



Submission to Treasury:  
Financial System Inquiry Final Report

31 March 2015

**AIST Submission**

## 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 \$600 billion not-for-profit superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training, consulting services 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.

## Contact

David Haynes, Executive Manager Policy & Research

03 8677 3803

Tom Garcia, Chief Executive Officer

03 8677 3800

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## 1 Executive summary

*This summary contains only those recommendations in the Final Report to which AIST has responded. Each recommendation is addressed in the numerical order of Final Report, however it should be noted that the responses in our submission are provided under specific subject heads which do not necessarily follow the order of the Report.*

Recommendation	AIST Response	AIST key points
<p>5. Crisis management toolkit</p> <p>Complete the existing processes for strengthening crisis management powers that have been on hold pending the outcome of the Inquiry.</p>	<p>Support</p> 	<p>While AIST strongly applauds APRA's work in setting risk management standards and progressing the review of crisis management in the financial system, we believe there remain a number of areas requiring attention. Of particular concern is the management of systemic risk from the interconnectedness of institutions within the superannuation system, including administrators, group life insurers, custodians and investment managers.</p>
<p>8. Remove the exception to the general prohibition on direct borrowing for limited recourse borrowing arrangements by superannuation funds.</p>	<p>Support</p> 	<p>Direct borrowing for limited recourse borrowing arrangements for superannuation funds creates systemic risk.</p>
<p>9. Seek broad political agreement for, and enshrine in legislation, the objectives of the superannuation system and report publicly on how policy proposals are consistent with achieving these objectives over the long term.</p>	<p>Support</p> 	<p>AIST supports enshrining the objectives of the superannuation system in legislation and urges the Government to convene a summit to reach bipartisan agreement.</p> <p>AIST supports a primary objective of the superannuation system that recognises the primacy of providing adequate income in retirement.</p> <p>AIST supports the codification of the subsidiary objectives of the superannuation system, with the subsidiary objectives proposed in the Final Report to be refined.</p>

		<p>There should be an objective way of measuring the performance of the superannuation system and proposed policy changes against the legislated objectives.</p> <p>The AIST Mercer Super Tracker provides an example of how this might be done.</p> <p>AIST believes the monitoring of the superannuation system against objectives should be undertaken by an independent, publicly funded body.</p>
<p>10. Introduce a formal competitive process to allocate new default members to MySuper products, unless a review by 2020 concludes that the Stronger super reforms have been effective in significantly improving competition and efficiency in the superannuation system.</p>	<p>Qualified support</p> 	<p>Any review of MySuper must have net return to members as its key focus, with issues such as fees and costs being important, but subsidiary, to net returns.</p> <p>AIST agrees that MySuper should be given time to settle but, in the meantime, we recommend the following to accelerate greater efficiency, comparability and fairness and to provide a better evidence base for any review:</p> <ul style="list-style-type: none"> <li>• Further disclosure to allow a better assessment of the efficiency of the system.</li> <li>• APRA to update its landmark 2010 report examining fees, concentrated markets, and related party transactions.</li> <li>• Accelerate the transition to MySuper of grandfathered default funds.</li> <li>• Develop a timetable to bring disclosure and reporting of CHOICE in line with MySuper</li> <li>• Review MySuper test of ‘scale’ for more focus on members’ best interests.</li> </ul>

		<p>AIST agrees with the Final Report that tailoring to member demographics in setting a default fund is important, but notes that a competitive process via the Fair Work Commission - taking member demographics into account - is already established and working.</p> <p>The Government should take all necessary steps to allow the FWC process to continue.</p>
<p>11. Require superannuation trustees to pre-select a comprehensive income product for members' retirement. The product would commence on the member's instruction, or the member may choose to take their benefits in another way. Impediments to product development should be removed.</p>	<p>Qualified support</p> 	<p>AIST agrees that funds should be required to implement a retirement income strategy for their members and that this should consider longevity. However while legislative impediments to longevity products should be removed, a CIPR should not be mandated for funds. Rather, they should be required to develop a framework appropriate to their membership.</p> <p>The superannuation system is continuing to mature, and existing allocated pension products will continue to be appropriate for many, especially low account balance members.</p> <p>A broader review of retirement incomes should be initiated, encompassing tax, age pension and broader consideration of all investment risks.</p>
<p>12. Provide all employees with the ability to choose the fund into which their Superannuation Guarantee contributions are paid.</p>	<p>Do not support</p> 	<p>Beyond the Final Report's general statement of belief that everyone should be able to choose the fund that receives their SG contributions, the Inquiry has not made out the case in support of this recommendation.</p> <p>Lack of choice does not contribute to multiple superannuation accounts, or higher fees, and default funds listed in Awards generally deliver higher returns.</p>

<p>13. Mandate a majority of independent directors on the board of corporate trustees of public offer superannuation funds, including an independent chair; align the director penalty regime with managed investment schemes; and strengthen the conflict of interest requirements.</p>	<p>Do not support</p> 	<p>AIST believes the representative trustee system delivers superior results for members and does not support the mandating of independent directors – either as a majority or a ‘one third’ requirement.</p> <p>Rather, we support flexibility around the equal representation system with the SIS Act being amended to allow boards to appoint <i>up to</i> one third non-representative directors.</p> <p>AIST believes there is no evidence to suggest that mandating a majority of independent directors will benefit members of not-for-profit funds.</p> <p>AIST urges the Government and industry stakeholders to work towards a common definition of independence.</p> <p>AIST supports retaining the SIS Act definition for equal representation boards, but removing the exclusion of members of the fund.</p> <p>AIST believes super fund boards should be free to choose the best person to chair their fund and that independence per se should not be a requirement.</p> <p>AIST believes the current legal requirements set out in the SIS Act, APRA Prudential Standards and trust law, with regulatory oversight from APRA provide a sound framework for the management of conflicts of interest. SPS 521 and the new SIS Act amendments should be allowed time to impact fund governance arrangements.</p>

<p>14. Collaboration to enable innovation</p> <p>Establish a permanent public–private sector collaborative committee, the ‘Innovation Collaboration’, to facilitate financial system innovation and enable timely and coordinated policy and regulatory responses</p>	<p>Support</p> 	<p>A single point of contact for innovators will aid efficiency and international competitiveness.</p> <p>A permanent public–private sector collaborative committee on innovation should include representation from the superannuation industry.</p>
<p>15. Digital identity</p> <p>Develop a national strategy for a federated-style model of trusted digital identities</p>	<p>Qualified support</p> 	<p>AIST supports a centralised rather than a federated-style model of digital identities.</p>
<p>19. Review the costs and benefits of increasing access to and improving the use of data, taking into account community concerns about appropriate privacy protections</p>	<p>Support</p> 	<p>A Productivity Committee inquiry into the use of data should include measures to facilitate superannuation account consolidation and encourage member-focused innovation.</p> <p>Superannuation regulators should be given an explicit requirement to encourage innovation by regulated entities in a way that also manages prudential risk (APRA) and provides consumer protection (ASIC).</p>
<p>23. Remove regulatory impediments to innovative product disclosure and communication with consumers, and improve the way risk and fees are communicated to members.</p>	<p>Support</p> 	<p>AIST strongly supports ASIC’s moves to improve electronic disclosure, and recommends the establishment of a standing working group to improve consumer usability, electronic delivery and use of electronic materials.</p> <p>There remain serious problems with the disclosure of risk and fees that have to be resolved in the interests of consumer protection.</p>

<p>24. Better align the interests of financial firms with those of consumers by raising industry standards, enhancing the power to ban individuals from management and ensuring remuneration structures in life insurance and stockbroking do not affect the quality of financial advice</p>	<p>Support</p> 	<p>AIST continues to support the eventual removal of conflicted remuneration from all financial products in the interests of all investors. We support this recommendation as part of a broader plan to phase these out entirely.</p>
<p>25. Raise the competency of financial advice providers and introduce an enhanced register of advisers</p>	<p>Support</p> 	<p>AIST supports improved industry standards in financial services. We note that the recommendation to implement an enhanced register of financial advisers is already in the process of implementation, and we support this measure.</p>
<p>27. Create a new Financial Regulator Assessment Board to advise Government annually on how financial regulators have implemented their mandate.</p> <p>Provide clearer guidance to regulators in Statements of Expectation and increase the use of performance indicators for regulator performance.</p>	<p>Do not support</p> 	<p>The new Cost Recovery Impact Statement and Government Cost Recovery Guidelines together with various other new regulator performance and audit frameworks should be given time for implementation.</p> <p>Regulators should continue to increase their use of outcomes focused performance indicators.</p>
<p>28. Provide regulators with a more stable funding model based on periodic reviews, increase the capacity to pay competitive remuneration, boost flexibility in respect of staffing and funding, and require them to undertake periodic reviews</p>	<p>Qualified support</p> 	<p>There is a lack of transparency and accountability in the funding model. Any changes in methodology around levies collected needs to be built on a well document and transparent model, with better alignment of expenses and levy revenue.</p>

<p>29. Introduce an industry funding model for Australian Securities and Investments Commission (ASIC) and provide ASIC with stronger regulatory tools</p>	<p>Qualified support</p> 	<p>Further information is needed about the application of levies to ASIC's operations so that an assessment of appropriate resourcing can be made.</p>
<p>30. Review the state of competition every three years, improve reporting of how regulators balance competition against their core objectives, identify barriers to cross border provision of financial services and include consideration of competition in ASIC</p>	<p>Support</p> 	<p>This review should be undertaken in conjunction between the ACCC and the Council of Financial Regulators.</p>
<p>31. Increase the time available for industry to implement complex regulatory change</p> <p>Conduct post-implementation reviews of major regulatory changes more frequently</p>	<p>Support</p> 	<p>Evaluation of regulatory changes should take into account impact on member engagement and general benefits to the economy, as well as timeliness and cost.</p>
<p>37. Publish retirement income projections on member statements from defined contribution superannuation schemes using Australian Securities and Investments Commission (ASIC) regulatory guidance.</p> <p>Facilitate access to consolidated superannuation information from the Australian Taxation Office to use with ASIC's and superannuation funds' retirement income projection calculators.</p>	<p>Support</p> 	<p>AIST supports greater use of standardised projections to encourage member engagement.</p> <p>AIST recommends standardised disclosure guided by ASIC.</p>

<p>40. Rename 'general advice' and require advisers and mortgage brokers to disclose ownership structures</p>	<p>Do not support</p> 	<p>AIST supports the creation of a central body to set financial adviser professional, ethical and educational standards.</p> <p>AIST recommends that the term 'general advice' be allowed for professionals who provide financial product advice where such advice is non-conflicted.</p> <p>AIST supports the relabelling of general advice as 'sales' but only where this is conflicted, such as the current situation with banking or general insurance products.</p> <p>AIST does not support conflicted sales roles in financial services.</p>
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## 2 Introduction

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We appreciate the opportunity to be able to respond to the Government on the Final Report of the Financial System Inquiry (FSI). The FSI Final Report makes a number of recommendations about superannuation and canvasses a range of policy options.

