AUSTRALIAN INSTITUTE of SUPERANNUATION TRUSTEES

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Post-Implementation Review of the Prudential Framework for Superannuation: Data and Reporting Framework

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AIST Submission to APRA

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Post-Implementation Review:
Data and Reporting Framework

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 $1.3 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

In brief:

AIST believes that the reporting framework does not presently meet its objectives and APRA needs to change its focus to include members' best interest. Reporting standards do not enable system performance assessment and AIST calls for a comprehensive data and reporting framework to be implemented, with a specification of what is needed to benchmark system performance.

AIST wishes to thank APRA for engaging the industry in this consultation. We support this opportunity to ensure that there is a common benefit to the industry, consumers and other stakeholders. The biggest question underpinning the reporting framework is whether the collection and analysis of data and actions subsequently taken has delivered good value to government, regulators, industry and consumers. For example, the current reporting framework has not delivered benchmarking of system and fund performance, enabled the identification of the impact of conflicts of interest, or whether members could have received better value. Our submission accordingly advocates that the reporting framework has not met its objectives.

This submission will remain mostly at a high level, together with several efficiency improvements.

We will examine five key areas in this submission:

- **Objectives** - the reporting standards do not meet the objectives.
- **Implementation** – system performance benchmarking and assessment has not been enabled and a data reporting framework is needed.
- **Implementation** - data quality is poor given that the data gathered does not enable the standards to meet their objectives. Consistent terminologies and uniform methodologies across funds is needed. A fundamental component of the standards not meeting its objectives is that neither disclosure or data reporting is on a level playing field across the system.
- **Royal Commission** - identification of concerns identified by the Royal Commission could have been identified sooner had APRA gathered and analysed appropriate data.
- **Timing of this post implementation review** – we repeat our earlier recommendations that there be a further post implementation review following the final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry ('Royal Commission') and Productivity Commission, and one which also considers other recent APRA reviews and initial industry feedback.

Regarding these five key areas, our chief concerns are:

- **Objectives are not being met** - The scope of the review is too narrow to address this, with a variety of stakeholders, fields, forms and reporting standards reflecting issues not strictly limited to the prudential framework.
    - The review should go further and embed the best interests of members in a revised measure of APRA's success. Currently, APRA's measurement of 'loss' relates to immediate failure or financial loss of regulated entities and does not include loss to member value arising from entities not acting in members' best interests. The Productivity Commission's final report[1] makes similar recommendations.
    - AIST strongly believes that government, industry, superannuation fund members need to understand whether appropriate value is being delivered to members, given the complexity and cost associated with data reporting.
    - Had the reporting framework been meeting its objectives, the issues raised by the Royal Commission could have been identified sooner.
- **Implementation -** A fundamental starting point is a well-conceived data and reporting framework. This is not in place.
    - Information needed to benchmark system performance should be specified. Benchmarking cannot be done. AIST has raised this on many occasions, and Productivity Commission's final report also raises this concern. Without this key information, AIST believes that other regulatory requirements such as the member outcomes test cannot be implemented meaningfully.
    - Consistency of terminology and uniform methodologies need to be developed within a data and reporting framework.
    - Funds are experiencing uncertainty regarding APRA's understanding of superannuation data and uncertainty regarding data fields.
    - The data and reporting framework must rest on a level playing field disclosure and reporting regime. This is currently not the case (For a summary, please see (http://www.aist.asn.au/media/1258881/annexure_-_disclosure_and_reporting_carveouts_oct_2018.pdf).
- **Timing** – The review needs to consider the findings of the Royal Commission and reports which APRA has undertaken.

While our overall concern is that the objectives have not and cannot be met, we have nonetheless provided some example comments about the current reporting standards.

[1] Productivity Commission (2019). *Superannuation: Assessing Efficiency and Competitiveness,* Report no. 91. [online] Canberra: Productivity Commission. Available at: https://tinyurl.com/y9ylxoll [Accessed 16 Jan. 2019].

