The Association of Superannuation Funds of Australia Limited
ABN 29 002 786 290
ASFA Secretariat
PO Box 1485, Sydney NSW 2001
p: 02 9264 9300 (1800 812 798 outside Sydney)
f: 02 9264 8824
w: www.superannuation.asn.au

The Productivity Commission
Annual Review of Regulatory Burdens
on Business - Business and
Consumer Services
Level 2, 15 Moore Street
Canberra City ACT 2600, Australia

Re: Annual Review of Regulatory Burdens on Business - Business and Consumer Services.

The Association of Superannuation Funds of Australia (ASFA) is pleased to make this submission to the Productivity Commission's Review of Regulatory Burdens on Business and Consumer Services.

ASFA is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. Our membership which includes corporate, public sector, industry and retail superannuation funds plus service providers who provide professional services to SMSFs, account for more than 5.7 million member accounts and over 80% of superannuation savings.

The announcement of this review coincides with the Australian Government Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System, also known as the Cooper Review. ASFA provided comprehensive submissions to each of the three phases of the Review following extensive consultation with our membership and the broader industry. As discussed in our meeting in December with Commissioner Sylvan, ASFA's contribution to this inquiry is an amalgam of key sections from previous ASFA submissions dealing with key regulatory themes. We understand that this review is focussing on multiple sectors of the Australian economy and hence the focus of this submission will remain 'high level' to the extent possible.

Effectiveness of regulation

There are two sides to assessing the effectiveness of regulation – the cost involved and the resulting benefit or usefulness of the regulation. The first part of the equation (i.e. the cost to funds) can certainly be identified. Increases in costs when regulations change, including setting up systems etc to deal with the change, can be monitored and recorded. However, assessing the effectiveness or usefulness of regulation is more difficult.

Most regulatory proposals in the last 5 years have included an impact assessment statement which attempts to assess the effect of implementation, although this assessment is usually around the impact and cost to government or the relevant regulator as opposed to the industry. The role of the Office of Best Practice Regulation (OBPR) – a federal department – is to assess whether the regulatory change is actually serving its purpose and of benefit to the impacted industry etc. ASFA welcomes the enhanced role of the OBPR and hopes that more superannuation regulation is reviewed by the agency.

While much regulation is necessary and beneficial, there are cases where this may not be so or where regulations could be better designed. There is a perception that law makers too often concern themselves with effectiveness, ignoring efficiency issues — that is, existing or proposed regulation may achieve a particular policy goal but not necessarily be the 'best' or lowest cost means of doing so.

In areas such as member disclosure, the effectiveness of regulation can be established through market research to determine how members have responded. ASFA's view with respect to regulatory change is that all future legislation should take into account a cost/benefit analysis by agencies such as the OBPR. That is, there should be more rigour on disclosing the cost of implementing legislation since this ultimately reduces members' account balances. Whilst we understand this is done now, it is not always done with industry consultation. ASFA believes there should be a formal industry consultation process with respect to costing proposed legislative changes. The industry should provide input on likely implementation costs (i.e. the industry as well as government should provide cost estimates, since the latter has often produced underestimated figures in the past).

An example of where regulation is now out of step is that the SIS Act, the governing statute for the superannuation industry, does not contain any references to financial advice. The legislation governing superannuation should recognise and accommodate the role financial advice plays in the Australian superannuation context. The Corporations Act should also be amended to explicitly include a fiduciary duty for financial advisers, as recommended recently by the Ripoll Inquiry.

Although ASFA is satisfied that Superannuation regulations have been optimised to protect members' interests and benefits, we also believe that there are a number of areas in which the current regulatory regime needs to be reviewed. These are outlined below under the relevant broad headings.

Disclosure

- Disclosure has become a millstone and has not achieved many of its objectives. In particular, its transfer to Chapter 7 of the Corporations Act has arguably been counter productive for the superannuation industry and has involved super funds in excessive compliance costs. The disclosure procedures previously included in the SIS Act were specifically designed for superannuation and generally worked better. There is a compelling argument that the disclosure requirements for superannuation should be either returned to the SIS Act and its regulations or separately dealt with in the Corporations Act, rather than trying to make superannuation fit in with other financial products which to-date has simply resulted in greater confusion/uncertainty.

- The costs incurred in revising benefit statements to comply with new requirements is another example of deadweight costs to the system – for example, the requirement to disclose historical long term investment returns in exit statements which arguably provides little or no value to an individual who is leaving the fund. We note that the Government has announced its intention to remove this requirement.