Our submission does not cover all recommendations raised in the Final Report. We have responded only to those where we believe we can add value or need to bring the Government's attention to significant issues.

As in previous submissions, the views expressed in this final submission on the FSI are based on the following key beliefs:

- Superannuation should exist to optimise retirement income in a sustainable way
- Australia's retirement incomes system is based on a three pillar framework
- Current default superannuation arrangements are fundamental for consumer protection in a compulsory system
- System sustainability is underpinned by high levels of disclosure, transparency and management of conflicts of interest

The Final Report recommended a package of reforms for superannuation, which – if adopted by Government – could have far-reaching impacts for generations to come, particularly in the post-retirement space.

While AIST supports many of these recommendations, there are some that we do not support. Others have our qualified support, either subject to certain matters being addressed or we have provided an alternate way to achieve the objective of the recommendation.

AIST was particularly pleased to see the FSI recommendation to enshrine in legislation clear objectives for superannuation. This is a much-needed reform to protect the superannuation savings pool from endless tinkering and provide the Australian public with greater certainty around their retirement planning. This submission urges the Government to act quickly on this recommendation and convene a summit to reach bipartisan agreement on both primary and subsidiary objectives for the superannuation system.

AIST has also welcomed the Inquiry's recognition that MySuper be given the opportunity to deliver improved outcomes for default members before any further reforms are considered. The industry has invested a lot of time and expense in implementing the MySuper and other Stronger Super reforms and it is only sensible that these reforms are given time to be implemented properly before they can be effectively assessed, particularly in regards to fee reductions and efficiency gains.

Other key recommendations we support - and urge the Government to act quickly upon - include the proposed ban on limited recourse borrowing within superannuation and the recommendation to encourage greater use and standardisation of retirement income projections.

In regards to the Final Report's recommendations on system efficiency measures, default fund selection and consumer protection in superannuation, AIST expresses a number of concerns.

While it was pleasing to see the FSI acknowledge the importance of the default fund selection process and the role of a quality filter, this submission points out that such a filter already exists as part of the Fair Work Commission process to select default funds. We contend that this process is much more transparent, contestable and competitive than before, and we urge the Government to recommence the process to provide much-needed certainty by proceeding with the appropriate appointments to the Commission.

In respect of the FSI recommendation to mandate a majority of independent directors on the boards of superannuation funds, we do not accept that this will be of tangible benefit to the members of out-performing not-for-profit funds.

Similarly, while we agree that funds should be required to implement a retirement income strategy for their members - and this should include a consideration of longevity - we have concerns that members' best interests will not be served by requiring super trustees to pre-select a mandated comprehensive income product for members' retirement. Rather, we believe funds should be required to develop a post-retirement framework appropriate to their membership, and be able to flexibly implement it.

As an overall comment, we are concerned that the Final Report places undue emphasis on some issues, while areas that we would argue are of equal, if not greater, significance, are either ignored or unrecognised. While the FSI was given a broad scope in respect of superannuation and has delivered recommendations in areas where reform is clearly needed, other recommendations reflect an arbitrary and narrow focus. Several key recommendations – notably around governance - lack any hard evidence to support the call for a change, which then begs the question: will this change demonstrably benefit members?

And while much is made of the need for a competitive default fund selection process, the Final Report provides no evidence that a more market-based system will deliver benefits for members and, importantly, protect the interests of the disengaged. What we do know from evidence, however, is that existing default funds have generally out-performed and delivered superior results for their members. Where for-profit super funds have been able to operate with fewer constraints, fees have almost always been higher and net returns lower. And while there are signs that - as result of the Stronger Super reforms – default fund fees are decreasing, not for profit fund fees are still consistently lower.

Other matters critical to the future success and sustainability of our retirement income system are ignored or dealt with superficially in the Final Report. Of particular concern – given the compulsory nature of superannuation - is the Final Report's failure to acknowledge the need for improved disclosure requirements in regards to structural conflicts through vertical integration in the for-profit superannuation sector. This is despite clear guidance in the G-20 high level principles on financial consumer protection of the importance of disclosure.

The issue of systemic risk arising from a growing interconnectedness across the superannuation sector has also been ignored. AIST's recommendations around the management of systemic risk – both at a micro and macro level - are contained in 'the missing chapter' on systemic risk on page 80.

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## 3 Governance

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### 3.1 FSI Recommendation 13: Governance of superannuation funds

***Mandate a majority of independent directors on the board of corporate trustees of public offer superannuation funds, including an independent chair; align the director penalty regime with managed investment schemes; and strengthen the conflict of interest requirements.***

#### 3.1.1 Our response

The FSI Final Report suggests that there are shortcomings in superannuation fund governance and in that light, makes recommendations about board composition, director liabilities and conflicts management. It does not provide details or evidence of these shortcomings. AIST strongly believes that good governance practices lead to improved performance and long-term sustainability. However, we strongly contest the proposition that there are shortcomings that need attention, or that the Final Report recommendations will lead to better outcomes for members of not-for-profit funds.

#### 3.1.2 Board composition

AIST takes this opportunity to reassert our position set out in our submission to the *Better regulation and governance, enhanced transparency and improved competition in superannuation* discussion paper, issued by the then Assistant Treasurer, Senator The Hon. Arthur Sinodinos.

Australia's \$1.93 trillion superannuation industry is made up of several types of superannuation funds, each with different governance and ownership structures. Some funds are owned by banks, insurance companies or other financial institutions and operate as profit-making entities (retail funds), some are owned by individuals (self-managed superannuation funds) while others, in the not-for-profit sector, were created by mutual agreement between employer and employee bodies who established trusts to manage members' retirement savings. As an industry body, AIST represents the interests of the not-for-profit superannuation sector, i.e. corporate, public sector and industry funds.

The trustee ownership structure of not-for-profit funds is distinctly different from the commercial ownership structure of most retail funds. While sponsoring organisations have an ownership interest in not-for-profit funds, they are not free to sell or trade their ownership interest, as it is held in perpetuity within the trust structure. The stewardship of the assets is protected through the trust structure set out in the governing rules and supervised by law.

Another important distinction in the ownership structures of the different types of funds is that unlike the parent companies of retail funds, sponsoring organisations of not-for-profit funds are generally not in the business of superannuation (or in any related business) and their relationship with the fund is not material or profit-driven. This is an important distinction when looking at director independence and conflicts of interest.

The governance framework of not-for-profit funds is based on an equal representation model whereby an equal number of the fund's employer and employee-sponsored directors are nominated or elected to the fund's board with the overarching protection of a two-thirds majority vote. While the two-thirds majority rule exists to protect beneficiaries and ensure that member interests are always prioritised, in practice the voting rule is seldom required as trustee directors pursue the best interests of members, usually on a consensus basis.

The equal representation model reflects both the occupational heritage of Australia's compulsory superannuation system and the view that member representation and a mutual ownership structure are critical to delivering the best retirement outcome for Australian workers. Direct member representation on the board of not-for-profit funds aims to ensure that member interests are aligned to the board's key strategic decisions and that trustee directors act solely in the interests of their members.

The Final Report<sup>1</sup> contends that "as more fund members exercise choice, directors appointed by employer and employee groups are less likely to represent the broader membership of public offer funds." It has also been suggested by commentators in the media that as not all super fund members are union members, a union may not be an appropriate representative. We take this opportunity to remind government and other interested stakeholders that in a mutual structure, such as an industry super fund, the owners of the trust are often employer groups on the one hand and unions on the other. As co-founders of these super funds, and sponsors of their ongoing success for members, their proprietary interest in the fund is not to be overlooked when setting requirements on board composition of private entities. And while union membership does not represent every single worker, unions as organisations are very in tune with industry-specific challenges and worker needs. They have a valid representational role and the same holds true for their employer group counterparts.

AIST submits that the governance model of not-for-profit funds has proven to be highly functional and effective, as well as highly adaptive to profoundly changing markets and commercial circumstances over time.

Another important attribute of the representative model is the diversity it brings to the boards of superannuation funds that generally have far greater occupational, gender and age diversity than corporate boards.

Against this backdrop, AIST believes that equal representation should continue to underpin the governance of not-for-profit funds.

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<sup>1</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia The Treasury, p.135. Available at: <http://tinyurl.com/n7wl3lb> [Accessed 23 Feb. 2015].

We do not, however, advocate a one-size-fits-all approach to the governance of superannuation funds and recognise that there should be flexibility for boards to appoint non-representative directors where appropriate.

AIST submits that one of the key strengths of the equal representation system is its focus on members' interests. The fact that the representative directors are independent of management of the fund, that they do not have a material relationship with the fund and are free to act without shareholder influence, also appears to drive the out-performance by not-for-profit funds.

The Final Report presents no evidence on how independent directors will benefit super fund members. The fact remains however, that not-for-profit funds are outperforming their retail peers and without any evidence to suggest gross misconduct, there is no evidence to suggest that independent directors would be a benefit to outcomes for members.

For equal representation boards the SIS Act limits the number of independent directors that such a board can appoint. AIST supports greater flexibility at law around this restriction and recommends that the legislation be amended to allow equal representation boards to appoint up to a third of their number from outside of the representative pool. AIST believes that up to a third independent directors preserves the benefits of the equal representation system, while offering boards greater flexibility.

### **3.1.2.1 The definition of 'independent director'**

In any change to the independent director requirements for public offer super funds, the definition of 'independent director' is crucial. It means different things in different contexts, and has a different meaning for superannuation funds and listed companies as the law now stands. The Final Report recommends that an arm's length definition should be adopted.

The existing definition of independent director in section 10(1) of the SIS Act adequately characterises non-representative directors for an equal representation board structure. The definition excludes employer sponsors and representatives of member and employer representative organisations. AIST submits however that the exclusion in section 10(1) of members of the fund is unnecessary as membership does not engender a material conflict that impacts on the director's ability to act with independence of mind and judgement. Accordingly we submit that the definition remains appropriate for equal representation funds, save for the exclusion of fund members.

AIST supports the ASX corporate governance principles and believes that they can offer additional guidance to boards on the concept of independence. However, there remains a fundamental structural difference between RSE licensees that operate as trusts and companies with different structures and responsibilities. These differences are significant and must be acknowledged and hence AIST contends that a blanket transposition of the ASX principles is not valid.

The ASX corporate governance principles definition excludes substantial shareholders as part of the independence test. In a corporate context, the shareholder exclusion arose from the need to protect minority shareholder interests against inappropriate dominance of substantial shareholders and management. The considerable pecuniary interest of a substantial shareholder can interfere with a director's independent exercise of judgement. In a not-for-profit superannuation context, no such issue exists.

