, given the significance of insurance in super, it is important that opportunities to improve practices are pursued. Following on from our findings in REP 529, in 2017-18 ASIC has been conducting a surveillance project about insurance, including in respect of issues such as disclosure, claims and complaints handling and conflicts. Our report is to be released shortly.

56 The findings from this project suggest that the superannuation industry has more work to do if it is to deliver consistently good consumer outcomes in relation to insurance offerings.

57 In this context, ASIC strongly supports the need for significant industry change in respect of insurance in superannuation. ASIC agrees with the PC that actions are needed to address issues such as:

(a) inappropriate balance erosion by insurance premiums

(b) multiple and confusing coverage and definitions

(c) inappropriate defaults

(d) lack of consumer awareness about insurance coverage

(e) inadequate consumer communication and information at the point that cover changes or ceases

(f) poor claims handling and complaints handling.

58 ASIC's ongoing work on insurance in superannuation will focus on claims processes and outcomes, complaints handling (including in relation to insurance), the use of defaults which result in higher premiums and monitoring industry progress in making insurance easier for consumers. In following up on issues ASIC identified as causing systemic consumer harm in relation to insurance, ASIC will consider enforcement action if appropriate.

59 There are however limitations to the improvements for consumers that can be achieved within the current system by ASIC.

Insurance code

60 ASIC considers that, with broad industry commitment and effective monitoring and enforcement arrangements, industry codes can support higher standards in relation to the provision of financial products and services to consumers as well as supporting the dispute resolution process and provide certainty for consumers.

61 However, ASIC notes that, at present, there are significant weaknesses in the current Insurance in Superannuation Voluntary Code of Practice, including around its monitoring and enforcement, that limit is potential effectiveness.

62 The PC also identifies that the deficiencies in the code and that it would not meet ASIC's Code approval standards under Regulatory Guide 183.

63 ASIC supports the broad direction set out in Recommendation 18 to improve the coverage and benefits of the Code. ASIC will work with APRA to monitor the implementation and coverage of the code. However, we note there are challenges for effective self-regulation in relation to Insurance in Superannuation. The superannuation sector has a number of characteristics which have traditionally limited the prospects for successful industry codes, particularly in the absence of supporting legislative intervention. These include:

(a) there are multiple, competing industry associations

(b) the superannuation industry has a range of business models and interests, and the role of a further group – insurers – with their own interests complicates things further

(c) the current compulsory setting for both superannuation, and the default setting for insurance in superannuation, means that the market is not one with strong demand-side competition

(d) there has been, to date, an absence of properly resourced and independent consumer organisations in the superannuation sector to help ensure accountability and appropriate standards, which has been a feature of code development in other sectors.

Note: See Self-Regulation Taskforce, Industry self-regulation in consumer markets, Commonwealth of Australia, August 2000, which has informed ASIC's views on industry codes.

64 In this context, ASIC would make the following observations about the process to achieve a robust code that delivers benefits across the superannuation sector:

(a) Coverage: given the fragmented nature of superannuation entities and industry representative associations, it is likely that full coverage will only be achieved if code membership is made mandatory. At present, ASIC cannot mandate a code for a particular sector – this would require legislative change.

(b) Approval: At present ASIC cannot force industry sectors to submit a code for approval. This limits ASIC's leverage around requiring improvements to the code. While ASIC has long had powers to approve codes, only one broad code, the Banking Code, has been voluntarily submitted to ASIC for approval.[4]

(c) Administration and Enforcement: It is typically a requirement of codes that an independent and appropriately resourced body undertakes to monitor and enforce the code, and that the code is effectively linked to a dispute resolution scheme. That is, an enforceable code is not one enforceable by ASIC, but rather is binding via contractual arrangements and where the code administrator is responsible for enforcement. The fragmented nature of industry associations may pose challenges in this respect.[5]

65 We consider that ASIC has clearly communicated what is needed for an enforceable code of conduct. We note that enforceability of a code is one of the key threshold criteria for approval by ASIC under Regulatory Guide 183 *Approval of financial services sector codes of conduct* (RG 183). It is essential that code breaches can be dealt with effectively and independently. Unless the Insurance Code becomes enforceable and overseen by an independent code administrator, there will be substantial limits to its effectiveness.

