



AUSTRALIAN INSTITUTE of
SUPERANNUATION TRUSTEES

Australian Financial Complaints Authority – Funding

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AIST Submission to AFCA

AIST

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the \$1.2 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.

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Executive summary

We welcome the opportunity to comment on the proposed Australian Financial Complaints Authority (AFCA) funding arrangements. The funding arrangements operate in three distinct phases being:

- Transition phase;
- Interim phase from 1 July 2018 to 30 June 2021; and
- A long-term phase commencing 1 July 2021.

Each phase will have a slightly different model and this submission will address concerns related to the transition and interim funding phases, however the principles remain relevant regarding the model for the long-term phase. We look forward to making an additional submission on the long-term phase closer to its commencement date.

We support a cost-recovery based funding model and believe it is essential that AFCA is appropriately funded to ensure they can provide an effective and efficient dispute resolution service to consumers and scheme members.

To ensure that AFCA will have the necessary resources to provide an effective dispute resolution service the funding arrangements must be developed according to the principles of equity, transparency and accountability.

If these principles are ignored there is a risk that AFCA will fail to deliver optimal outcomes and may result in super fund members contributing their retirement savings to a dispute resolution system that is not operating effectively and efficiently.

Key issues

Principles

AFCA is not a regulator or statutory entity however it has responsibilities to several stakeholders and its performance will have a material impact on consumers. Efforts must be taken to ensure that it operates effectively and that the funding arrangements are appropriate for its needs.

To ensure AFCA's funding arrangements are appropriate they must be developed according to a set of basic principles. The consultation paper notes the interim and long-term funding models have been developed with reference to ASIC RG267 and the principles of:¹

- Adequacy.
- Fairness.
- Avoiding cross subsidisation.
- Efficiency.

While these go some way to ensure the appropriateness of AFCA's funding arrangements the funding models should be based on a broader set of principles to ensure the models are effective and fair to all participants.

In 2014 the OECD developed a set of best practice principles for regulatory policy that are intended to assist countries in developing a policy covering the roles and functions of regulatory agencies, to provide confidence that regulatory decisions are made on an objective, impartial and consistent basis.²

While these principles are intended to apply to regulators they are relevant for AFCA because, like most regulators, AFCA has responsibilities to the Australian community and the ability to exercise legislative powers. It also needs to meet several legislated requirements some of which are to:³

- Ensure the complaints mechanism is appropriately accessible to persons dissatisfied with members of the scheme (including superannuation funds).

¹ AFCA Funding Consultation Paper. (2018). [online] p.9. Available at: <https://tinyurl.com/y6vfd7vc> [Accessed 12 Jul. 2018]

² OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators. (2014). [online] p.3; 97-101. Available at: <https://tinyurl.com/ycmehhcl> [Accessed 11 Jul. 2018].

³ *Corporations Act 2001 (Cth)* s 1051(3).

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- Ensure complaints against members of the scheme are resolved in a way that is fair, efficiency, timely and independent.

AFCA's status and role in achieving policy objectives means that it should, as a minimum, consider elements of the OECD principles where relevant.

Additionally, AFCA should also consider the Australian Government Charging Framework.⁴

One of the Charging Framework's objectives is to improve the consistency of charging activities and to support government entities in designing, implementing and reviewing their charging activities.⁵ While AFCA is not a government entity, it should be held to the same, or similar standards because it has a key role in the resolution of all financial sector complaints and a significant role and presence in the community. Thousands of complainants will rely on the services of AFCA to manage and resolve their complaints about financial firms. Some of these complaints can be about large sums of money, particularly within the superannuation context where total and permanent disablement and death payments can have lifechanging impacts. AFCA also exercises a range of legislative powers and if financial firms fail to comply with specific AFCA requests they can be subject to criminal liability.

As a minimum AFCA should adopt the following charging principles outlined in the framework:

- Transparency.
- Efficiency.
- Performance.
- Equity.
- Simplicity.

While AFCA is a non-commonwealth, private, not for profit corporation, the OECD principles and those in the Charging Framework are useful in ensuring that AFCA is appropriately funded.

This submission will deal with three of the essential principles drawn from the OECD and Charging Framework which are:

- Funding equity and cross-subsidisation.
- Financial transparency.
- Accountability.

⁴ Australian Government Charging Framework. (2018). [online] Available at: <https://tinyurl.com/y8s8r7kh> [Accessed 12 Jul. 2018].

⁵ Ibid.