In a superannuation fund setting, shareholders could be viewed as the members of the fund and their beneficiaries, or, the owners of the trust. The owners of not-for-profit RSE licensees can include employer-sponsors, member and employer representative organisations, and in some cases sitting individual directors. Their shareholding is not tradeable, and their obligations as trustees highlight the significant difference in organisational structure to corporations. Should appropriate amendments be made to the ASX definition to reflect the unique trust structure of superannuation funds, then - as a broad principle to guide funds on the concept of independence - they should take on a similar guidance role in APRA's prudential guidance material.

APRA has meanwhile attempted to merge the ASX principles with the SIS Act definition, resulting in a definition of non-affiliated director in SPG 510 *Governance*. This definition has not, however, resulted in a solution that appropriately recognises the trust system, or the diversity of governance models in superannuation. We note, too, that some significant amendments were made to the final version of the SPG 510 definition from the draft that was released for consultation in December 2012. The addition of clause (g) at paragraph 9 of SPG 510 unjustly excludes all member and employer representatives from being non-affiliated directors, regardless of whether the organisation they represented has any connection with the RSE licensee. AIST submits that while this may be an unintended consequence of the drafting of the provision, it nonetheless extends too far. The inclusion of directors of standard employer sponsors at clause (c) of paragraph 9 of SPG 510 also covers a wide array of potential super board directors, in funds where there can be thousands of standard employer sponsors. This provision should have a materiality filter applied to it to avoid unintended consequences and the screening out of otherwise suitably qualified super board director candidates.

SPG 510 struggles to reconcile the SIS Act definition of independent director with the broader understanding of that term in a corporate context. The unique nature of trusts and the diversity of our operating models adds complexity that is not easily resolved when attempting to consolidate and align a regulatory approach across the superannuation industry. A single, workable and relevant definition will require serious consideration. AIST submits however, that the SIS Act definition is appropriate to the equal representation funds (save for being excluded if a member of the fund) and that the Government should be cautious in making unnecessary changes.

### **3.1.2.2 The appropriate number of independent directors**

AIST rejects the assumption that adding independent directors to boards in and of itself results in better governance. As an organisation committed to assisting its members in achieving best governance

outcomes, we support evidence-based reform that improves governance practices and leads to better retirement outcomes for superannuation fund members. However, that evidence is distinctly absent from the debate and is not referenced in the Government’s discussion paper of November 2013 or the final FSI Report of November 2014. The focus of the independence proposals appears to be directed at equal representation boards and not other sectors of the superannuation industry.

Funds with equal representation boards collectively account for approximately a third on the \$1.93 trillion superannuation fund pool in Australia. Any significant change to their operating structure - such as a mandated change to board composition - should not be pursued lightly. A proper risk assessment and cost projection of a mandated board composition change - be that to a third independent directors, or moreover, a majority – must underpin such a significant policy shift.

The fundamental criteria in respect to the suitability and competence of any trustee director should lie in their skills and knowledge, their commitment and dedication to a process of continuous learning and a deep understanding of the members, the membership demographics, and the members’ needs. The current APRA Prudential Standards entrench these fundamental principles and clearly make trustee boards accountable.

AIST supports the equal representation system where the accountability to members through representation of stakeholders of the fund is central to its operating model. As the financial services environment continues to evolve, and the superannuation system matures, AIST submits that the new heightened obligations pursuant to the Stronger Super reforms have established the necessary framework to assist that growth and allow the industry to prosper within appropriate regulatory parameters.

Super fund boards are composed of a group of people who collectively make decisions that further the best interests of the RSE licensee’s members. The skills, experience, diversity and character of each of the individual directors must add to creating value to the collective board and ultimately the beneficiaries for whom they are responsible.

AIST supports the development of trustee director skills not only in investments, insurance, risk and financial management, but also any other skills that are necessary to assist the board to drive its strategic objectives into the future and to make the best decisions as a group. Diversity, behavioural competencies and the necessary dedication and commitment to the fiduciary responsibilities of being a trustee director should sit alongside the necessary skill requirements. AIST’s commitment to this principle can be demonstrated by the development of our Trustee Director Course, an educational program specifically addressing the skills and knowledge necessary to best discharge the duties and responsibilities of a superannuation fund trustee director.

Achieving the right mix of skills on a fund board has become intertwined with the independence debate and has led to some confusion as to why individual boards appoint directors who are not a representative or in any way associated with an employer or employee representative group or employer-sponsor of the fund.

As the superannuation and financial services environment has evolved over recent years, some representative boards have taken a number of active steps to supplement their skills and professional competencies at board level through the appointment of directors outside of the representative pool (*11% of directors on not-for-profit trustee boards are independent; 19 of 59 not-for-profit fund Chairs are independent*). In most cases, these appointments have nothing to do with achieving independence *per se*.

AIST agrees that non-representative directors can and do add substantial value to boards. However, that does not mean that other classes of directors are therefore of lesser value. AIST does not support the prescription of board composition by legislative instrument or regulatory mandate, and rejects the assumption that directors who meet a legal definition of independence add value to the members of the trust, by that virtue alone.

Representative boards currently have the flexibility to appoint one additional independent director (section 89(9) SIS Act) or, by approaching APRA, more than one additional non-representative director. Good governance practice dictates that boards are constituted of the right mix of people. In this context AIST supports an amendment to the SIS Act allowing RSE licensees to appoint up to a third independent directors to their board. Retaining equal representation of employers and employees, and preserving a balance of diverse backgrounds and skills remains AIST's position. It is a matter for individual boards to consider the ultimate composition of their board having regard to the best interests of their own members and the requirements at law. This may indeed include additional non-representative directors on boards.

AIST supports the implementation of a positive obligation of super fund boards to demonstrate to APRA that they have duly followed an appropriate and documented process and considered the composition of their board, including the appointment of independent directors. They should be able to report to APRA on how their board composition meets the requirements of the SIS Act and prudential regulation and that it is in the best interests of members.

The Final Report suggests that the inclusion of independent directors accords with international best practice. In the pension fund area, however, this is not what AIST has found.

Equal representation of employer and employee interests on boards of pension schemes is not a model that is unique to Australia. Many countries around the world adopt equal representation as their preferred governance model.

A 2008 OECD *Working Paper on Pension Fund Governance*<sup>2</sup> asserts that employee or member representation can ensure a better alignment of the interests of the board with the fund beneficiaries. That paper goes on to comment that this needs to be balanced against the need for experience and knowledge (in Australia, the fit and proper requirements deal with this matter).

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<sup>2</sup> Stewart, F. and J. Yermo (2008), "Pension Fund Governance: Challenges and Potential Solutions", *OECD Working Papers on Insurance and Private Pensions*, No. 18, OECD publishing, OECD. Available at <http://tinyurl.com/pa65bm7> [accessed 24 March 2015]

That paper provides the following summary of representation on superannuation boards across various countries:

<b>Australia</b>	<b>Non-public offer funds (company and industry-wide funds) must have an equal number of employer representatives and member representatives on the board of directors of the corporate trustee or in the board of trustees.</b>
<b>Austria</b>	The board of supervisors of the pension fund may have two seats fewer for employee representatives than for the sponsoring employer or other shareholders of the pension fund.
<b>Belgium</b>	The board of directors of a pension fund must have equal representation of employers and employees.
<b>Brazil</b>	At least one third of the supervisory board and the audit committee must be composed of worker representatives.
<b>Canada</b>	There are no requirements for single employer plans. Multi-employer plans established pursuant to a collective agreement are governed by a board of trustees composed in accordance with the plan or collective agreement (typically equal representation).
<b>Germany</b>	Supervisory Board: employee representation depends on the number of employees in the pension fund, with a maximum of equal representation.
<b>Hungary</b>	Mandatory pension funds must have member representatives in their board of directors.
<b>Iceland</b>	The board of the pension fund must have equal representation of employers and employees
<b>Ireland</b>	No requirement for employee representation.
<b>Israel</b>	No requirement for employee representation.
<b>Italy</b>	The general assembly and the board of directors must each have equal representation of employers and employees.
<b>Japan</b>	The Board of Representatives of Employee Pension Funds must have equal representation of employers and employees.
<b>Mexico</b>	No requirement.
<b>Netherlands</b>	The board of the pension fund must have equal representation of employers and employees.
<b>Norway</b>	The board of the pension fund must have at least as many employee as employer representatives.

<b>Poland</b>	Not less than half of the members of the supervisory board of the occupational pension society should be nominated by the members of the fund.
<b>Spain</b>	The majority of the control commission must be selected by plan members and beneficiaries. No requirement for member representation in the board of pension fund management companies.
<b>South Africa</b>	At least half of trustees must be elected by plan members.
<b>Sweden</b>	The board of the foundation must have equal representation of employers and employees.
<b>Switzerland</b>	The supreme council of a pension fund must have equal representation of employers and employees.
<b>United Kingdom</b>	At least one third of trustees must be member-nominated.
<b>United States</b>	No requirements for single-employer funds. Multi-employer (Taft-Hartley) funds must have equal representation of employers and employees.

Table 1

**AIST position:** That the SIS Act be amended to allow up to a third of equal representation board directors to be non-representative directors. That boards have a positive obligation imposed on them to report to APRA, if required, that they have followed an appropriate process in deciding on their board composition, and that their structure is in the best interests of members.

### 3.1.2.3 *An independent chair*

AIST submits that the board should choose its chair on the basis of its specific requirements and appoint the best person for the job, regardless of what class of director he or she falls into.

AIST supports the implementation of a positive obligation on super fund boards to report to APRA that they have an appropriate process for appointing their chair and that they have duly followed the process and considered the appropriateness of appointing an independent chair. They should be able to demonstrate in their reporting on board composition to APRA that their appointment is in the best interests of members.

The role of the Chair is crucial to the effective functioning of the board. Chairs influence the board culture and its working dynamic enormously. When replacing a chair it is vitally important to recruit the right person who can bring out the best in the individual directors and run a collegiate board. The right person for the job may not always be an independent director.

**AIST position:** Super fund boards should be free to choose the best person to chair their fund, be they a representative director or not. Funds should be required to report to APRA if requested as to the process for the selection of their chair, the considerations that formed part of their criteria and how the appointment is in the best interests of members of that fund.

### 3.1.3 Director penalty regimes

AIST believes that continuing improvements to disclosure and reporting practices are more effective measures against malpractice than punitive sanctions for legislative or regulatory breaches.

As noted by the Super System Review's Final Report<sup>3</sup>, 'clearly it is a basic principle that trustees should always endeavour to comply with the relevant law and members would expect nothing less. If trustees do not comply and that leads to damage or loss to members, trustees should be accountable to members who are affected. In the Panel's view, however, it is dangerous to rely too heavily on the threat of regulatory sanction to deter transgressions. The Panel believes that its various recommendations for more transparency in superannuation will do more for members than heavier enforcement penalties for wrongdoing. Further, the SIS Act and the Corporations Act currently provide a range of actions that APRA and ASIC can take against a trustee or trustee-director who fails to comply with the law.'