We make the following **recommendations** as part of this submission:

1. A further post implementation review should take place following the final reports of both the Productivity Commission and the Royal Commission.
2. The further review should have a broader scope.
3. APRA should gather choice sector data.
4. An independent agency such as the Australian Bureau of Statistics (if resourced) should analyse and benchmark both MySuper and choice sector data and report to APRA.
5. A data reporting framework needs to be developed.
6. What data is needed to benchmark fees and performance needs to be specified.

Reporting standards objectives

We are concerned that the review's focus is too narrow by examining whether the framework supports meeting the objectives of the prudential framework. Our member funds have several concerns that the reporting framework is designed not to merely underpin the prudential framework, but also gather information for a number of stakeholders where APRA may not be the primary user. Given the lack of a data reporting framework (which we examine in point 2 below), this leads to ambiguities, inefficiencies and differing interpretations.

To compound this, legislation presently in front of Parliament to legislate the proposed outcomes test may require a thorough overhaul of the reporting framework to ensure that APRA is able to carry out its role effectively.

AIST welcomes APRA's willingness to consider changes, where the existing framework can be improved from an effectiveness or an efficiency perspective. We applaud this, although we believe that opportunities to do this may be limited, if only the perspective of supporting the prudential framework is being considered.

Reporting standards objectives have not been met

The objectives of the prudential standards focus on clarity, certainty, alignment of the prudential framework with other parts of the prudentially regulated financial sector where appropriate, and enhanced data collection and publication to promote the increased transparency on the industry. The objectives of the reporting standards underpin the prudential standards objectives.

AIST strongly contends that the objectives of the prudential standards have not been met. The corollary is that the objectives of the reporting standards also have not been met:

- There is a lack of data regarding the choice sector. This means there is not 'increased transparency on the industry'.
    - Rice Warner has estimated that there are over $1 trillion funds under management in the choice sector.
    - The Productivity Commission's final report highlights that the choice sector underperforms. Data is needed to understand the cause of this underperformance.
- Given that the Productivity Commission has recently handed down its final report, and that the final report of the Royal Commission is likely to criticise the lack of focus on retail funds (and choice products), it is critical that APRA gathers, analyses, and benchmarks choice performance.
- AIST has long advocated that it is APRA's role to analyse and benchmark the performance of both MySuper and the choice sector. The Productivity Commission's final report also

refers to the need to benchmark performance, and how this would enable APRA to identify underperforming funds.
- The systemic carveouts from the legislative and regulatory environment (including the lack of choice data) all mean that neither the prudential nor reporting standards can deliver transparency or consistency. We enclose a summary of key carveouts (Annexure A).

The essential question when examining whether the reporting standards have delivered is whether either APRA, superannuation funds, or superannuation fund members can clearly say whether either the system at high level or individual funds have delivered fair value.

Impact of Royal Commission and Productivity Commission reports demonstrates AIST advocacy

The Productivity Commission's final report (and indeed their entire review process) has been critical of the value for money and comparability provided in the choice sector of superannuation. In their final report, the Productivity Commission found that there is a wide variation in performance in the choice sector that is not explained fully by asset allocation. More publicly available data from APRA may assist inquiries such as this.

AIST has long supported APRA's original idea of an online data dissemination tool that could be used to provide stakeholders with flexible use of the available data. We believe that it is an appropriate role of the regulator to be subjecting the industry to as much public scrutiny as possible and believe that such a device would allow stakeholders to have this degree of scrutiny. We are concerned that this idea, which we believe to be vital, has been progressively prioritised downwards with no signs that this will be reviewed. This is regrettable.