- Other examples of deadweight costs include:

    - paper based communications, particularly annual reports;
    - the amount of resources required to undertake the annual APRA reporting process;
    - breach reporting across all regulators including APRA, ASIC, ATO and AUSTRAC; and
    - the complex contribution rules (Particularly the 'work test' that applies to contributions by those of age 65).

Sole Purpose Test

- The sole purpose test has existed since 1993 and has been manipulated and massaged to try and make it fit in with the superannuation regime as it currently stands.

- Government has been reluctant to review this aspect of superannuation up to this point. As this is a corner stone of superannuation, it is something which should be part of the current debate on the operation and efficiency of the system. An example is the arrangements which now proliferate for funds to provide financial advice to members and to allow members to pay for that advice from their superannuation accounts. APRA deals with this by confining the advice to superannuation only and the amount deducted from their account can only be in payment for that part of the advice. This is an artificial contrivance and the practice should be an ancillary purpose under section 62 of SIS so that it is clear to any fund what the parameters are in this regard.

Investment

- Section 52(2)(f) of the SIS Act requires a trustee to develop an investment strategy based on the elements outlined in that covenant. ASFA's view is that the covenant has not kept pace with member investment choice. APRA's position on this covenant is that trustees must still meet this requirement when members exercise investment choice. ASFA considers this to be unworkable as the concept of choice by its very nature requires a shift of responsibility for the investment decision from the trustee to the member. While trustees should remain responsible for the options offered and how they are delivered and communicated to members, they should not remain liable for the properly informed decisions of members who take up choice. The covenant should apply to the default option offered to members by the trustee, but where they choose to invest outside of that option it should be up to the member to take responsibility for their choice.

Licensing

Trustees

- The requirements to qualify for an RSE Licence are extremely high and comprehensive. Trustees should not be required to obtain an AFS Licence in addition to an RSE Licence just to provide members with general advice.

Administration

- It is common for superannuation funds to outsource their administration. Another common situation is a large conglomerate organisation where the administration is performed "in house", but by a different company within that organisation. To this end, **ASFA recommends that where the administration for a superannuation fund (or RSE) is performed by a separate entity, APRA should also regulate that entity.**

- ASFA has had advice from third party administrators that they would like to be regulated by APRA. The feedback is that there are times when the administrators want to ask questions of APRA or enlist their assistance to solve an issue. However as APRA does not currently regulate these businesses, they do not have the ability to respond to such requests by advising the administrator to have the trustee ask the question.

Ratings agencies that rate superannuation funds

- There are a range of companies performing this service, and we are aware that some have Australian Financial Services licences and others do not.
  ASFA recommends that all superannuation ratings agencies should be required to hold an ASIC Australian Financial Services Licence, and be licensed as a principal.

Reporting to regulators

- An example of the inefficiencies that result from multiple regulators is the reporting of attempted or real identity fraud cases. The information needs to be lodged with AUSTRAC, ASIC, ATO and APRA, all of whom require the information in their own form, within the relevant reporting timeframe. Thus it can take several hours of repetitive input to report a single case. While there has been some alignment in reporting of breaches (now both have a significance test) each of APRA and ASIC require separate unique lodgements and depending on the nature of the breach the auditors may also have to lodge a notice. There is a risk that the industry will spend more resources on reporting rather than on prevention and rectification.

- We also note there is duplication of activities, as well as risks that issues may fall between the gaps and that dialogue and referrals between the regulators may not always be consistent. ASFA's view is that there is a need for a joint forum involving the four key regulators (and greater transparency to industry on the joint forum which has been established between APRA and ASIC).

Tax and prudential law inconsistency

- There is regulatory inconsistency with regard to what constitutes a 'superannuation interest' for the purposes of tax, disclosure, Family Law and prudential purposes. This can have implications for systems design and member disclosure and may give different outcomes depending upon fund structures. It also potentially leads to confusion and inefficiencies resulting from different providers (and members) having inconsistent views of the requirements.

- In a similar vein, there are complexities that have arisen with income streams and the distinction between capital and income for tax purposes and the nature of what constitutes an income stream for statutory/prudential purposes in the superannuation context. A review of these concepts given changing markets and policy environment is needed to ensure consistency of treatment and outcomes based on intended policy.