Since the Super System Review's Final Report, APRA has issued superannuation Prudential Standards, the SIS Act has imposed higher obligations on trustees and individual directors, ASIC has continued to improve disclosure requirements, and superannuation reporting requirements have come into effect. AIST believes that through the combination of trust law, the SIS Act, the Corporations Act 2001, and various superannuation Prudential Standards, the legal liabilities for superannuation trustee directors are already higher than those referred to by the FSI Final Report.

AIST questions the evidentiary basis for the Final Report concluding that there is a significant gap in the current framework regarding superannuation director penalties. The Final Report comments that superannuation directors are not subject to criminal or civil penalties in relation to their duty to act in the best interests of members. A superannuation member who has incurred loss or damage as a result of director misconduct can seek recovery through civil action – or APRA can disqualify the director. The Final Report comments that this is inconsistent with the regime applying to directors of responsible entities of MISs under the *Corporations Act 2001*, who are subject to criminal and civil penalties.

AIST strongly believes that it is more important to continue to improve disclosure and reporting practices.

#### **3.1.3.1 Continuation of the focus on better disclosure and transparency is paramount**

AIST concurs with the comments of the Super System Review's Final Report that greater measures for disclosure and transparency will do more for members than heavier enforcement penalties. AIST strongly supports work which has occurred and is continuing in this space, including APRA Prudential Standards and Practice Guides, ASIC improved disclosure requirements, and reporting to APRA. All of these measures

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<sup>3</sup> Cooper, J., Casey, K., Evans, G., Grant, S., Gruen, D., Heffron, M., Martin, I. and Wilson, B. (2012). *Super System Review Final Report Part One Overview and Recommendations*. [online] Canberra: Commonwealth of Australia, Attorney-General's Department, Section 5.4. in chapter 2. Available at: <http://tinyurl.com/nevhras> [Accessed 25 Mar. 2015].

continue to deliver improved efficiencies to members as well as to the Australian superannuation system as a whole. Continuation of this work is paramount.

### **3.1.3.2 Superannuation trustee directors' legal liabilities already higher through civil and criminal sanctions**

Sanctions under the SIS Act for Trustee non-compliance broadly fall into four categories:

- Administrative sanctions such as disqualifying trustees (section 126A of the SIS Act).
- Court imposed sanctions for contravening civil penalty provisions (section 196 of the SIS Act).
- Court imposed criminal sanctions for offences defined to be civil penalty provisions contravened with dishonest or fraudulent intent (section 202 of the SIS Act).
- Administrative penalties introduced from 1 July 2014.

Civil penalty provisions are listed in section 193 of the SIS Act. The superannuation sole purpose test (section 62 of the SIS Act), if breached, could trigger a civil penalty under section 193 of the SIS Act. AIST notes that section 196 of the SIS Act provides for the making of civil penalty orders in connection with civil penalty provisions. If the Court is satisfied that a contravention has occurred, then similarly to the *Corporations Act 2001* regime, the Court may then make an order that the person is to pay to the Commonwealth a monetary penalty.

### **3.1.3.3 Low level of regulatory infringement by superannuation trustees**

Donald<sup>4</sup> refers to the low incidence of regulatory infringement by trustees compared to some other individuals such as company directors or public officials and references note 5.68 of the 2006 Parliamentary Joint Committee on Corporations and Financial Services' Inquiry into the Structure and Operation of the Superannuation Industry.

### **3.1.4 Strengthened conflicts regime**

The existing conflicts of interest regime for APRA-regulated super funds is one of the strongest in any industry sector. The nature of fiduciary obligations under trust law, the SIS Covenants and APRA's SPS 521 *Conflicts of Interest* ensure that the overriding obligation in all cases is to give priority to the interests of beneficiaries.

The SIS covenants state (among other things) at section 52(2)(c) and (d) SIS Act:

- (c) to perform the trustee's duties and exercise the trustee's powers in the best interests of the beneficiaries;*

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<sup>4</sup> Donald, M. (2010). *What contribution does trust law make to the regulatory scheme shaping superannuation in Australia?* [online] APRA. Available at: <http://tinyurl.com/nlsczks> [Accessed 25 Mar. 2015].

(d) *where there is a conflict between the duties of the trustee to the beneficiaries, or the interests of the beneficiaries, and the duties of the trustee to any other person or the interests of the trustee or an associate of the trustee:*

- (i) *to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons; and*
- (ii) *to ensure that the duties to the beneficiaries are met despite the conflict; and*
- (iii) *to ensure that the interests of the beneficiaries are not adversely affected by the conflict; and*
- (iv) *to comply with the prudential standards in relation to conflicts*

SPS 521 *Conflicts of Interest* requires all RSE licensees to have and maintain a robust conflicts framework and policy that is independently reviewed at least every three years.

Section 29QB of the SIS Act disclosure requirements also mandates the disclosure of any conflicts of interest and the conflicts of duty register. All conflicts need to be documented and disclosed publicly on a fund's website, commencing 1 July 2014.

The Final Report at page 136 recommends that conflicts of interest be deemed to have been disclosed when they are acknowledged by all the directors, and that a register in and of itself is insufficient. AIST submits that this suggestion is currently common practice.

The obligation for ASX listed companies is to identify, monitor and manage conflicts of interest. They do not have an additional overarching obligation, in all circumstances, to prioritise the interests of the company and/or the shareholders. The obligations on super fund trustee directors in terms of prioritising member interests is therefore higher than in other APRA-regulated industries and the corporate arena.

APRA's research into related party transactions in the superannuation industry has highlighted the conflicts of interest inherent in the board composition and ownership structure of many retail superannuation funds, particularly where parent companies are aligned to the fund's material service providers. In the area of administration fees, for example, APRA found that some retail trustees using related-party administrators were paying significantly higher fees, "effectively doubling the median member's cost load". APRA noted that "reconciling this finding with the superannuation trustee's fiduciary duty to fund members will bear further investigation".<sup>5</sup> In contrast, APRA concluded that the fees paid by trustees of not-for-profit funds to related parties were "not significantly different than those to independent service providers".

Other research papers add weight to the view that appointing directors who are independent of management and free of the conflict of having to serve both members and parent company shareholders is

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<sup>5</sup> Sy, W. (2015). *Superannuation fund governance: An interpretation*. APRA Working Paper. [online] Canberra: Australian Prudential Regulation Authority. Available at: <http://tinyurl.com/odrrmv6> [Accessed 24 Mar. 2015].

one of the key issues – if not **the** key issue - when it comes to best practice governance of managed funds. Bogle,<sup>6</sup> for example, pointed out that executive directors of American mutual funds, in trying to serve two masters, have tilted the balance of interest in favour of company shareholders to the detriment of fund beneficiaries.

Further, AIST submits that more related party conflicts are likely to result from the implementation of a mandated policy to appoint more independent directors on boards. The inference in both the discussion paper and the FSI Report is that independent directors will be drawn from the financial and professional services industries. The Australian financial services market is small, and the potential for conflicts that arise on boards will increase as a result. The Bogle research also supports this.

**AIST position:** The current legal requirements set out in the SIS Act, APRA Prudential Standards and trust law, with regulatory oversight from APRA provide a sound framework for the management of conflicts of interest. SPS 521 and the new SIS Act amendments should be allowed time to impact fund governance arrangements.

### 3.2 Our Recommendations

- AIST does not support mandating a majority of independent trustee directors onto the boards of not-for-profit superannuation funds. AIST believes that up to a third ‘independent’ directors preserves the benefits of the equal representation system, while offering boards greater flexibility.
- Retain SIS Act definition for equal representation boards, and remove the exclusion of members of the fund. Modified ASX principles of independence - which recognise the trust structure - to be added as further whole-of-industry guidance in APRA guidance material.
- AIST believes the current legal liability imposed on superannuation trustees is higher than those referred to in the Final Report and that, accordingly, we do not support harsher director penalties. We believes that continuing improvements to disclosure and reporting practices are more effective measures against malpractice than punitive sanctions for legislative or regulatory breaches. The current legal requirements set out in the SIS Act, APRA Prudential Standards and trust law, with regulatory oversight from APRA provide a sound framework for the management of conflicts of interest. SPS 521 and the new SIS Act amendments should be allowed time to impact fund governance arrangements. The focus on continuing the development of Superannuation Prudential Standards and ensuring greater disclosure and transparency is paramount. The continued clarification of these issues gives greater certainty to trustee obligations.

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<sup>6</sup> Bogle, J. (1999). *Common Sense of Mutual Funds*. New York: John Wiley 7 Sons, Inc.

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## 4 Efficiency

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### 4.1 FSI Recommendation 10: Improving efficiency during accumulation

***Introduce a formal competitive process to allocate new default members to MySuper products, unless a review by 2020 concludes that the Stronger Super reforms have been effective in significantly improving competition and efficiency in the superannuation system.***

#### 4.1.1 Our response

AIST notes that the Final Report - in examining how to improve efficiency during accumulation - focuses on fees, net investment returns, and options for setting default funds. AIST agrees with the Final Report in that MySuper needs time to settle before a review takes place. However, AIST contends that before such a review, it is necessary to first assess the impact of structural conflicts arising from the for-profit superannuation sector not having a clean separation of banking from wealth management. These structural conflicts impact on fees, net returns to members, and disclosure. AIST appreciates that in order to do this a program of practical steps is needed and accordingly makes the recommendations, below.

#### 4.1.2 Introduction to this section

The Final Report comments that while Stronger Super sought to lower fees and bring greater competition into the superannuation market, the Inquiry had reservations about whether Stronger Super would deliver.

The Final Report expressed a major concern that the system as a whole has been unable to realise the full benefits of scale. The Final Report comments that this has been partly caused through market fragmentation, consumer disengagement, and employers selecting default funds. While AIST agrees with the Final Report that time is needed to assess the impact of MySuper, AIST strongly believes that certain things must occur beforehand so that any assessment can be based on meaningful evidence. These include bringing forward the transition to MySuper, ensuring greater disclosure of fees and costs, assessing the impact of related-party costs on investment and administration fees and costs, and bringing the disclosure and reporting of Choice products into line with MySuper.

As a preliminary indicator to the impact of MySuper, research commissioned by AIST with RiceWarner<sup>7</sup> suggests that MySuper will, over time, have 'a profound impact on fees within the superannuation industry.' The research indicated a lowering of fees. A separate report by RiceWarner provided to the FSI shows similar findings<sup>8</sup>.

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<sup>7</sup> RiceWarner (2014) *Navigating the New MySuper Landscape*, AIST and Rice Warner Research, available at <http://tinyurl.com/mhczs9x>

<sup>8</sup> RiceWarner (2014) *MySuper fees*, data provided to the FSI, 6 November 2014.

