



7 November 2018

Mr Alan Raine
Acting Committee Secretary
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Email: economics.sen@aph.gov.au

Dear Mr Raine,

Re: Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018

Thank you for the opportunity to provide our answers to the questions on notice following our appearance before the Committee on 1 November 2018 regarding the *Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018* ('the Bill').

Deficiencies where AIST views the regulators as being hamstrung by not having access to reports or disclosures

AIST is concerned that the Bill will not be effective, given the practical impossibility of the regulator being able to identify which of the 40,000 choices should be subject to the product intervention power.

Additionally, the regulators are placed in a difficult situation given that there is a lack of a level playing field regarding both disclosure and reporting to the regulators. Our key concerns are:

- A lack of dashboards for Choice products.
- APRA does not collect or publish statistics for Choice products.
This – and the lack of Choice dashboards – will also render a regulator assessment of member outcomes ineffective.
- Regulatory Guide 97 fee and cost disclosure has numerous carveouts which mean fees and costs cannot be compared.

Because carveouts to both disclosure and reporting requirements are systemic, we **enclose** a document which outlines the key carveouts - *At a glance – inconsistent treatment of choice superannuation products) October 2018*.

Whether product manufacturers are included within design and distribution obligations within the UK system

As AIST commented to the Committee, product manufacturers are included within the design and distribution obligations under MiFIDII, an EU requirement.

The EU has made it very clear as to why manufacturers were included:

‘The financial crisis has shown that there are instances where the application of conduct of business rules in the context of the provision of investment services to individual clients may be insufficient to ensure that firms fulfil their duty of acting in the best interests of their clients. Therefore, MiFID II, in Article 16(3) and Article 24(2), introduced product governance obligations for manufacturers and distributors. These obligations were further specified in Articles 9 and 10 of the MiFID II Delegated Directive, with the objective of enhancing the level of protection of investors by way of requiring firms to take responsibility, **from the beginning** (emphasis added), that products and the related services are offered in the interest of clients.’¹

The Financial Conduct Authority in the United Kingdom has made it clear that until a formal withdrawal from the EU has occurred, it is business as usual. This means that EU law such as MiFIDII will continue to apply.

UK Commentators have noted that it is possible that the UK may decide to keep the MiFIDII regime largely in place, especially given the ease this would give UK firms to access the EU market. The difficulties of the UK potentially not coming under MiFIDII requirements were recently outlined by the EU, and included such a lack of access to the EU market².

Treasury feedback regarding insufficient guidance, the triggering of market reviews, and ASIC intervention and timeliness

AIST has not had any specific Treasury feedback regarding these matters.

For further information regarding our submission, please contact Karen Volpato, Senior Policy Advisor at [REDACTED]

Yours sincerely,

[REDACTED]
Eva Scheerlinck
Chief Executive Officer

¹ ESMA (2017). Final Report on MiFIDII product governance requirements. ESMA. Available at <https://tinyurl.com/y9k5z4pa> [Accessed 7 Nov 2018]

² EU (2018). *Notice to Stakeholders – Withdrawal of the United Kingdom and EU Rules in the Field of Markets in Financial Instruments*. [online] Brussels: EU. Available at: <https://tinyurl.com/y8xeokdc> [Accessed 7 Nov. 2018].



AUSTRALIAN INSTITUTE of
SUPERANNUATION TRUSTEES

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.

At a glance



AUSTRALIAN INSTITUTE of
SUPERANNUATION TRUSTEES

Inconsistent treatment of choice superannuation products

October 2018

The following table summarises the numerous exemptions, gaps and inconsistencies afforded through the legislative environment to Choice superannuation products. This table builds on and adds to AIST commissioned research '*Gaps and exemptions in the regulation of superannuation – their scope, rationale and impact*', Ailsa Goodwin April 2017.

At July 2017, choice superannuation products cover approximately \$832 billion compared with approximately \$594 billion in MySuper.