Funding equity and cross-subsidisation

The Australian Securities and Investments Commission (ASIC) expects that AFCA's funding model should minimise cross-sectorial subsidisation to the extent practicable.⁶

We agree with ASIC's expectations however the funding model must go further and completely avoid any cross-subsidisation during all phases of funding. Each of the models requires superannuation funds to provide financial resources to AFCA and these will be drawn from members' retirement savings. It would be unacceptable, inequitable and unfair if a member's retirement savings were used to fund the resolution of disputes unrelated to superannuation, such as complaints against banks and financial advisers.

As each sector of the financial industry will be required to fund AFCA it is important that each does not pay more than their fair share.

Furthermore, there is both a moral and legal obligation upon superannuation trustees to ensure that members' superannuation monies held in trust are not used to fund the settlement of complaints in other areas of the finance sector.

The lack of transparency around the interim funding model and cost projections, as discussed below, makes it difficult to determine the risk of cross-subsidisation. We request that AFCA release detailed cost projections for each dispute resolution stream at a higher level to enable us to analyse the extent of cross-subsidisation.

Transparency

The OECD principles and the Government Charging Framework both highlight the importance of financial transparency when developing and undertaking activities that are funded through cost recovery.⁷

⁶ RG267 Oversight of the Australian Financial Complaints Authority. (2018). [online] Australian Securities and Investments Commission, p.30. Available at: <https://tinyurl.com/ya4muslx> [Accessed 12 Jul. 2018].

⁷ Australian Government Charging Framework. (2018). [online] Available at: <https://tinyurl.com/y8s8r7kh> [Accessed 12 Jul. 2018]; OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators. (2014). [online] p.3; 97-101. Available at: <https://tinyurl.com/ycmehhcl> [Accessed 11 Jul. 2018].

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Transition phase funding

The paper notes that AFCA expects the costs of transition to be approximately \$5.5 million and some of the transition funding will be collected through membership fees and the superannuation levy.⁸

However, the paper does not accurately detail:

- How much will be collected from each member type (FOS, CIO and superannuation funds)
- A breakdown of costs that have been incurred under the transition.

We request that AFCA release this information because without it we are unable to assess the proposals adequately.

Interim phase funding

We are concerned about the interim funding model. The paper outlines that a flat levy will be applied to superannuation funds totalling \$6.9 million for 8 months of operation in 2018-2019 and an estimated \$11.7 million for the 2019-2020 financial year.⁹

AFCA should provide a breakdown these figures to detail how the money will be allocated to their operations. As a minimum the following cost bases should be covered:

- Staffing
- Complaint handling
- Legal and compliance
- Audit
- Technology
- Communications

By performing a detailed breakdown AFCA will be able to accurately assess and, if required, revise their forecasting methodology. This exercise, and the learnings will be useful as they shift towards a long-term funding model.

⁸ Above n 1, 10.

⁹ Above n 1, 12.

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We request that AFCA prepare a cost breakdown by developing a document similar to a Cost Recovery Implementation Statement (CRIS). The Australian Government has released a CRIS template¹⁰ that contains many key questions and explanations that AFCA should endeavour to respond to, including:

- How the charging activity is costed.
- The main cost drivers.
- Assumptions that have been made.
- Sensitivity of cost estimates.
- Direct costs.
- Indirect costs.
- How direct costs are allocated to outputs.
- How indirect costs are apportioned to outputs.
- Cost apportionment between other funding sources.

This list is not exhaustive and while some of these matters have been addressed in the consultation paper, AFCA does not go far enough to give funds a clear insight into how their money will be allocated. AFCA must adequately disclose projected expenditure and a failure to do so will result in a departure from the principles set out by the OECD and the Australian Government Charging Framework.

Transparency is also necessary because of the trust structure under which funds operate. The use of members money by trustees is tightly regulated and trustees have a duty to ensure that expenditure is appropriate and in the best interests of their members. Trustees must be given visibility over AFCA expenditure to satisfy themselves that, by contributing to AFCA, they are acting in the best interests of their members.

It would be difficult to see how a trustee decision to fund AFCA would be in the best interests of their members if it turned out that some, or most of that funding went to the resolution of complaints unrelated to superannuation.

In addition to accurately detailing the expected costs of operation and disclosing these, AFCA also state how much the levy will be for superannuation funds. The paper says that they expect 137 trustees to share the funding responsibilities, but do not detail how much each fund will be required to pay. This information is essential to fully understand the proposals.

¹⁰ Cost Recovery Implementation Statement. (2018). [online] Australian Government. Available at: <https://tinyurl.com/yc9bzcwl> [Accessed 12 Jul. 2018].

We question whether AFCA's forecasts have considered the potential increase in complaints because of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

Long term funding

While it is anticipated that the long-term funding model will be implemented from July 2021 the principles detailed in this submission remain relevant. We believe once the model has been developed AFCA should undertake a post-implementation review of the model to determine the efficiency and effectiveness of the funding model.

