

5 December 2013

Head of Secretariat Financial System Inquiry The Treasury Langton Crescent PARKES ACT 2600

Email: fsi@treasury.gov.au

Dear Sir/Madam,

### Financial System Inquiry – Draft Terms of Reference

The Australian Institute of Superannuation Trustees (AIST) welcomes the opportunity to comment on the draft terms of reference for the Financial System Inquiry (the Inquiry).

AIST is an independent, not-for-profit professional body whose mission is to protect the interests of Australia's \$500 billion not-for-profit superannuation sector. AIST's members are the trustee directors and staff of industry, corporate and public-sector superannuation funds, who manage the superannuation accounts of two-thirds of the Australian workforce.

In summary, we recommend that the Inquiry's focus include:

- Methods for setting a series of key superannuation benchmarks (Retirement Adequacy, System Sustainability, and Longevity Index) which would assist with providing greater certainty and transparency to the Australian superannuation system;
- Appropriate regulation of all sectors of the superannuation system;
- An examination of the potential impact of Self-Managed Superannuation Fund failure on funding the age pension;
- Provision of retirement products which remove barriers to annuities;
- An examination of whether increased superannuation disclosure has aided member comprehension or their capacity to compare superannuation funds;
- Methods for ensuring that the imposition of Government levies upon the Australian financial sector are consistent, transparent and promote the efficient allocation of resources;
- Collection of superannuation information by the regulators to ensure whole of sector reporting and comparability;
- When examining the financial system's contribution to Australia's productivity growth, commenting on methods for tracking and reporting on the concentration of wealth within both Australia's financial systems as well as the general population;
- That a superannuation expert be included on the Inquiry panel;



- Measures to encourage and enhance the diversity of capital funding in Australia; and
- Investigation of the appropriateness of financial services practitioner qualifications in the context of systems integrity and consumer priotection.

We include further detail below, together with our recommended additions to the Draft Terms of Reference (Annexure A).

In particular, AIST would be very pleased to make recommendations as to specific individuals who could make a significant contribution to this Inquiry.

If you have any further questions regarding this submission, please contact David Haynes, Executive Manager, Policy & Research on 03 8677 3803 or at <a href="mailto:dhaynes@aist.asn.au">dhaynes@aist.asn.au</a>.

Yours sincerely,

Tom Garcia

**Chief Executive Officer** 



# Tracking and transparency to underpin a well-functioning financial system

AIST recommends that the Inquiry examines the establishment of a nationally accepted benchmark of what is an "adequate retirement", how the sustainability of the superannuation system can be tracked, and set a method for tracking the impact of longevity issues.

AIST submits that there are three key drivers to a well-functioning retirement financial system:

- Adequacy of the retirement benefit
- Sustainability of the retirement benefit
- The management of longevity risks.

While there are various definitions of "adequate" superannuation in use, none drive policies such as contribution levels or lump sum tax.

AIST recognises that the need for adequacy needs to be balanced against sustainability of the Australian superannuation system. AIST supports a national definition of "sustainability" being developed (Sustainability Benchmark). The Sustainability Benchmark could be used to:

- Set a measure for whether the current superannuation system is sustainable in the long term, thereby providing greater certainty for policy making.
- Examine any proposed changes to the superannuation system against the Sustainability Benchmark.

AIST notes the impact of increasing longevity on the Australian superannuation system. A Longevity Index could assist with understanding the changing costs for those who wish to fund their retirements and, in particular, examines changing interest rates, inflation and longevity risks and assists with building markets to help manage longevity risks.

### Management of systemic risk

AIST recommends that the Inquiry examines the impact of failure of Self Managed Superannuation Funds on the funding of the Age Pension.

A feature of past financial system reviews was to examine major changes since the last review. One such major change is the growth of Self Managed Superannuation Funds (SMSFs). Since June 2000, the amount of retirement moneys within SMSFs has grown from \$74.9 billion to \$531.5 billion in September 2013.