66 ASIC engaged proactively with the ISWG prior to and during the development of the Insurance Code. We supported the ISWG's original intention of creating a binding and enforceable code for the whole industry, which would ultimately be submitted to ASIC for approval. However, during the course of the consultation period, this intention was abandoned.

Other observations about the Insurance Code

67 As noted above, ASIC will work with APRA to monitor the adoption of the Insurance Code across the sector over the remainder of 2018 to understand

[4] This will change if the Government implements the recommendations of the ASIC Enforcement Review Taskforce Report, which include recommendations that ASIC approval should be required for the contents and governance arrangements of relevant codes and that entities should be required to subscribe to approved codes relevant to the activities in which they are engaged (ASIC Enforcement Review Taskforce Report, Recommendations 18 and 19)
[5] This would remain the case if the Government implements the recommendations of the ASIC Enforcement Review Taskforce Report which recommends that should be binding on and enforceable against subscribers by contractual arrangements with a code monitoring body (Recommendations 20).

its impact and if there is scope for improvement. One issue that ASIC will be interested to test is whether the superannuation industry can collectively commit to the establishment of a properly resourced code administrator, especially given the challenges noted above.

68 The Life Insurance Code, which applies to insurers, also has the potential to improve outcomes. For those issues where the Insurance Code is not effective, another solution will most likely be required, rather than trying to strengthen the Insurance Code.

Review of insurance in superannuation

69 ASIC considers that Draft Recommendation 19 and the proposal for an independent review of insurance in superannuation should be prioritised. Given the number of insurance policies held within superannuation, and the impact of insurance on consumers' retirement benefits, it is critical that the system operates effectively and for the benefit of consumers. ASIC could provide input into this independent review, based on our work to date and early observations about the impact of the Insurance Code.

70 For completeness, we note the Government's in principle agreement to the ASIC Enforcement Review Taskforce's recommendations about industry codes. This includes ASIC approval being required for relevant codes. Implementation of these recommendations is unlikely to change ASIC's position on the issues above.

MySuper and the Insurance Code

71 We are strongly in favour of additional, and stronger, criteria for MySuper authorisations, as this authorisation operates as a consumer protection mechanism for default members in superannuation.

72 This could usefully include specific requirements relating to insurance.

73 One option is the adoption of the Insurance Code as a mandatory requirement for MySuper authorisation, as proposed in Draft Recommendation 17. However, ASIC would suggest that the issues raised in the preceding sections may need to be addressed before such a reform was introduced to ensure that the code was robust and effectively monitored.

74 Having the code approved by ASIC, with requirements for regular review, might also be a necessary step prior to such a reform.

75 Currently, neither the characteristics for a MySuper product in section 29TC of the SIS Act nor the additional obligations of a trustee in relation to a MySuper product in section s 29VN impose specific requirements in relation to insurance in a MySuper product. The *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation*

Measures No 1) Bill (Member Outcomes Bill) will, if passed introduce specific obligations for trustees to assess the insurance strategy and insurance fees for the MySuper product.

Additional insurance law reform

76 We support Draft Recommendations 14 and 15 in relation to opt-in insurance for young members, and ceasing insurance cover for inactive accounts. Both these recommendations will reduce the incidence of member accounts being unnecessarily eroded by insurance premiums. In particular, these two recommendations will benefit those consumers (e.g. young members, casual workers, etc.) most vulnerable to significant erosion of their balances.

77 We note that the proposals in relation to both of these Draft Recommendations have been recently announced as part of the Government's 'Protecting Your Super' package. Further, and in respect of ceasing cover when there are no contributions, the Insurance Code currently provides for the cessation of income protection insurance in cases where contributions have not been received in 13 months, as well as in respect of death and TPD where the balance is below $6,000.