The recent release of the Productivity Commission's final report and the pending final report from the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the "Royal Commission") may reveal issues that are unaddressed by this review. In August 2018, AIST wrote to APRA's chair Wayne Byres noting that the review of prudential standards (as explained in the Regulation Impact Statement) was to 'ensure that they continue to reflect good practice and remain relevant and effective'. We explained that this aim is unable to be met unless the recommendations from the Royal Commission, and the prudential inquiry into the Commonwealth Bank of Australia, are considered as part of conducting this review. Whilst our comment was made in the context of the review of the prudential framework, we believe that this statement is just as accurate for the broader reporting framework, including the parts of the framework which do not underpin the prudential framework. Consequently, we re-state our position that this review is premature, and that conclusion of this review should be deferred until both the final report from the Royal Commission is completed, and the CBA prudential inquiry is mapped to the current coverage of the prudential standards.

AIST would support a holistic review of the reporting framework to ensure that all present and future needs are met. We believe that this must involve all stakeholders, including government agencies who may be additional users of data collected.

Recommendation 27 in the Productivity Commission's final report includes the establishment of a permanent superannuation data working group. AIST believes that this is a concept well worth considering in the quest for placing a focus on member outcomes, evaluating the value delivered to superannuation fund members, the Government, regulators and other stakeholders.

Bringing members' best interest into the scope of both prudential and reporting standards

The Royal Commission has highlighted many cases where members' best interest was not the applied test. APRA presently uses measures which focus specifically upon providers in the industry and whether consumers have incurred losses. This involves measures such as the Performing Entity Ratio (PER), which measures the degree to which regulated entities have not incurred failure, as well as the Money Protection Ratio (MPR), which measures the degree to which liabilities to beneficiaries in the financial sector are affected by losses due to prudential failure.

These measures, presently at a laudable 99.93% and 99.97% repetitively, may not be as appropriate to the superannuation sector. Superannuation is a mandatory system, where the retirement savings of consumers are at risk of not receiving fair value.

The measures fail to capture, for example, the costs of choice superannuation products compared to MySuper products, which in research for AIST, Rice Warner estimate as costing superannuation fund members $53 billion over the next 10 years[2]. This is costed by Rice Warner as 3% of GDP, more than an entire year of Age Pension outlays, but will not form part of these ratios.

Recommendation 23 of the Productivity Commission's final report includes that the Australian Government should set an explicit 'member outcomes' mandate for APRA in its regulation of superannuation. AIST highlights that this can only happen if a proper reporting framework is in place.

[2] Rice Warner (2018). *Analysis – MySuper vs Choice*. 11 September 2018. [online] Melbourne: Australian Institute of Superannuation Trustees. Available at: https://tinyurl.com/y9dps4ue [Accessed 14 Dec. 2018].

Implementation of the reporting framework

The need for a comprehensive data reporting framework

The absence of a true reporting framework means that there is insufficient information to assess the performance of the superannuation system. This is a major omission in APRA's prudential framework for superannuation.

An objective of data reporting is to support APRA's prudential supervision and provide appropriate transparency and disclosure. Disclosure requirements and reporting standards are primary mechanisms for improving transparency and accountability of APRA regulated funds.

While APRA has referred to a reporting framework in this consultation, this 'framework' is merely a list of the Superannuation Reporting Standards RSEs are required to comply with. APRA information about the 'framework' is entirely technical and operational in nature.

While the reporting standards may provide some useful information about the operation of the system, they are not tied to any benchmark assessment of system performance, nor does any such benchmark currently exist.

A comprehensive data reporting framework must articulate what information is needed to benchmark system performance and articulate how this information supports an assessment of system performance and whether members' needs are being assessed.

There is no APRA policy framework that articulates the purpose for the provision of reporting requirements (either separately or jointly), and which high-level or long-term information requirement or policy objective each requirement supports.

Policy objectives about the need for the accessibility, consistency and reliability of information needs to be specifically articulated and incorporated into an APRA policy framework for reporting.

APRA has raised numerous concerns about the nature, reliability and completeness of data but its actions about this have not always been undertaken or completed, and there is a further need to bring these concerns, clarifications and requirements together in a reporting framework. The framework also needs to settle consistent terminology and uniform methodologies to ensure consistency and comparability and benchmarking of data.