(Note: FSRC = Financial Services Royal Commission)

DIFFERENT TREATMENT

PUBLIC COMMENTARY

IMPACT ON CONSUMERS

ONE

In the past, there were no explicit duties on trustees to promote the financial interests of beneficiaries, or apply a scale test for Choice products/investment options.

APRA has issued a member outcomes prudential standard to enhance and replace the scale test and which would include Choice products/investment options.

The Government's Bill which would legislate a member outcomes test is currently within the Senate and if passed unamended, would not include Choice products/investment options: *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No 1) Bill 2017*

According to APRA there are 120 MySuper products but over 40,000 member investment choices.

SuperRatings found substantial differences between fees for MySuper and choice products, particularly within retail superannuation funds – even when the underlying asset allocations were almost identical. <https://tinyurl.com/yal75ayt>

The Productivity Commission¹, noted funds should be required to report to APRA how many switch from MySuper to higher fee Choice; that the lack of data meant portfolios could not be benchmarked.

AIST advocates that the lack of comprehensive Choice disclosure or reporting means that it is difficult to gauge member outcomes for Choice products – even with a new member outcomes test.

The compounding effect of higher fees over long term reduces retirement incomes for members of choice products.

Choice overload baffles members.

The choice sector of the superannuation system is not achieving efficiencies of scale.

TWO

The Government deferred the requirement for choice dashboards in 2014, 2015, 2016 and 2017.

It plans to amend the law so funds would only need to produce dashboards for their 10 largest choice options.

The Super System Review, Financial System Inquiry, and the Productivity Commission have all concluded that the level of fees paid by members is too high.

SuperRatings criticises the poor level of disclosure of fees, noting there is still a long way to go to achieve comparability of fees across MySuper and choice products/investment options.

Members of choice products/investment options do not have a dashboard and so cannot easily compare their returns, fees or costs with MySuper products.

Under the Government's proposal, dashboards will not be required for most choice investment options.

1 Productivity Commission (2018). *Competition in the Financial System – draft report*. [online] Productivity Commission. Available at: <https://tinyurl.com/y8cf2j7o> [Accessed 29 August. 2018].

DIFFERENT TREATMENT**PUBLIC COMMENTARY****IMPACT ON CONSUMERS****TWO** *(continued)*

The draft PC Report notes that on average funds which charge higher fees do not deliver better returns, and ‘there are inconsistencies in how fees and costs are reported, despite regulator endeavour. ...This needs immediate redress by the regulators.’

THREE

APRA does not collect or publish statistics on choice products/ investment options equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.

APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.

AIST has advocated that sufficient data should be collected to enable the regulators (APRA at system and fund level and ASIC at product level) to benchmark whether good value is being delivered to members and to identify adverse impacts of conflicts of interest.

Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of choice products/ investment options.

Lack of data hampers this.

FOUR

No requirement to ensure switching funds is in the best interests of the member when giving general advice or under no-advice business models.

ASIC accepts EUs from CBA and ANZ regarding distribution of super products through branches².

ISA analysis³ of Roy Morgan research found an increase in cross-selling retail superannuation using general advice and no-advice business models.

Members are switched from a MySuper product to an inferior choice product/investment option, when it is not in the best interests of the member.

FIVE**Regulatory Guide 97 – platforms**

New fees and costs disclosure under Regulatory Guide 97 fee and cost disclosure requirements do not apply to superannuation held via a platform.

Mr Darren McShane⁴ recommends changes to help members understand platform aggregated costs and undertaking a review of platforms to determine if value is being delivered (similar to UK).

According to Rainmaker, over 70 per cent of retail superannuation assets in Australia are held via platforms.

According to the UK Financial Conduct Authority, platforms add 20-90 basis points to costs.

Disclosure for superannuation held via a platform understates fees and costs paid by the member.

ASIC admits it would be misleading to compare the fees and costs of platforms and non-platform superannuation funds.

The compounding effect of higher costs over long term reduces retirement incomes for members.

SIX (and see point four)

The (unimplemented) dashboard regime for choice products/ investment options will not include platforms.

While the Government amended the regime to require dashboards for products/investments held via a platform, platforms themselves will be exempt.