As regards the selection of default funds, AIST endorses the emphasis the Final Report places on the objectives of ensuring a long term best interests of members' test; a focus on net returns (while realising fees and costs are important); the need for a quality filter over and above being a MySuper product; and the need for comparability and efficiency. AIST strongly believes that these objectives are already taken into account by the Fair Work Commission process. This means that a new government organisation need not be established. AIST recommends that the Fair Work Commission process continue.

#### **4.1.2.1 While fees are important, net return to members is the key**

AIST endorses the objective stated in the Final Report<sup>9</sup> to 'enhance efficiency in the superannuation system to improve long-term net returns to members and build trust and confidence in funds regulated by the Australian Prudential Regulation Authority (APRA).'

AIST agrees that operating costs and fees should not be looked at in isolation without regard to net investment returns, and certainly not without an explanation of the true value for money and services received by Australians in their super account.

It is therefore essential that any review of Stronger Super should focus on net return to members, with fees and costs being important but subsidiary issues.

The not-for-profit superannuation sector continues to demonstrate its long-term value to members. As Cummings & Ellis<sup>10</sup> found, not-for-profit funds earn higher risk-adjusted returns than retail superannuation funds (high-fee funds). Recent data aggregated<sup>11</sup> by Industry Super Australia from the SuperRatings crediting rate survey shows that the not-for-profit sector has once again outperformed the retail fund sector over the one, three, five, seven and ten years based on balanced fund median rolling returns to 30 December 2014.

#### **4.1.2.2 Fees are important and an 'equal playing field' would assist drive fee and cost efficiencies**

The FSI Final Report comments that fees have not fallen by as much as would be expected given the substantial increase in the scale of the superannuation system. While AIST reiterates its comments made in

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<sup>9</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia, The Treasury, p. 135. Available at: <http://tinyurl.com/n7w3lb> [Accessed 12 Mar. 2015].

<sup>10</sup> Cummings, J. R. and Ellis, K. (2011) 'Risk and return of illiquid investments: A trade-off for superannuation funds offering transferable accounts', APRA Working Paper.

<sup>11</sup> Industry Super Australia, (2015). Industry super fund outperformance reinforces undivided loyalty model | Industry Super Australia. [online] Available at <http://tinyurl.com/jwcc3qe> [Accessed 13 March 2015].

its submission<sup>12</sup> to the FSI Interim Report that MySuper has already brought about lower fees, AIST strongly contends that there are three key issues that would further assist fee and cost efficiencies:

- Many fees and costs are not disclosed, making it difficult to assess the efficiency of the system. Disclosure and reporting should be further strengthened.
- The impact of related-party transactions on the efficiency of investment and administration fees should be reviewed through requesting APRA to update the 2010 report examining fees, concentrated markets, and related-party transactions<sup>13</sup>.
- The transition to MySuper should be brought forward from 2017. While an estimated \$395B has been transitioned, there is \$77B yet to be moved across.

#### **4.1.2.3 Competition and greater efficiencies through alignment of APRA reporting requirements**

Recent APRA data shows that at December 2014, there is \$395B in MySuper and \$898B in Choice (also known as Select Investment Options). APRA has commented<sup>14</sup> that at 30 June 2014, there are over 42,500 investment options offered within RSEs across the industry.

APRA has released its select investment option reporting to APRA guidelines, with the effect that there are significant differences between reporting MySuper and select investment options.

AIST had submitted that the reporting guidelines for select investment options should be the same as for MySuper for the following reasons:

- Both MySuper and Select Investment Options are APRA-regulated and receive the same taxation concessions.
- Alignment of reporting assists greater transparency, efficiency and competition.
- Select Investment Options cover a considerable number of members and funds under management. Thus scrutiny - as well as consistency of reporting - is important.
- Funds choose to have Select Investment Options as a competitive decision; regardless of whether or not these are advised, members should have access to the same information.

There is a threshold set below which certain select investment options do not have to be reported. Of the 42,500 investment options, 2,481 meet the original select investment option definition. This means there are some 40,019 investment options which are not reporting.

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<sup>12</sup> AIST, (2014). *Response to the Financial System Inquiry Interim Report 26 August 2014*. Australian Institute of Superannuation Trustees.

<sup>13</sup> APRA, (2010). *Working Paper Australian superannuation outsourcing - fees, related parties and concentrated markets*. APRA.

<sup>14</sup> APRA, (2015). *Response to submissions: Reporting Standards for Select Investment Options*. [online] Australian Prudential Regulation Authority. Available at: <http://tinyurl.com/pmrxxz8> [Accessed 13 Mar. 2015].

AIST continues to have concerns regarding the variances between reporting MySuper and select investment options:

- Based on APRA's comments, data is not being received regarding \$242 billion of RSE managed assets (i.e. 20% of the \$970 Billion managed by pooled superannuation funds).
- There are a considerable number of member investment options that are clearly causing inefficiencies within the industry.
- How to handle legacy products – as well as the creation of so many investment options – are key issues affecting superannuation system efficiencies.

#### **4.1.2.4 Competition and greater efficiencies through better disclosure of true fees and costs**

In our previous submission to the FSI Interim Report, we noted that not all fees and costs are disclosed by super funds. We are concerned that this was not addressed in the Final Report.

Further examples of non-disclosure include:

- Instances where there is a single fee across all cohorts of members invested in MySuper lifecycle and cohort default investment options. This makes it difficult for the member to compare or understand the degree of cross-subsidisation across the cohorts.
- Shelf-space fees should reflect the true underlying costs to particular platforms.

We reiterate our support for the G20 High-Level Principles on Financial Consumer Protection<sup>15</sup>, which include product comparability. While MySuper has furthered the delivery of comparable product disclosure, there are still a number of areas where key matters are not being fully disclosed. Such a lack of disclosure leads to:

- A lower degree of regulatory protection for members.
- A lack of comparability and protection at member level.
- A reduction in the capacity of the Regulators to understand the totality of fees and other costs in the Australian superannuation system.
- The inability to fully assess the impact of legislative reforms such as MySuper.
- A reduction in competition within the system itself.

AIST applauds the work of ASIC to improve disclosure. The intention behind draft Regulatory Guide 97 – Fee Disclosure Superannuation and Managed Investments (which has been released for consultation since the FSI Interim Report) is welcomed. The draft seeks to ensure that the promotion of lower fees and costs

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<sup>15</sup> OECD, (2011). G20 High-Level Principles on Financial Consumer Protection. Paris: Organisation for Economic Co-operation and Development. Available at: <http://www.oecd.org/daf/fin/financial-markets/48892010.pdf>

(or, in some instances, a no fee product) is misleading where in fact those fees and costs are being paid by a promoter or other related-party of the product issuer.

#### **4.1.2.5 Negative impacts of related-party transactions should be examined to highlight inefficiencies. Vertical integration does exist**

As we commented in our recent submission<sup>16</sup> to the Senate Standing Committee on Economics inquiry into Scrutiny of Financial Advice, structurally it is difficult to ensure that consumers are as fully protected as they should be, given the structural conflict of interest arising from not having a clean separation of banking from wealth management.

Such structural conflicts of interest have, AIST submits, led to major financial planning advice scandals, as well as the proliferation of hidden fees and costs from consumers. While the Final Report chapter on 'Consumer Outcomes' refers to the removal of certain commissions and aligning remuneration structures with a customer-focused outcome, AIST believes that these do not address the issues arising from the heart of the matter – that structural conflicts of interest still exist.

AIST's view is shared by other commentators. The International Organisation of Pension Supervisors comment that '...the limited capacity of individuals to choose what is best for them means that competition and markets rarely work effectively within pension systems – leaving too much power in the hands of pension providers. The problem is only exaggerated when pension providers are commercial financial institutions. Conflicts of interest can therefore exist between the fiduciary duty to act in the best interests of the pension fund members and beneficiaries and making profits for shareholders<sup>17</sup>.'

AIST's involvement in industry consultation roundtables has given rise to our concern that there may be industry opposition to ASIC's proposal in draft RG97 to ensure disclosure of lower fees and costs which are in fact paid by a promoter or related-party. We also note that the Final Report does not take into account the impact of related-party fees and costs on the Australian superannuation system.

This very important issue was examined in a 2010 APRA report<sup>18</sup>, where the comment was made that '[I]n the case of a public-sector, corporate, or industry fund, the trustee is organised on a not-for-profit basis, and that in the case of a retail fund, though, the trustee (or the corporate group to which it belongs) has the strong expectation of profiting from its superannuation business. It also recognises that because retail

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<sup>16</sup> AIST, (2014). *Scrutiny of Financial Advice*. Australian Institute of Superannuation Trustees. Available at <http://tinyurl.com/qxxq8dd> [Accessed 13.3.2015]

<sup>17</sup> International Organisation of Pension Supervisors, (2010). *Managing and Supervising Risks in Defined Contribution Pension Systems*. Working Paper No.12. Available at: [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1809741](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1809741)

<sup>18</sup> Liu, K. and Arnold, B. R. (2010) 'Australian superannuation outsourcing: fees, related parties and concentrated markets', Australian Prudential Regulation Authority Working Paper, p. 6.

trustees must reconcile their (group's) profit motives with their fiduciary duty to act in the members' best interest gives rise to agency risk.'

Critically, the 2010 APRA report found that trustees of retail funds pay related party service providers significantly higher fees than independent service providers. Conversely, the fees paid by trustees of not-for-profit funds to related parties are not significantly different to those paid to independent service providers.

The information contained in the 2010 APRA Report is based on a unique data set provided via an APRA survey conducted in 2006. This information, while providing an invaluable insight into the efficiencies and inefficiencies of the fees and costs of the Australian system, has not been updated. AIST recommends that prior to any review of MySuper, the information in this report be updated by APRA.

Given the compulsory nature of superannuation and APRA's role as a key regulator AIST contends that APRA has a clear responsibility to ensure that related-party transactions and arrangements are managed on a best practice basis and always in members' best interests. Moreover, APRA is in the unique position of having access to relevant and current data on related party transactions across the superannuation sector that is not readily, if at all, available to other industry stakeholders. Given the disturbing findings of APRA's 2010 report and lack of follow-up investigation by the regulator, we believe an update is urgently required. This information is critical to understanding key factors underpinning fees and costs, and which cannot be obtained elsewhere.

#### **4.1.2.6 MySuper transition**

The transition to MySuper should be brought forward from 2017. Some \$395B has been transitioned, with some \$77B yet to be moved across. While many retail funds have introduced new low fee MySuper products, they have very little funds under management, with large sums remaining in previous high-fee products. The reality is that many retail members are locked out of this low cost environment due to uncompetitive grandfathering arrangements. AIST contends that the sooner MySuper transitioning is finalised, the more efficient any review of MySuper will be.