In some instances, however, it is even questionable if all of the information reported and disclosed is accurate, useful or meaningful to APRA or a consumer. The adverse consequences of not having a coherent reporting framework is illustrated below by reference to a number of ongoing reporting issues.

Standard Risk Measure

The Standard Risk Measure, for example, requires funds to report on their MySuper product dashboard and in their reporting to APRA the likely number of negative annual returns over a 20-year period. However, it does not provide members with information about the likely magnitude or path of negative returns, or their timing, and also implies that cash is the best is the long-term investment.

AIST, Rice Warner, the Actuaries Institute and others have consistently raised these issues with APRA but a better metric for reporting and displaying long-term investment risk has not been developed and does not appear to be in contemplation. Some funds (such as AustralianSuper) have developed enhanced displays of long-term investment risk but these are not comparable across industry.

This gap in the reporting standards would have been identified and addressed in a comprehensive policy framework for reporting.

Fees and costs

APRA has made many comments about the need to improve the accessibility, consistency and reliability of information that is reported to APRA, that AIST broadly supports.

Similarly, AIST also supports APRA identifying the need for greater consistency of reporting of the underlying costs associated with running a superannuation fund to be able to meaningfully assess the relative efficiency (or otherwise) of different RSEs and the impact of fees and costs on the outcomes for members.   There is inconsistent reporting on investment costs across funds with some funds not reporting all of costs embedded in investment returns (rather than reflected in disclosed fees).

However, these issues should be addressed, and outcomes should be made consistent with objectives specifically included in an APRA policy framework for reporting.

SMSFs

APRA does not generally have responsibilities for the SMSF sector, meaning that the information reported to it is not sufficient to assess the overall performance of the superannuation system. This is further complicated by the ATO using different methodologies and requiring different reporting practices for SMSFs.

AIST recommends that an ATO/APRA cross-agency taskforce be established to ensure greater alignment between the SMSF and APRA regulated sectors, and for this greater alignment to be reflected in an APRA data reporting framework.

Data quality

AIST strongly contends that reporting standards data quality cannot be good since the data does not meet the prudential or reporting standards objectives. We have outlined this major concern earlier. AIST calls for a review of the current reporting standards.

AIST also believes that the reporting standards data quality does not meet the OECD definitions of data 'quality'. The OECD[3] defines data 'quality' as 'fitness for use' and goes onto comment that the concept of *quality* includes relevance, accuracy, credibility, timeliness, accessibility, interpretability, and coherence.

Apart from the key criteria of relevance, AIST believes that the reporting standards data also does not meet the other OECD criteria:

- The data is not accurate, credible, coherent or capable of being easily interpreted, given the substantive lack of comparability and transparency. Various legislative and regulatory carveouts and lack of clarity impact on accuracy: examples include RG97, the lack of a taxonomy, the lack of Choice data.
- The data is not timely.
- The data is not easily accessible or useful for industry.

Nonetheless, AIST has consulted with its member funds to identify key concerns with data quality. We emphasise that our comments below are within the narrow context of the current reporting standards and forms.

APRA's understanding of the data

Our member funds have drawn attention to several key concerns regarding APRA's understanding of the data requirements:

- It is very difficult for either funds or their custodian to gain a clear interpretation of the forms from APRA. Because of this, custodians are sometimes required to re-lodge information over multiple periods.
- Many APRA queries seem to be derived from percentage or dollar movements from period to period. APRA provides little or no context around queries. This does not assist funds in providing data.

[3] OECD (2011). *Quality Framework for OECD Statistical Activities*. [online] OECD. Available at: https://tinyurl.com/y9a67cpm [Accessed 12 Dec. 2018].

Issues with the current forms

Our member funds have raised the following key concerns.

Timing –28 calendar day requirement adversely impacts days covered

This requirement can be impacted by how the weekends and public holidays are distributed across the quarter. It can significantly change the number of business days covered by the report. AIST recommends that the requirement to submit should related to 28 business days rather than calendar days.

Duplication of reporting – annual and quarterly

The requirement to submit both annual and quarterly reports is inefficient and costly.