78 ASIC also notes its existing support for law reform in relation to life insurance that would help improve outcomes in insurance in super. For example, proposed priority legislative changes in relation to insurance in super include:

(a) removing the current exemption for insurance claims handling from the definition of 'financial service' in the Corporations legislation and amending the law to give ASIC power to act in relation to claims handling conduct. ASIC has also recommended that more significant penalties be introduced for misconduct in relation to claims practices;

(b) extending unfair contract term provisions to contracts of insurance to ensure that consumers who purchase insurance have the same access to protection from unfair terms in insurance contracts as they do for other contracts for financial products and services. The Government is currently consulting on this proposal until 24 August 2018.

D Regulatory Architecture

ASIC's role in superannuation

79 Within the scope of ASIC's jurisdiction under the regulatory framework, ASIC's aim is to have a superannuation system that delivers good outcomes for consumers.

80 ASIC seeks to promote the fair treatment of consumers within the superannuation system, and to reduce the incidence and impact of poor conduct. ASIC applies a strategic approach that aims to improve the behaviour of industry participants across the superannuation sector. This is particularly important given the default and compulsory nature of superannuation.

81 ASIC is responsible for granting Australian financial services licences to superannuation trustees making public offers of superannuation products or providing other financial services, such as financial product advice. ASIC also oversees compliance with a range of obligations designed to promote good consumer outcomes, in particular in relation to marketing, disclosure, information updates and complaints handling. ASIC also oversees specific transparency obligations. More broadly ASIC's work is focused on other aspects of superannuation, not simply on those offering superannuation products. As highlighted in the Draft Report, financial advice can be important for consumer outcomes within superannuation.

82 ASIC works within a regulatory framework that includes important roles for APRA and the ATO. From 1 November 2018 this framework will be strengthened by a new dispute resolution body, Australian Financial Complaints Authority, operating to address the disputes of individual consumers across financial services including superannuation.

Regulatory responsibilities in superannuation

83 Both ASIC and APRA have a key role in ensuring good consumer outcomes in the superannuation system. The allocation of responsibilities between the regulators (and any modifications to the current regime) is ultimately a matter for Government to consider.

84 The Draft Report raises concerns about the conduct regulation arrangements for the superannuation system, with a focus on the roles of APRA and ASIC (Draft finding 10.2).

85 To provide more information about the roles and relationship between APRA and ASIC in relation to RSE Licensees ASIC and APRA have recently published a joint document entitled 'Regulation of superannuation entities by APRA and ASIC'.[6]

86 The document sets out how APRA and ASIC understand their responsibilities are currently divided under existing legislation and describes their approach to carrying out their roles. The document is not intended to give the agencies' views on the appropriateness of the current legislative arrangements.

Conduct regulation under the SIS Act

87 ASIC notes that APRA has a different role in superannuation compared to its role in other parts of the financial system. APRA is tasked under the SIS Act with a greater conduct regulation role in relation to superannuation, which is different to its traditional prudential role.

88 While APRA monitors risk in the superannuation system to mitigate the chance of a fund failure, APRA's focus is additionally directed at monitoring the performance of funds, licensing superannuation entities, product authorisation and ensuring that trustees act in the interests of members – much of which would be performed by ASIC in other parts of the financial system.

89 The SIS Act provides that APRA has the general administration of a long list of specific provisions and the administration of provisions under Parts 3 and 6 of SIS (and that can deal with a wide range of subject areas) to the extent not conferred on another regulator.

90 In contrast, ASIC's jurisdiction is limited under the SIS Act in two ways. Firstly, the areas of conduct that ASIC is responsible for are limited (e.g. ASIC does not have responsibility for the best interests provisions except to the extent it concerns disclosure). Secondly, ASIC has limited powers of enforcement, whether compared to APRA and the ATO or compared to our powers under the Corporations Act (e.g. there is no ability for ASIC to institute civil penalty proceedings under the SIS Act).