#### **4.1.2.7 Default funds – a competitive process exists which meets the FSI Final Report's recommendations**

##### **4.1.2.7.1 Members' best interest test is fundamental**

AIST strongly agrees with the Final Report that a quality filter is needed for default fund selection. This is needed because, notwithstanding the best intentions of most employers, the Government has a responsibility to protect employees and provide a safety net for them. Superannuation is an important condition of employment.

The Final Report has outlined objectives to drive a process for fair and robust default fund selection, which includes assessments around the long term best interests of members, net returns and transparency of process, with competitive pressures for innovation and efficiency.

#### **4.1.2.7.2 A centralised system is needed to ensure members' best interests are met**

The payment of the Superannuation Guarantee employer contributions to members of super funds is inextricably linked to their employment, and is a condition of employment.

AIST believes that to best achieve these objectives and to maintain the association with employment, a centralised system is needed. Such a system connects employers with default superannuation arrangements that are most appropriate to them. The current Fair Work Commission process, involving both an expert panel and industrial parties, ensures that this occurs.

AIST strongly believes that any decentralised process (e.g. tenders or auctions) would not produce a more efficient and stable system. A centralised system is the most efficient way of ensuring that the best interests of members are met:

- Superannuation in Australia is based on a compulsory savings system, where the Government needs to ensure that there is a suitable safety net in place.
- The current FWC process applies a quality filter to ensuring the needs of employers and members are met.
- Through Modern Awards employees are connected with the default superannuation arrangements which are most appropriate to them, as reflected through features such as default investment strategy, insurance and consumer services.
- A centralised system provides an additional form of consumer protection.
- A decentralised system would produce inefficiencies of process, especially given that small business accounts for approximately 50% of private sector employment in Australia<sup>19</sup>.
- The FWC process would give employers a choice of between 10-15 funds.

A centralised system – coupled with a quality filter - assists with reduction of third-line forcing. In 2010, Australian Taxation Office commissioned research<sup>20</sup> found that 13% of employers surveyed said that they had received a direct or indirect benefit from a superannuation provider. A centralised system is therefore important to ensuring that the best interests of members are met.

#### **4.1.2.7.3 A quality filter is needed to meet members' needs**

It is also imperative, as the FSI Final Report recommends, that a quality filter is applied to the selection of a default fund is applied so that the members' best interest is met. As the FSI Final Report notes, any tendering or auction system may deflect from meeting a quality filter.

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<sup>19</sup> DIISRTE, (2015). *Australian Small Business: Key Statistics and Analysis*. [online] Australian Government, Department of Industry, Innovation, Science, Research and Tertiary Education. Available at: <http://tinyurl.com/ofr9g4n> [Accessed 15 Mar. 2015].

<sup>20</sup> Colmar Brunton Social Research prepared for the Australian Taxation Office. *Understanding Superannuation: Preliminary Report: Qualitative Investigation with Employers, Consumers and Industry*, 25 March 2010.

The FSI Final Report recommends that a new process should be introduced unless a review of Stronger Super shows that the Stronger Super reforms have been effective, and, while not pre-empting any review outcome, the Productivity Commission should begin preliminary work in 2015 to design a competitive process.

#### **4.1.2.7.4 Productivity Commission previous work already underpins current Fair Work Commission processes**

AIST believes that the current Fair Work Commission process (which includes quality filters) meets objectives outlined in previous work undertaken by the Productivity Commission. The Fair Work Commission process is already in place, and is fully transparent and contestable. Applications to be included on a Default Superannuation List can be any MySuper product and need to include the following:

- The appropriateness of the product's investment return target and risk profile.
- Its expected ability to deliver on the product's return target.
- Fees and costs.
- Net returns.
- Governance practices.
- Administrative efficiency and quality of advice.

This list of factors is the same as that recommended for consideration in the Productivity Commission's review of Default Superannuation Funds in Modern Awards. An employer having to make a choice directly might appropriately consider the same sort of factors, but would do so in a process that would be without the expertise, resources or efficiency available through the FWC process.

AIST highlights that the Productivity Commission accepted that the FWC is the appropriate body to regulate the selection of default funds by employers. The Fair Work Act 2009, under which the FWC operates, was created to ensure that there is a balanced framework for cooperative and productive workplace relations. The Productivity Commission accepted that as an employment-based entitlement, the balance of employer and employee interests in relation to superannuation could be efficiently regulated by the FWC.

The involvement of an expert panel within the FWC ensures that alignment is provided between experts and workplace representatives. This ensures the continuation of a safety net, where quality is at the centre of agreements over industrial default retirement savings arrangements, and where a list of appropriate defaults can save time for employers when considering default arrangements.

The FWC process is currently stalled pending the filling of vacancies on the Expert Panel. AIST strongly recommends that the Government fulfil its undertaking to the Federal Court to appoint members to the vacant positions, and that the FWC then recommence the process as a matter of urgency. AIST notes that this will both allow the introduction of more transparent and accountable processes for the selection of default superannuation fund and allow the current round of award modernisation to be concluded.

## 4.2 Our Recommendations

- AIST believes that the existing FWC process to allocate new default members to MySuper products is fully transparent, contestable and competitive.
- The existing legislative scheme for the selection of default funds through the FWC and Modern Award should be implemented.
- The Government should fill vacancies on the Expert Panel of the FWC as a matter of urgency to allow this to happen.
- A review of the Stronger Super reforms in 2020, including MySuper, is appropriate, but not on the basis of a predetermined alternative set five years in advance.
- AIST agrees with the Final Report that net returns to members is the critical criteria, and that a focus solely on fees will lead to poor outcomes for superannuation members.
- Any review of MySuper must have net return to members as its key focus, with other issues such as fees and costs viewed as being important, but subsidiary to net returns.
- In the meantime the Government should:
  - Commit to improved disclosure and reporting, especially on fees, performance and related party arrangements;
  - Review the impact of related party costs on super fund members, including through but not necessarily limited to requesting APRA to update the 2010 report examining fees, concentrated markets, and related party transactions<sup>21</sup>;
  - Require the accelerated transition to MySuper of remaining Accrued Default Amounts; and
  - Given that MySuper covers \$395B and Choice covers \$898B, AIST recommends that a timetable for bringing the disclosure and reporting of Choice into line with MySuper needs to be developed in order to provide consumers with consistency and to aide system efficiency. In this way, a more meaningful comparison of MySuper and Choice may be made.

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<sup>21</sup> APRA, (2010). *Working Paper Australian superannuation outsourcing - fees, related parties and concentrated markets*. APRA.

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## 5 Objectives

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### 5.1 FSI Recommendation 9: The objectives of the superannuation system

***Seek broad political agreement for, and enshrine in legislation, the objectives of the superannuation system and report publicly on how policy proposals are consistent with achieving these objectives over the long term.***

#### 5.1.1 Our response

##### 5.1.1.1 *Seeking political agreement on the objectives of the superannuation system*

AIST supports the Final Report recommendation to seek broad political agreement on the objectives for the superannuation system.

This is entirely consistent with the view that we put in our second round submission to the Inquiry about obtaining bipartisan support for legislated objectives of superannuation, including the provision of equitable, adequate and sustainable retirement incomes (also having regard to the relationship with the Age Pension and the health care system).

AIST believes that such an outcome is achievable in the short term, and calls on the Government to announce a structured and concrete approach, with a finite timeframe, as part of its response to the Inquiry.

We note and applaud the recent comments from the Assistant Treasurer, The Hon. Josh Frydenberg MP supporting legislative objective for the superannuation system<sup>22</sup>:

*This recommendation is designed to address one of the most common criticisms of the superannuation system – a lack of certainty and stability in policy settings.*

*For example, the SMSF Association supported the Inquiry’s observation that the lack of stability in superannuation policy settings undermines consumer confidence and trust in the superannuation system.*

*The Inquiry’s preferred model includes enshrining the objectives in legislation and public reporting on how policy proposals are consistent with these objectives.*

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<sup>22</sup> Frydenberg, J. (2015). *Address to the SMSF Association National Conference, 20 February 2015.*

*My view is that a carefully drafted objective – with bipartisan support – would have positive benefits for the stability and accountability of the system and those who play a role in it.*

*I welcome the recent indication from the Shadow Treasurer that he also supports a bipartisan approach in this area.*

These comments in support of legislated objectives have been echoed by the Shadow Treasurer, The Hon. Chris Bowen MP<sup>23</sup>:

*Having an agreed and simple objective would mean that progress could be measured against that objective. It would also mean that new policy ideas could be tested against the criteria of whether they meet that objective.*

*I'm in favour of an agreed objective for the superannuation system and I am more than happy to invest the time and effort to see if we can make that objective bipartisan.*

In the same address, the Shadow Treasurer also stated his wish:

*...that as many Australians as possible have access to the resources for a dignified retirement without recourse to the full age pension."*

The Annual General Meeting of AIST on 18 March 2015 discussed and applauded the emerging bipartisan support for legislated objectives for superannuation.

AIST is committed to working with the Government, other political stakeholders and the rest of the superannuation industry to define the objectives for superannuation.

As a first step in this process, we recommend that the Government directly task Treasury to draft a more detailed discussion paper on the objectives of superannuation based on the recommendations of the Inquiry or commission this from an academic centre that specialises in superannuation and financial services.

Given the widespread support, this should not wait for the Government's comprehensive response to the Inquiry.

The discussion paper should take the broad consensus around the Inquiry's recommendation as the starting point, and address the following questions:

- How should the primary superannuation objective proposed by the Inquiry be drafted?
- How should the subsidiary superannuation objectives proposed by the Inquiry be drafted?

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<sup>23</sup> Bowen, C. (2015). *Address to Centre for International Finance and Regulation.*

- Should the objectives be principle-based or should they include explicit targets? (eg, superannuation replacement rate of 70% of pre-retirement incomes for middle income earners)
- Do the objectives cover the voluntary savings pillar of superannuation as well as the mandatory savings pillar?
- What assumptions, if any, should the objectives make about the level and eligibility for the age pension?
- Is it also a subsidiary objective of superannuation to promote sustainable economic growth through infrastructure investment and otherwise support financial system efficiency?
- Are there other subsidiary objectives that should be considered?
- How should the objectives relate to the sole purpose test?
- How should the objectives relate to other parts of the SIS Act and other legislation?
- What methodology and criteria should be used to measure the success of the superannuation system in meeting its objectives?
- How should this methodology and criteria be developed?
- Should the methodology and criteria also be enshrined in legislation or regulation?
- Should each significant superannuation policy proposal be measured against the objectives?
- Should the overall performance of the retirement income system be measured against the objectives on a regular basis?
- What body should undertake this assessment, and should it be independent from government and the superannuation industry?
- Can the objectives and supporting mechanisms be enshrined in legislation by 1 July 2016?

AIST proposes that the Government convene a summit on the objectives for superannuation at the earliest opportunity during 2015. This summit should involve consumers, employers, the superannuation industry, Government, other political parties and regulators.