AIST recommends that the year-end quarter reporting be removed and have annual APRA reporting forms. This recommendation would have the following benefits:

- Considerable cost savings. Funds have estimated that the duplication of effort costs funds at least $30k per fund – which calculated across 130 superannuation funds would deliver cost savings of nearly $4million.
- Removal of the overlap of data points across SRF 160,1 Defined Benefit Member Flows, SRF 320.0 Statement of Financial Position, SRF 330.0 Statement of Financial Performance, SRF 410.0 Accrued Default Amounts, SRF 530.0 Investments, SRF 531.0 Investments Flows, SRF 532.0 Investment Exposure Concentrations, SRF 533.0 Asset Allocation.
- Better quality reporting because most data points within the year-end quarter reporting are estimates and information is more readily available to meet the annual reporting timeframes. Additionally, annual reporting provides for greater governance oversight than year-end quarter, given the Risk Management Declaration process. Also, some annual form data is independently audited.

Field data ambiguities and inconsistencies

Our member funds refer to ‘constant feedback from staff’ regarding the lack of clarity and inconsistencies in the instructions supporting the forms and data fields. Our member funds have developed worked examples to try and assist their staff. Our member funds are also concerned with various inconsistencies: a good example is that the financial statement forms do not reflect the format of the AASB 1056 forms. Such inconsistencies cause additional work through reconstructing the AASB 1056 format into APRA reporting format. AIST recommends that a series of workshops be held to identify these concerns and find solutions.

Earlier calls by regulators for data could have detected problems now identified by the Royal Commission

Within this and indeed many previous submissions, AIST has strongly advocated that APRA should collect additional data. We have also called on ASIC and government for a level playing field in terms of disclosure. Both APRA data collection and disclosure are naturally inter-related. We have also drawn these matters to the attention of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry ('Royal Commission').

Professor Thomas Clarke[4] highlights that there is '(a) consistent pattern running through all of the legislative and regulatory gaps and governance failures that have allowed members to be manipulated.'

The case studies before the Royal Commission have highlighted the detrimental consequences of insufficient data being provided to or analysed by APRA. Examples of these include:

Issue examined by the Commission	**Data which AIST had called for**
Impact of conflicted related parties **(eg case studies involving AMP, CBA, IOOF and NAB)**	AIST has long called on APRA to update its report[5] on the impact on value to members of related parties.
Delayed transition of Choice product members to MySuper **(eg case studies involving CBA and NAB)**	AIST has long called for APRA to benchmark fee and cost performance to assess whether members are being delivered fair value. Had this occurred, the lack of value through delayed MySuper transitions may have been highlighted. Additionally, AIST has long called for APRA to ensure the early transition of Choice members to MySuper.

[4] Clarke, T. (2018). *Serious failures in superannuation governance and critical omissions in superannuation regulation*. [online] AIST. Available at: https://tinyurl.com/y7kmtsvo [Accessed 16 Dec. 2018].

[5] APRA (2010). *Working Paper Australian superannuation outsourcing - fees, related parties and concentrated markets*. APRA.

Advice charges **charging trailing commissions banned under FOFA and cross selling superannuation products to bank customers**	While such matters fall under ASIC's jurisdiction, AIST's call for APRA to benchmark fee and cost performance may have highlighted the poor value members were receiving. Additionally, AIST has long called on both ASIC and government to ban both trailing commissions and cross-selling superannuation products to bank customers.

Timing of this review

We repeat our recommendation in our submission of 26 September 2018, namely that the superannuation industry is currently subject to multiple reviews and inquiries some of which deal with matters that are directly relevant to the prudential standards framework. AIST believes that the post-implementation review cannot be meaningfully conducted without the following four key issues being examined and the results included within the review:

- APRA's own insights.
- New APRA requirements.
- Insights from the substantive reviews which are in train.
- AIST's Governance Code 2017.

There are matters before both the FSRC and arising from the Productivity Commission's final report which need to be considered once the FSRC final report has been released.

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