AIST expects to comment on the long-term model closer to its implementation.

Accountability

As detailed above AFCA has a pivotal role in the dispute resolution framework and the financial services sector more broadly. Because of its standing, it must be seen to be acting with integrity and be held accountable for its actions, including cost recovery collection and expenditure.

AFCA is funded by industry and its ongoing operational costs are significant therefore there must be a mechanism for superannuation funds to assess the performance of AFCA against its stated objectives.

We believe that the most reasonable mechanism for funds to assess AFCA is for AFCA to develop and release a CRIS prior to each annual billing cycle and an annual statement following each cycle. This disclosure will enable funds to examine AFCA expenditure and understand fee allocation.

There is a balancing act between providing a detailed account of expenditure and efficiency. It would be appropriate to detail what areas of operations the money was spent on and this breakdown would also contemplate a split between the dispute resolution streams.

Funding model methodology

We understand AFCA does not wish to assess matters relating to superannuation levy calculation however it is essential to provide a high-level response.

AFCA has adopted an asset-based methodology for the interim funding phase however this should only be used as a temporary measure because a risk-based model is more appropriate. Further,

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we cannot comment on the proposed interim model due to limited transparency. AFCA must prepare a CRIS, or similar document, so that the model can be assessed fully.

Notwithstanding our concerns about the interim model, once dispute information becomes available the funding model should be reviewed and should transition towards a risk-based, long term model. Significant industry consultation is essential prior to the model being implemented in July 2021.

We support a risk-based model, and believe that relevant risk-related metrics could include:

- The number of complaints made against the scheme member.
- The amount of time or resources spent by AFCA in resolving complaints against the scheme member.
- The number of complaints resolved by the scheme member through their IDR processes.
- Whether the fund actively attempts to resolve member dissatisfaction prior to a complaint being lodged.

A risk-based model is beneficial for several reasons:

- It ensures that the superannuation industry does not subsidise other financial sector participants, as institutions will pay a fee in proportion to the number of complaints brought against them and the resources AFCA uses to resolve those complaints.
- It is an equitable model that minimises cross-subsidisation between superannuation participants and other financial services entities.

We look forward to preparing a further submission on the final model in the future. We would expect that during the model consultation phase AFCA would detail:

- How it determines the 'complexity' of a complaint, particularly because AFCA assumes that no super complaints will be resolved during registration or referral stage and all will go to case management or jurisdictional assessment.

Reform timeline flexibility

AFCA expects to consult on the long-term funding model prior to 1 July 2021, with the model to come into effect from 1 July 2021. In order to ensure effective consultation, stakeholders must be given ample time to comment on the proposed funding model.

Response to consultation questions

Question 1: Do you have any fundamental concerns with the high level three phase funding model approach, and if so what are they?

As detailed above we believe greater funding transparency and AFCA accountability is required. AFCA should have regard to these two principles throughout the development of the funding models and a failure to do so would decrease confidence in the scheme. It would also make it difficult to determine whether money has been allocated appropriately between dispute resolution streams and operational areas.

The model must also completely avoid (as oppose to minimise) cross subsidisation.

Question 2: Does the proposed interim funding model, including the levy for superannuation trustees, provide a reasonable approach to enable AFCA to establish an evidence base of complaint volumes and flows, and to inform any subsequent long-term funding model?

The interim funding model methodology is reasonable as a temporary measure only and it is impossible to determine whether the model itself is reasonable. This is because AFCA has not provided sufficient information about the breakdown of projected costs, nor how the superannuation funds contribution amount was set.

As detailed above, AFCA must prepare a CRIS, or similar, so that the model can be assessed fully.

Question 3: Do you have any comments on invoicing arrangements for superannuation trustees in relation to the superannuation levy? In particular, feedback is sought as to the preferred frequency of the invoicing of the superannuation levy for:

a. FY2018-19 (covering period 1 November 2018-30 June 2019). Invoicing could occur either:

- i. 100% on 1 November 2018, or**
- ii. 50% on 1 November 2018 and 50% on 1 March 2019.**

b. FY2019-20 (Covering period 1 July 2019 to 30 June 2020). Invoicing could occur either:

- i. 100% on 1 July 2019**
- ii. 25% on 1 July 2019, 1 October 2019, 1 January 2020 and 1 April 2020; or**
- iii. 50% on 1 July 2019 and 1 January 2020.**

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Where possible the invoicing arrangements should be aligned with the APRA Levy collection cycle. Further, a CRIS or similar document should be prepared prior to the invoice being sent to superannuation funds.

Question 4: Are there any other issues that require consideration?

Please see the 'Key Issues' part of this submission for a detailed analysis of outstanding issues.