AIST recognises the usefulness of SMSFs to sectors of the Australian population. However, given that SMSFs are now a significant component of the Australian retirement system, an examination of the regulation of SMSFs as well as systemic risk would be timely.



#### Remove barriers to annuities

### AIST recommends that the Inquiry examines the removal of barriers to annuity products

AIST advocates that where appropriate, the legislative and taxation environment for retirement products and various sectors within superannuation must be on an equal playing field.

AIST supports a review of the legislative framework for Annuities (forming part of the Post Retirement and Superannuation Sustainability Review), so that members are incentivised to take up all or part of their retirement benefit as an annuity. In so saying this, AIST recognises that members with amounts lower than the "Adequacy Benchmark" should not be penalised for taking part or all of their benefits as an annuity.

# Is increased disclosure informing members and improving comparability and comprehension?

AIST recommends that the Inquiry examines whether the ever-increasing volume of disclosure has helped members

Disclosure within the financial system (and superannuation in particular) is driven by many purposes such as managing organisational risk, aiding consumer awareness, and assisting comparability of products.

In the end, it is the member of superannuation funds who is the most directly affected.

# Transparency and efficiency in raising financial sector levies

AIST recommends that the Inquiry examines transparent and efficient methods for raising levies which are imposed on the financial sector

AIST submits that because hundreds of millions of dollars are raised each year from the superannuation sector, a transparent and efficient way of disclosing the composition of the levies be examined.

# Whole of superannuation sector data collection and comparability

AIST recommends that the Inquiry examines whole of superannuation sector reporting and comparison for both system integrity and consumer protection.

AIST submits that all sectors of the superannuation industry should provide regulators with regular information and reports.



# Tracking concentrations of wealth in financial sector

AIST recommends that the Inquiry examines methods for tracking and reporting on concentrations of wealth both within Australia's financial system as well as the general population

AIST submits that tracking these issues is important in understanding the productivity of Australians, and the financial rewards which that can bring. It is also important from a financial organisation perspective, to ensure that sufficient competition remains within the marketplace.

# Superannuation expertise on the Inquiry panel

AIST recommends that the Inquiry panel includes someone with superannuation expertise

Australian superannuation assets total \$1.7 trillion, and bank assets total \$2.7 trillion. While both of these parts of Australia's financial sector are large, they have very different focal points. Superannuation is a long term savings mechanism of a (basically) non day-to-day nature. Banking is of a day-to-day transactional nature. The viewpoint of both superannuation organisations, and the members it represents, are very different to banking organisations.

AIST would be very happy to make recommendations as to individuals who would make a significant contribution to this extremely important Inquiry.

### Measures to enhance diversity of funding

AIST recommends that the Inquiry panel consider measures to enhance the diversity of capital funding in Australia.

Business ventures in Australia require funding from a variety of sources and in a number of different forms. AIST notes that superannuation funds are representing an ever increasing source of investment funds, with investors themselves having different risk and investment time horizon profiles to funds sourced elsewhere, such as the banking or investment banking sector. This, in turn, can fund different business ventures.

AIST recommends that this diversity of funding should be encouraged, with steps taken to encourage innovation in this area.



# **Appropriateness of practitioner qualifications**

AIST recommends that the Inquiry panel considers the existing qualification requirements for professionals in financial services from a perspective of systems integrity and consumer protection.

AIST maintains that professionals who work in financial services should be appropriately qualified in order to ensure a consistency of knowledge and skill, as well as integrity when consumers deal with such practitioners. AIST would support a thorough investigation of what might be considered to be appropriate in this context.



#### Annexure A

AIST has included additional recommended terms of reference for consideration.

These additional terms of reference are <u>underlined</u> for ease of reference.

# Financial System Inquiry – Draft Terms of Reference

# **Objectives**

The inquiry is charged with examining how the financial system could be positioned to best meet Australia's evolving needs and support Australia's economic growth.