Members who hold their superannuation via a platform will not have a dashboard for it, compounding an existing difficulty comparing their returns, fees or costs with MySuper products.

SEVEN

APRA does not collect or publish statistics on platforms equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.

APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.

Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of superannuation held via a platform. Lack of data hampers this.

2 <https://asic.gov.au/about-asic/media-centre/find-a-media-release/2018-releases/18-206mr-asic-accepts-court-enforceable-undertakings-from-cba-and-anz-over-superannuation-product-distribution/>

3 <http://www.industrysuperaustralia.com/assets/MediaRelease/160904-The-Hard-Sell.docx.pdf>

4 McShane, D. (2018). Review of ASIC Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements Report to the Australian Securities and Investments Commission. [online] ASIC. Available at: <https://tinyurl.com/y7l82sho> [Accessed 15 Aug. 2018].

DIFFERENT TREATMENT**PUBLIC COMMENTARY****IMPACT ON CONSUMERS****EIGHT**

No requirement to produce a shorter PDS for legacy products.

According to Rice Warner, around 30% of personal superannuation assets are held in legacy products.

This makes it difficult for members in legacy products to compare the performance, fees or costs of the product with a contemporary product, understand the exit costs and assess whether they would be better off switching to a contemporary product.

NINE (and see point four)

The (unimplemented) dashboard regime for choice products/ investment options will not include legacy products.

Rice Warner found fees and costs for legacy products are on average more than double those for contemporary products. UK Independent Project Board found £26 billion in legacy pension schemes had investment manager fees above 1%, with nearly £1 billion exposed to fees over 300 basis points per annum.

Members who hold legacy superannuation products will not have a dashboard, making it difficult to compare their returns, fees or costs with contemporary products.

TEN

APRA does not collect or publish statistics on legacy products equivalent to the comprehensive statistical collection derived from the MySuper reporting standards.

APRA deferred collecting data for choice products/investment options for consideration during the development of the requirements for choice dashboards.

Members rely on APRA, employers, advisers, Government, researchers, commentators and trustees to analyse the characteristics and performance of legacy products. Lack of data hampers this.

ELEVEN

Conflicted remuneration is banned for most of the financial services industry, but there is an exemption for advice about retail life insurance.

In 2017, ASIC sets commission caps and clawback amounts⁵. In 2014 ASIC found more than one third of advice about retail life insurance reviewed did not comply with the law. 96% of non-compliant advice was given by advisers paid an upfront commission.

Consumers are at significant risk of being recommended a life insurance policy that is not in their best interests. Industry and Government proposals to address this do not include banning commissions.

TWELVE

Grandfathered commissions permitted under FoFA.

AIST has advocated these should be banned as they may encourage advisors to keep clients in legacy products rather than moving them to better products. ASIC has called for an end to grandfathered commissions.

Consumers are at a significant risk of being recommended to stay in a product which is not in their best interests.

THIRTEEN (see also point two – these two things deferred in sync)

Portfolio Holdings Disclosure deferred four times 2014, 2015, 2016 and 2017.

Consumers unable to see individual holdings for their super investments.

FOURTEEN

Product design and distribution obligations. Product distributors and manufacturers would be exempted if the Bill is passed.

The complete chain of product manufacturers and distributors should be included to ensure ownership; the focus on individual products is meaningless given the systemic carveouts from the legislative framework and the lack of data to assess system/fund value; the proposals are out of sync with MIFIDII requirements which include the complete chain.

This proposal would require entities issuing PDSs to undertake a target market assessment and would provide ASIC with product intervention powers to remove unsuitable products, including choice products but not legacy products.

FIFTEEN

Government's Protecting your super package, which would cap fees for low account balances and ban exit fees.

The proposals do not include sell spreads in the calculation of exit fees (buy/sell spreads are generally applied in the retail fund sector) – this exclusion enables gaming.

The possibility of fee gaming would adversely impact members.

5 <https://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-168mr-asic-releases-instrument-setting-the-commission-caps-and-clawback-amounts-as-part-of-the-life-insurance-advice-reforms/>