91 Generally, to avoid overlap in roles, where APRA's role has been extended it has displaced the application of some of the conduct related provisions administered by ASIC. A current example of this is the planned limitation of the proposed Design and Distribution Obligations. These obligations would extend ASIC's regulatory conduct toolkit to cover aspects of the design and

[6] https://download.asic.gov.au/media/4837214/regulation-of-superannuation-entities-by-apra-and-asic.pdf; https://www.apra.gov.au/sites/default/files/regulation_of_superannuation_entities_by_apra_and_asic.pdf

marketing of financial services products. However, the draft legislation to implement those obligations provides an exemption for MySuper products, presumably on the basis that obligations administered by APRA already provide an equivalent additional measure of conduct regulation.[7]

92 More generally, under the existing regulatory framework there is also an issue with regulators lacking the full suite of powers and sanctions of sufficient strength to enable them to properly fulfil their existing functions. Both regulators would argue that there is scope for improvement in their powers, which the Government has accepted as indicated by the reforms that have been proposed for both APRA's and ASIC's powers more broadly.

ASIC and APRA co-operation and co-ordination

93 Within the structure of the current legislation, APRA and ASIC seek to co-operate and co-ordinate their activities as effectively as possible. Communication and collaboration between APRA and ASIC takes place under both formal and informal arrangements and at a range of levels.

94 The formal framework for co-operation and information sharing between APRA and ASIC is provided by the legislation governing each agency.[8] This is built on by a Memorandum of Understanding (MOU) between the two agencies and a Joint Protocol. The objective of the MoU is to provide a framework for co-operation between the two agencies whilst the Joint Protocol facilitates appropriate, early and effective communication and co-operation.

95 There are also regular engagements for the sharing of information and working on regulatory priorities which involve information-sharing about trustees. There are more informal regular person to person engagements in the nature of general discussions that happen as well.

96 In other areas of financial services ASIC and APRA have undertaken joint project work to address problems together using the skills of each agency (e.g. ASIC and APRA are working on data collection and publication of Life Insurance claims data). Opportunities to apply this approach in superannuation may arise.

[7] July 2018 Exposure Draft Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018, No , 218, Schedule 1, Clause 994B(3)
[8] See s 56 of the APRA Act and s 127 of the ASIC Act.

Conduct regulation, current regulatory approaches and settings

97 Given the compulsory, default and long-term nature of superannuation, the ability for demand-side pressure to drive better conduct in superannuation is limited, as the PC recognises.

98 Therefore, ASIC agrees that there is a significant role for strategic conduct regulation in superannuation, in particular that goes beyond disclosure and addresses misconduct relevant to outcomes. ASIC is currently implementing an enhanced approach to its regulation of superannuation, but also notes that a greater conduct regulation role would desirably require law reform (see below).

99 ASIC's approach as a conduct regulator more broadly involves a focus on public enforcement and transparent regulatory actions. That is, in part, due to the broader deterrent effect that such action can have. ASIC believes that public enforcement action is an important tool in trying to minimise the incidence of misconduct. ASIC has released Information Sheet 152 which sets out our views on public enforcement. In that sense, ASIC's role as a conduct regulator is different to the prudential part of APRA's role which may require a less public approach than that taken by ASIC.

100 The PC recognises that legislative reform would be required if ASIC were to take on a clearer strategic conduct regulation in relation to superannuation trustees (p398). ASIC would need additional powers if it were to have a more significant role in enforcement under the SIS Act.

101 ASIC's view is that any proposal to modify responsibilities or powers under SIS should not be done at the expense of APRA's ability to properly carry out its functions. Indeed, APRA's powers may also require strengthening. The Government has proposed a strengthening of APRA's powers in the Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Bill 2017, which is currently before the Senate.