In line with the model adopted in constitutional conventions, AIST recommends that the summit be chaired by a representative appointed by the Government, with the deputy chair appointed by the Opposition.

In order to keep the discussion at a high level, and to build on the current level of bipartisan support, AIST also recommends that a brief high-level statement of principles be developed by a preliminary working group based on the discussion paper recommended above.

AIST is committed to achieving a bipartisan outcome on this issue, both politically and at a superannuation industry level. We will provide whatever support we can to encourage industry participants to work together and adopt a common and reasonable member- and system- focused outcome.

### **5.1.1.2 Primary objective**

The Final Report recommends the legislation of both primary and subsidiary objectives for the superannuation system.

The primary objective recommended by the Inquiry is:

*To provide income in retirement to substitute or supplement the Age Pension<sup>24</sup>.*

The recommended objective has two parts; firstly, to provide retirement income, and secondly to put this in the context of the age pension. The first part of the objective already exists, and any change to the construction of this objective must be carefully managed to avoid harm to the superannuation system.

Trustees of regulated superannuation funds already have a primary objective they must comply with.

The primary objective is the sole purpose test prescribed in s62 of the SIS Act. S62 prescribes both core purposes (in s62(1)(a)) and ancillary purposes in s62(1)(b)):

- (1) *Each trustee of a regulated superannuation fund must ensure that the fund is maintained solely:*
  - (a) *for one or more of the following purposes (the **core purposes**):*
    - (i) *the provision of benefits for each member of the fund on or after the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged (whether the member's retirement occurred before, or occurred after, the member joined the fund);*
    - (ii) *the provision of benefits for each member of the fund on or after the member's attainment of an age not less than the age specified in the regulations;*
    - (iii) *the provision of benefits for each member of the fund on or after whichever is the earlier of:*
      - (A) *the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged; or*
      - (B) *the member's attainment of an age not less than the age prescribed for the purposes of subparagraph (ii);*
    - (iv) *the provision of benefits in respect of each member of the fund on or after the member's death, if:*
      - (A) *the death occurred before the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged; and*
      - (B) *the benefits are provided to the member's legal personal representative, to any or all of the member's dependants, or to both;*
    - (v) *the provision of benefits in respect of each member of the fund on or after the member's death, if:*
      - (A) *the death occurred before the member attained the age prescribed for the purposes of subparagraph (ii); and*
      - (B) *the benefits are provided to the member's legal personal representative, to any or all of the member's dependants, or to both; or*

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<sup>24</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia The Treasury, p.95. Available at: <http://tinyurl.com/n7wl3lb> [Accessed 23 Feb. 2015].

(b) for one or more of the core purposes and for one or more of the following purposes (the **ancillary purposes**):

- (i) the provision of benefits for each member of the fund on or after the termination of the member's employment with an employer who had, or any of whose associates had, at any time, contributed to the fund in relation to the member;
- (ii) the provision of benefits for each member of the fund on or after the member's cessation of work, if the work was for gain or reward in any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged and the cessation is on account of ill-health (whether physical or mental);
- (iii) the provision of benefits in respect of each member of the fund on or after the member's death, if:
  - (A) the death occurred after the member's retirement from any business, trade, profession, vocation, calling, occupation or employment in which the member was engaged (whether the member's retirement occurred before, or occurred after, the member joined the fund); and
  - (B) the benefits are provided to the member's legal personal representative, to any or all of the member's dependants, or to both;
- (iv) the provision of benefits in respect of each member of the fund on or after the member's death, if:
  - (A) the death occurred after the member attained the age prescribed for the purposes of subparagraph (a)(ii); and
  - (B) the benefits are provided to the member's legal personal representative, to any or all of the member's dependants, or to both;
- (v) the provision of such other benefits as the Regulator approves in writing

The sole purpose test is a civil penalty provision that can be summarised as requiring trustees to ensure that the fund is maintained solely for the provision of retirement or death benefits. Ancillary purposes include employment termination insurance, salary continuance and other benefits after conditions have been met.

The sole purpose test has helped maintain the integrity of the system, and the legislation of objectives should be built on this base and not supplant or replace it. AIST supports the sole purpose test and argues that the primary objective recommended by the Final Report should be separate and additional.

APRA has provided guidance on the sole purpose test<sup>25</sup> and it has been successfully used to prosecute non-complying superannuation funds for non-retirement purposes<sup>26</sup>. The strong track record of enforcement and high levels of compliance have been significant factors contributing to the integrity of the superannuation system.

25 APRA, (2001). *The sole purpose test*. Superannuation Circular No.III.A.4. [online] Canberra: Australian Prudential Regulation Authority, para 5. Available at: <http://tinyurl.com/nun9af8> [Accessed 24 Mar. 2015].

26 Leow, J., Murphy, S. and Hooper, G. (2013). *Australian Master Superannuation Guide*. 17th ed. North Ryde: CCH. ¶3-200.

*5. The sole purpose test and the associated standards prohibit the use of concessional tax superannuation savings for purposes such as providing pre-retirement benefits to members, benefits to employer-sponsors or facilitating estate planning. The sole purpose test, with the prescribed SIS investment restrictions, ensures that the retirement income objective is paramount.<sup>27</sup>*

The Final Report stated that the legislative objectives recommended by the FSI should not be used by courts to interpret law. This is in contrast to the sole purpose test which is an important governor of the operation of individual superannuation funds.

Both the sole purpose test legislation and the consequent case law have played an important role in maintaining the integrity of the superannuation system and should not be disturbed. AIST agrees that the emphasis of the superannuation system should be on providing income (rather than benefits *per se*) but notes that in the quote above, the regulator APRA has characterised the sole purpose test as being the foundation of the “retirement income objective”.

The second part of the recommended objective is for superannuation-sourced income to substitute or supplement the Age Pension. This part of the recommendation also has two components that AIST responds to in turn.

Firstly, AIST supports the implication in the recommendation that the purpose of superannuation should be about the provision of retirement *income* (rather than, for example, for lump sum benefits taken from superannuation to support retirement). This commentary is further developed in this submission in the section on post-retirement arrangements.

Secondly, AIST supports the view that this retirement income should be seen in the context of substituting or supplementing the Age Pension, both at an individual and a system level.

It is clear from a reading of the Final Report that the options of substituting or supplementing the age pension are to be seen at an individual level, with individuals at different income levels interacting with the age pension in different ways.

*Those with small balances are likely to continue to take their benefit as a lump sum and rely primarily on income from the Age Pension. Individuals with very high balances may be able to generate satisfactory retirement income from an account-based pension, drawn down at minimum rates<sup>28</sup>.*

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<sup>27</sup> APRA, (2001). *The sole purpose test*. Superannuation Circular No.III.A.4. [online] Canberra: Australian Prudential Regulation Authority, p.1. Available at: <http://tinyurl.com/nun9af8> [Accessed 24 Mar. 2015].

<sup>28</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia The Treasury, p.124. Available at: <http://tinyurl.com/n7wl3lb> [Accessed 23 Feb. 2015].

The Inquiry is not suggesting the abolition of the age pension as a long term goal, but is suggesting (explicitly, as a subsidiary objective) the alleviation of fiscal pressures on Government from the retirement income system.

AIST submits that the Intergenerational Report 2015 supports this balanced view about the provision of both the age pension and superannuation retirement income, and hence this perspective on the primary objective of superannuation.

### **5.1.1.3 *Subsidiary objectives of the superannuation system***

AIST supports the codification of the subsidiary objectives of the superannuation system. These may include the subsidiary objectives proposed by the Final Report. AIST further supports the development and refinement of subsidiary objects on a consensus basis at the superannuation objectives' summit recommended earlier in this part.

The alleviation of fiscal pressures on Government from the retirement income system may be appropriate as a subsidiary objective, as a well-functioning retirement income system will achieve an appropriate equilibrium between the age pension, superannuation and other assets. The economic modelling in the Intergenerational Report also shows the higher retirement incomes of Australian retirees as the superannuation system matures and reflects this as a restraining influence on Australian Government spending on age-related pensions over time.

AIST does however side with those who argue the importance of the superannuation system for national saving and funding economic activity, and submits that the Government should include nation-building as a subsidiary objective.

As well as providing retirement incomes, the superannuation savings pool acts to create sustainable economic growth. It does so by investing in Australia's infrastructure and promoting efficiency in the broader financial system. AIST submits that policy settings should assist (though, not direct) super funds to invest in infrastructure and build the Australian economy, and list nation-building as a subsidiary.

However, a lack of fairness and equity are a major challenge to the operation of the current retirement income system. As the Final Report records, the highest income decile in Australia receives a disproportionate share of superannuation tax concessions. This is compounded by the superannuation gender gap – women on average have approximately half the superannuation balances of men both during their working lives and at retirement. As has been widely documented this is a function of both lower average incomes and longer career breaks. Consideration should also be given to the achievement of fairer outcomes as a subsidiary objective.

In the Final Report there is discussion attempting to differentiate causation from correlation, and objectives from the consequences of actions. AIST is not confident that all of these issues have been fully (or accurately) thought through or resolved. We are concerned to ensure that final positions are not developed before all of these issues have been thoroughly addressed. To do otherwise will result in

unintended consequences, and ongoing confusion about the objectives of the retirement income system. A summit on the objectives of superannuation would be an important step in the careful and considered resolution of these matters.

#### **5.1.1.4 How to assess superannuation system performance and policy changes**

The Final Report generally proposes an ad hoc approach to assessing the performance of the superannuation system against the proposed objectives. While the Final Report identifies proposed objectives it does not set out how the objectives should be objectively measured.

AIST submits that an objective measure of superannuation performance is a critical adjunct to the setting and assessing of objectives and should be developed as a matter of urgency.

Within this context, AIST has developed the AIST Mercer Super Tracker to assess the progress of the retirement income system based on available evidence and to support a reasoned discussion about the system's ongoing progress. The Tracker will be used by AIST for this purpose, but is also presented to governments and others as a starting point or potential framework to measure performance against superannuation objectives.

The Super Tracker has considered several indicators under the broad headings on adequacy and sustainability. There is a natural and healthy tension between adequacy and sustainability. It is important to recognise the importance of both providing adequate benefits and long term sustainability.

Notable findings from the Tracker included scores for equity, the gender gap, superannuation coverage, personal contributions, cost of government support, and length of retirement. The scores highlighted the need for improvement in the areas of tax, gender and workforce participation. The Tracker will be used to test a number of different scenarios and can be used to help shape policy positions and measure the performance of the retirement income system.

A copy of the inaugural AIST Mercer Super Tracker report of March 2015 'How the super system stacks up on fairness, adequacy and sustainability' is attached to this submission as a separate document.