- Despite the joint forum between APRA and ASIC, there still appears to be evidence of many instances of duplication of reporting etc to the regulators (eg. breach reporting, reporting of fraud – also involving AUSTRAC and the ATO). With both AML and the SIS legislation having their own differing proof of ID requirements, it would make sense to align these and have only one set of rules.

- ASFA believes there should be one universal proof of ID regime (i.e. whichever of the two current ID requirements is most appropriate). Also, the proof of ID requirements should be removed or relaxed for rollovers between APRA regulated funds such that:

    - A superannuation fund should not have to re-verify any part of a member's identity if another APRA regulated fund has already verified that information. They should be able to rely on the other fund's verification.

- A standard form and standard industry process is required. ASFA is fully supportive of the recent landmark arrangement between AAS, Pillar and Superpartners in agreeing on a set of principles and protocols covering data and money flow for rollovers. This is a fantastic example of the industry participants coming together to overcome challenges faced by the industry to improve efficiency and reduce operational costs.

- Where a superannuation fund has received the agreed minimum required data and notification from another APRA regulated fund that the member's identity has been verified and the data items match, the fund should have to make the rollover payment without seeking further information from the member.

Regulation of Defined Benefits Funds

Legislation in recent years which has resulted in problematic or inappropriate application to defined benefit funds includes:

- Elements of the tax legislation relating to notional contributions and the multitude of uncertainties that arise in implementation.
- Calculation of the members' crystallised tax free components as at 30 June 2007.
- Corporations Act requirements in regard to the periodic reporting of costs and investment returns to members.
- The tax legislation relating to the caps on concessional contributions given that notional contributions again have to be allocated to individual members.
- The potential inability for a sponsoring employer to make contributions to a defined benefit plan that comprises only lifetime pensioners, and the potential inability of an employer to obtain a tax deduction for contributions made in these circumstances, are problems that need to be resolved.

Should you have any questions please contact our Manager of Government Relations & Policy Strategy, Khaldoun Hajaj.

Yours sincerely

David Graus
General Manager, Policy & Industry Practice

Appendix A

ASFA's Top 5 for the Cooper Review

ASFA provided comprehensive submissions to each of the three phases of the Cooper Review. We also took the unprecedented step of lodging a joint submission with AIST, IFSA and CSA in which we expressed concern regarding the Review Panel's proposed choice architecture. ASFA has provided a range of recommendations in each of our submissions to the three phases, however there are five key issues which we believe are the most critical to improving the superannuation system and, as a result, delivering enhanced retirement outcomes for fund members. These key issues are:

1. Choice architecture

There is growing recognition that the current regulatory framework is geared towards members who do not want to exercise investment choice (fund choice and investment choice are very different.) The current structure works when the vast majority of members default into a portfolio or rely on the trustee to set and manage the investment strategy. But that too is changing. There are three broad types of members emerging in both the pre and post retirement phases:

- Members who leave it to the trustee to make investment decisions - **the trustee chooses.**
- Members who want a limited choice of broad asset allocation portfolios, based upon their own time horizon and risk tolerance - **the trustee helps members choose**
- Members who are confident investors and who want to make full choice on their investment portfolio but still want to be part of a pooling arrangement - **the member chooses.**

Our current regulation does not support different types of members in either the accumulation or retirement stage, as it does not support trustees being subject to the direction of fund members. Hence the second group of member type is difficult to support and the third group is only supported in the SMSF regime. Cooper can fix this.

2. Legislative support for lifetime income stream products

A legislative framework that enables the industry to develop and provide "lifetime income stream products", as well as allow funds and members to invest "through retirement". The current legislative framework finishes at retirement.

3. Industry efficiency

Enabling efficiency and security throughout the industry and the reduction of multiple accounts. We need to remove impediments to using the TFN, the imposition of minimum data from employers, greater incentives for electronic transactions as well as a single rollover form/hub.

4. A set of standards and naming conventions for investment portfolios

This will assist members who want to make investment choice, so they can easily identify the risk of the portfolio. Risk descriptors such as a possibility for negative return one in five years can be set against whatever disclosure will make sense to members. Disclosure could be in the form of a "fire warning" for example. These standards must be accompanied with a defined set of asset management expenses that must be taken into account when disclosing risk rated investment returns.

5. Reviewing the framework around SMSFs

This includes naming conventions, licensing of accountants, raising of auditor standards and ensuring consumer protection provisions are in place. With the growing popularity of SMSFs, there are also emerging risks where the second or less sophisticated trustee members (often the female partner) could be disenfranchised.