Conduct regulation within the regulatory framework

102 ASIC also notes that there are some deficiencies within the superannuation system that are better addressed through changes to system design rather than (or in addition to) conduct regulation. For example, the PC's recommendations about the default system recognises that the framework for the allocation of default funds needs changing to improve consumer outcomes. In any recasting of the regulatory architecture it would be important to assess the intended outcomes and the nature of deficiencies in the super system in considering those problems that can best be addressed by conduct regulation by ASIC.

103 On this point, ASIC's role as a conduct regulator cannot of itself ensure good performance of financial products. Rather it can act against failures to comply with specific expectations of behaviour set out in the law, which contribute to the performance achieved. By way of illustration, in the context of director duty actions ASIC notes that ASIC's role is not to take action on the basis that a better business judgement could have been made. Instead ASIC needs to identify a failure to comply with the particular obligations applying to directors.

A role for ASIC in financial reporting and audit for superannuation

104 One area in which ASIC has identified a "gap" in the regulation of superannuation trustees is in respect of financial reports and audits. ASIC has raised this issue publicly before Parliamentary Committees in the past.

105 Currently, no Australian regulator undertakes surveillance of the financial reports of regulated superannuation funds, approved deposit funds and pooled superannuation trusts or inspects the audits of those financial reports. Note that this is in contrast to the SMSF auditors who are both registered and regulated by ASIC.

106 While ASIC has expertise in regulating financial reports and audits of entities under the Corporations Act 2001, we do not presently have the statutory powers (or funding) to oversee regulated superannuation entity financial reports and audits. ASIC would be willing to undertake this role, including conducting proactive surveillance of financial reports and audits.

Enhancements to ASIC's approach

107 As noted above, within the scope of ASIC's existing jurisdiction under the regulatory framework ASIC is currently assessing how we can enhance our approach to superannuation regulation to achieve better consumer outcomes.

108 We are examining ways of intensifying our regulatory supervision and have already started to strengthen our team focused on this area.

109 ASIC will implement a more intensive engagement model with the opportunity for more consistent oversight by ASIC staff of RSE licensees, more frequent onsite visits, more public actions in superannuation and better leveraging of data. This is consistent in our view with the 'strategic conduct regulation' approach discussed by the Productivity Commission.

110 Nevertheless, as noted earlier, our role will necessarily be defined by the regulatory settings in place.

111 This evolving approach would improve ASIC's ability to engage efficiently and effectively with APRA, as well as the regulated population.

Data

Superannuation data working group

112 ASIC supports Recommendation 22 concerning the establishment of a superannuation data working group with APRA, ASIC, the ATO and the ABS.

113 ASIC's ability to achieve its regulatory objectives could be improved through increased data availability. This includes data that ASIC already collects, data from other government agencies, and data from private sector parties. Data analytics can play a critical role in identifying and mitigating conduct risk. This will increasingly be the case in the context of some of the law reform arising from the Financial System Inquiry, such as the development of product intervention powers and the comprehensive income product in retirement.

114 The increased sharing of data across government agencies is also of benefit to ASIC. Data from agencies such as APRA and the ATO already form part of ASIC's monitoring activities, although there is scope to increase the breadth of data that is systematically shared and the ease of access to that data. The establishment of a superannuation working group with shared database access could also reduce the business reporting burden while also increasing the effectiveness of agencies requiring access to this data.

115 We also strongly support increased product-level reporting into APRA’s reporting framework. In addition to enhancing ASIC’s ability to better analyse an understand practices, and identify misconduct, there may also be scope to explore publication of some of this data to promote better consumer decision making (like the joint ASIC-APRA project to publish life insurance claims data).

Consumer advocacy

116 Finally, ASIC notes that, as opposed to other parts of the financial services sector, there is no dedicated consumer body to broadly advocate for superannuation members. ASIC is mindful of this and has been supportive of the establishment of the Superannuation Consumers’ Centre to address this gap. The Centre is aimed at improving the operation of the system by providing input into policy and industry practice and informing consumers on superannuation. An appropriately funded consumer organisation in the superannuation sector will assist ASIC, and other regulators, to more effectively assess and prioritise issues impacting superannuation members.