Recommendations will be made that foster an efficient, competitive and flexible financial system, consistent with financial stability, prudence, integrity and fairness.

### **Terms of Reference**

- 1. The Inquiry will report on the consequences of developments in the Australian financial system since the 1997 Financial System Inquiry and the global financial crisis, including implications for:
- 1.1. how Australia funds its growth;
- 1.2. domestic competition and international competitiveness; and
- 1.3. the current cost, quality, safety and availability of financial services, products and capital for all end users.
- 2. The Inquiry will refresh the philosophy, principles and objectives underpinning the development of a well-functioning financial system, including:
- 2.1. balancing competition, innovation and efficiency, with stability and consumer protection;
- 2.2. how financial risk is allocated and systemic risk is managed;
- 2.3. assessing the consequences of financial regulation, including its impact on compliance costs, flexibility, innovation and financial services trade;



- against systemic risks (e.g., by recognizing the pivotal value of the superannuation sector in holding national wealth, nation building, & providing financial stability to the overall financial system);
- 2.5. the role of Government; and
- 2.6. the role, objectives, funding and performance of financial regulators <u>as well as the scope</u> and public policy implications of prudential regulation of financial products.
- 3. The Inquiry will identify and consider the emerging opportunities and challenges that are likely to drive further change in the financial system, including:
- 3.1. the role and impact of new technologies, market innovations and changing consumer preferences and demography;
- 3.2. international integration, including international financial regulation;
- 3.3. changes in the way Australia sources and distributes capital, including the intermediation of savings through banks, non-bank financial institutions, insurance companies, superannuation funds and capital markets;
- 3.4 how to track and report on concentrations of wealth both within Australia's financial system as well as the general population;
- 3.5. changing organisational structures in the financial sector;
- 3.6. <u>assessing the potential risk of the rapid growth of the superannuation system of Self</u>
  Managed Superannuation Funds on the funding of the age pension;
- 3.7 whether the increased volume of disclosure within the financial system has aided Australian's comprehension of financial system issues which affect them;
- 3.8 corporate governance structures across the financial system and how they affect stakeholder interests; and
- 3.9. developments in the payment system.
- 4. The Inquiry will recommend policy options that:
- 4.1. promote a competitive and stable financial system that contributes to Australia's productivity growth;
- 4.2. promote the efficient allocation of capital and cost efficient access and services for users;



- 4.3. support individuals and businesses to be reasonably able to manage their finances by understanding risks and rewards in the financial sector;
- 4.4 examine establishing a nationally accepted benchmark of what is an 'adequate retirement', how the sustainability of the superannuation system can be tracked, and set a method for tracking the impact of longevity issues on the Australian population;
- 4.5 promote transparent and efficient methods for raising levies which are imposed on the financial sector;
- 4.6 examines the whole of financial sector reporting from the viewpoint of both systems integrity and consumer protection;
- 4.7 support financial services businesses by examining the appropriateness of practitioner qualifications from the viewpoint of both systems integrity and consumer protection;
- 4.8. foster dynamic and innovative financial service providers; or
- 4.9. relate to other matters that fall within this terms of reference.
- 5. The Inquiry will take account of the regulation of the general operation of companies through corporations law to the extent these impinge on the efficiency and effective allocation of capital within the financial system.
- 6. The Inquiry will examine the taxation of financial arrangements, products or institutions to the extent these impinge on the efficient and effective allocation of capital by the financial system, and provide observations that could inform the Tax Policy White Paper.
- 7. In reaching its conclusions, the Inquiry will take account of, but not make recommendations on the objectives and procedures of the Reserve Bank in its conduct of monetary policy.
- 8. The Inquiry may invite submissions and seek information from any persons or bodies.
- 9. A final report is to be provided to the Treasurer by 1 November 2014, following an extensive period of consultation. Consultation will include the publication of an interim report that communicates the Committee's predispositions, allowing adequate time for interested persons or bodies to provide input to the final report.