E Other issues

117 Section C of this submission comments on some suggestions for further ASIC work concerning disclosure. Set out below are comments on additional areas covered in Draft Recommendation 21.

Related party outsourcing arrangements

118 The PC has suggested that ASIC require all superannuation funds to publicly disclose to current and prospective members the proportion of costs paid to service providers that are associated with related party outsourcing arrangements. ASIC can see merit in this recommendation but would make the following observations.

119 Although there are elements of the current disclosure and transparency regime that touch on related party or outsourcing arrangements, specific and more detailed information of the kind contemplated by Recommendation 21 would require legislative reform.

120 ASIC notes that disclosure to individual consumers about conflicts of interest in financial services has, of itself, not often been effective in helping to reduce the impact of these conflicts, and there is research from behavioural economics that helps to explain this experience. This may be particularly the case in a compulsory superannuation system. Therefore, ASIC suggests that the Productivity Commission may wish to consider how this information could be made more generally available to the broader market, other regulators and policy makers.

121 That is, ASIC supports transparency about related party arrangements, but this greater transparency is likely to have a greater impact if it can convey information in an accessible manner to a broader audience and thereby have the potential for positive effects on the behaviour of regulated entities in superannuation.

122 Finally, ASIC notes that transparency can be an important means to address issues of conflicts of interest, but other tools will often be required to incentivise improved behaviour in relation to conflicts.

123 ASIC notes the work that APRA has been doing in relation to outsourcing arrangements giving rise to conflicts of interest concerns (see APRA's findings from its thematic review of related party arrangements released on 29 May 2018).

Merger investigations

124 ASIC supports the PC's focus on ensuring that directors of superannuation trustees focus on furthering the interests of members, including in pursuing mergers.

125 Under the current SIS Act settings there are however challenges in ASIC pursuing action against directors in related to failed mergers. In particular the enforcement powers of ASIC under the SIS Act are limited. This is because APRA rather than ASIC has the general administration of the s.52A covenant applying to directors under the SIS Act and there is no civil or criminal penalty associated with a failure to comply with the covenant. ASIC has no power to disqualify a director under the SIS Act.

126 To the extent that director misconduct is of concern in relation to failed mergers ASIC would favour strengthening the consequences for failing to comply with the s52A covenant under the SIS Act. ASIC notes that law reform to achieve this has been proposed (see Treasury Laws Amendment (Improving Accountability and Member Outcomes No. 1) Bill 2017 which is currently before the Senate).

Exit and switching fees

127 In relation to exit fees, ASIC notes that the Government has proposed legislative reform under the Government's 'Protecting Your Super' package that will prohibit the charging of exit fees.

128 Currently, exit fees, switching fees and buy-sell spreads must be charged at no more than on a cost recovery basis (s 99C of the SIS Act). This and other fee charging rules are contained in Part 11A of the SIS Act, and this is also where the proposed fee amendments in the 'Protecting Your Super' package are proposed to be included.

129 ASIC's role in administering Part 11A is limited to administering restrictions about how the cost of financial product advice can be passed on to members. ASIC does not administer the other fee rules – this is overseen by APRA. There is no change to this proposed under the 'Protecting Your Super package'. Accordingly, and consistent with other parts of the superannuation system, ASIC's role in relation to fees charged by trustees is focused on disclosure.

130 The PC has suggested ASIC should review whether exit and switching fees are unrelated to the underlying performance of the product or unreasonably impede members switching to better products.

131 Given the limits on ASIC's responsibility in fees, ASIC would not able to take action if a trustee were contravening the existing restrictions on exit or

switching fees, or the proposed ban on exit fees. ASIC could only take action if the fee disclosed is inaccurate, misleading or deceptive. In light of this ASIC is unlikely to prioritise work of this kind soon.