#### **5.1.1.5 What body should assess superannuation system performance?**

AIST supports the recommended inclusion of this assessment in Regulatory Impact Statements but argues that this needs to be soundly and empirically-based. A periodic assessment by governments, as suggested in the Final Report, runs the risk of the process being captured by short term considerations and is open to tinkering. It is not supported by AIST.

The Inquiry considered but dismissed the establishment of an independent publicly-funded body to assess the superannuation system's performance and report on superannuation policy changes. It did so largely on the basis of concern about appropriate accountability mechanisms.

AIST supports the establishment of an independent publicly-funded body for this role and urges the Government to revisit this issue. The funding of such a body should be subject to regular review by

Government, with the funding tied to a performance audit undertaken as part of a review. While the body should be chosen following a competitive evaluation or tender process, AIST notes that bodies such as the Australian Centre for Financial Studies or the Centre for Financial Regulation may be suitable for this task.

This body should use objective measures such as the Super Tracker to assess performance and policy against the key principles of fairness, adequacy and sustainability. While of itself this will not guarantee impartiality or consensus, it will nonetheless institutionalise a process that will add transparency, objectivity and stability.

## 5.2 Our recommendations

- AIST supports legislating the objectives of the superannuation system.
- The Government should urgently convene a summit to reach bipartisan agreement on the objectives of the superannuation system.
- AIST supports a primary objective of the superannuation system that recognises the primacy of providing adequate income in retirement, and accepts that this may substitute or supplement the age pension.
- The implementation of this objective should be designed so as not to interfere with the operation of the sole purpose test.
- AIST supports the codification of the subsidiary objectives of the superannuation system, with the subsidiary objectives proposed in the Final Report (and other proposed by stakeholders) to be further considered and refined at the summit.
- The role of the superannuation system in national saving and funding economic activity, especially infrastructure, should be identified as a subsidiary objective.
- Consideration should also be given to the achievement of fairer outcomes, especially to address the gender gap, as a subsidiary objective.
- There should be an objective way of measuring the performance of the superannuation system and proposed policy changes against the legislated objectives.
- The AIST Mercer Super Tracker provides a robust example of how this might be done.
- This assessment should not be undertaken on an ad hoc basis nor should it be undertaken by Government.
- The assessment should be undertaken by an independent, publicly funded body.

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## 6 Consumer outcomes

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### 6.1 FSI Recommendation 12: Choice of fund

***Provide all employees with the ability to choose the fund into which their Superannuation Guarantee contributions are paid.***

#### 6.1.1 Our response

The Final Report came to the view that the absence of choice is a barrier to members engaging with their superannuation, and that this barrier should be removed. In coming to this view, the Final Report approvingly noted submissions that highlighted the benefit of choice in providing flexibility for members and lowering fees through greater competition. The Final Report also asserted that this exemption to choice also contributed to employees having multiple accounts and paying multiple sets of fees.

The Final Report identifies employees in super funds nominated in enterprise agreements, workplace determinations or state-based awards as being particularly in this category. AIST also notes that persons covered by constitutionally-exempt superannuation funds and many defined benefit funds closed to new entrants are also in this category.

A common characteristic of many of these environments not providing choice of fund is that they often provide benefits in excess of that provided by the *Superannuation Guarantee (Administration) Act 1992*, including additional employer contributions (or their equivalent in the case of Defined Benefit funds), insurance, and, in the case of some government funds, guaranteed levels of retirement benefits. It is therefore not in the interests of members of such funds to switch into superannuation funds that offer lesser benefits and may remove certainty and security.

AIST disagrees with the underlying assumption of the Final Report that choice of fund will result in members becoming more engaged and making decisions that are in their financial best interests, and that this benefit should therefore be made available to all superannuation fund members. The experience of the past decade does not support this.

The *Superannuation Legislation Amendment (Choice of Superannuation Funds) Act 2004* became effective on 1 July 2005, almost ten years ago. It allowed many employees to choose which superannuation fund received their mandatory Superannuation Guarantee contribution. The Government at the time argued that choice would result in greater engagement, lower fees, and allow fund members more options to choose the investment strategy that was right for them.

This outcome has not been realised. It was the conclusion of the Super System Review that:

*The Panel therefore accepts that the model of member-driven competition through ‘choice of fund’ (in the form of SG Act choice and consequent portability) has struggled to deliver a competitive market that reduces costs for members.<sup>29</sup>*

...

*A key tenet of the 1997 Wallis Report was that super fund members should be treated as rational and informed investors, with disclosure and market conduct controls being the main regulatory instruments with which to oversee the industry. More specifically, these settings assume that members have the tools at their disposal, and the necessary regulatory protections in the market place, to enable them to make optimal decisions about their investment strategies, about when to enter and exit the market, and about what to do with their super on reaching retirement. In a compulsory system, it also assumes that members have the requisite degree of interest.*

*But, for many members, this is not the case.<sup>30</sup>*

After citing the 2006 *Adult Literacy and Life Skills Survey of Australians* published by the Australian Bureau of Statistics (ABS) in January 2008, the Super System Review also concluded:

*While these financial literacy statistics are stark, the fact remains that a compulsory system based on informed investors making rational choices fails to confront this reality<sup>31</sup>.*

While the Final Report recycled the arguments used in 2005 to support choice of fund, it did not present any evidence to counter the conclusions reached by the Super System Review in 2010. Five years later, and notwithstanding the introduction of MySuper to further protect disengaged and disinterested members, this remains the case.

Furthermore, a headline finding of the Final Report was that fees in superannuation have not reduced significantly in the period since the introduction of choice of fund. What has happened in the past decade is that superannuation funds have greatly increased the number of investment options that they have available, providing members with more and more investment choices within their existing superannuation

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<sup>29</sup> Cooper, J., Casey, K., Evans, G., Grant, S., Gruen, D., Heffron, M., Martin, I. and Wilson, B. (2012). *Super System Review Final Report Part One Overview and Recommendations*. [online] Canberra: Commonwealth of Australia, Attorney-General's Department, p.8. Available at: <http://tinyurl.com/njmq3wo> [Accessed 25 Mar. 2015].

<sup>30</sup> Cooper, J., Casey, K., Evans, G., Grant, S., Gruen, D., Heffron, M., Martin, I. and Wilson, B. (2012). *Super System Review Final Report Part One Overview and Recommendations*. [online] Canberra: Commonwealth of Australia, Attorney-General's Department, p.8. Available at: <http://tinyurl.com/njmq3wo> [Accessed 25 Mar. 2015].

<sup>31</sup> Cooper, J., Casey, K., Evans, G., Grant, S., Gruen, D., Heffron, M., Martin, I. and Wilson, B. (2012). *Super System Review Final Report Part One Overview and Recommendations*. [online] Canberra: Commonwealth of Australia, Attorney-General's Department, p.8. Available at: <http://tinyurl.com/njmq3wo> [Accessed 25 Mar. 2015].

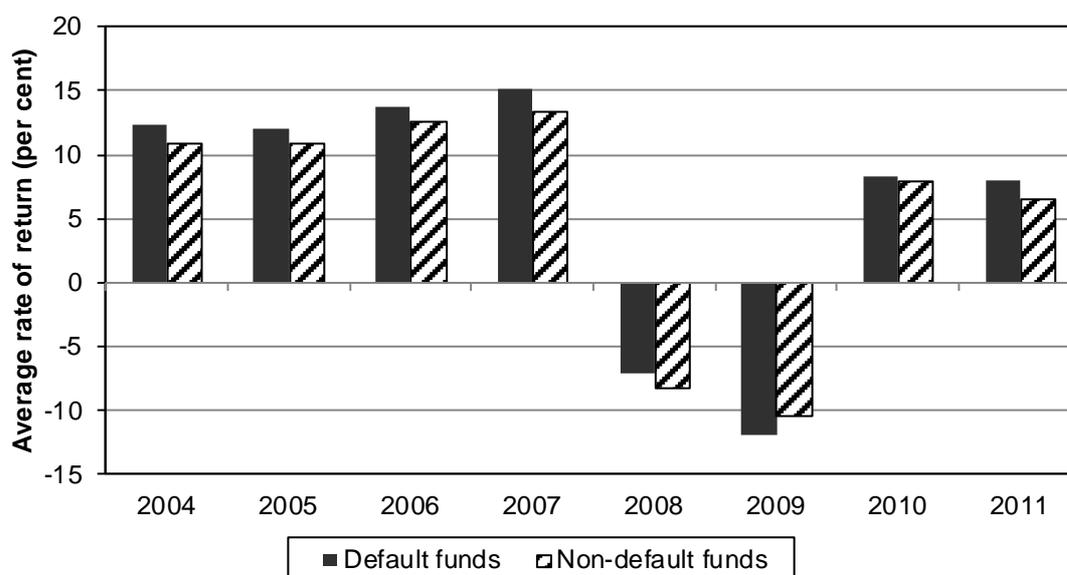
fund. This phenomenon is evident in defined contribution superannuation funds available to members not able to choose their superannuation fund.

In contrast, however, is the clear evidence that superannuation funds listed in Awards deliver higher investment returns than those not listed in Awards? An analysis of comparative performance was undertaken by the Productivity Commission inquiry into *Default Superannuation Funds in Modern Awards*.

*The investment performance of default funds listed in modern awards has been relatively strong when compared to non-default funds. Over the eight years to 30 June 2011, default funds averaged an annual (after tax) rate of return of 6.4 per cent, compared with 5.5 per cent for non-default funds, and default funds collectively outperformed non-default funds in each year except 2009 (figure 4.1 – see below).<sup>32</sup>*

**Figure 4.1 Superannuation fund performance**

Default funds versus non-default funds



Sources: Productivity Commission estimates based on APRA fund-level profiles and financial performance data 2011 (APRA 2012j); FWA (2012e)

<sup>32</sup> Productivity Commission, (2012). *Default Superannuation Funds in Modern Awards*. Report No. 60, Final Inquiry Report. [online] Canberra: Productivity Commission, p.73. Available at: <http://tinyurl.com/qxct8jo> [Accessed 25 Mar. 2015].

The Final Report also asserted that the absence of choice also contributed to employees having multiple accounts. However, ASIC in its initial submission noted that choice of fund had not resulted in a reduction of duplicated accounts:

*These [choice of superannuation fund] changes also made it possible for members with multiple accounts to more easily consolidate these accounts and reduce the amount of fees they pay for maintaining multiple accounts. However, in practice, this consolidation did not lead to a decrease in the number of accounts in the industry. The number of accounts continued to grow to more than 30 million, even though the number of employed persons in Australia is roughly 40% of this number. This means that for every employed person there are approximately 2.5 accounts. A large number of these accounts are small, unclaimed or lost and some are for retirees receiving superannuation in the form of a pension<sup>33</sup>.*

Finally, the Final Report asserts that lack of choice contributes to disengagement with superannuation but does not provide any evidence to support this. While the low level of engagement in superannuation is universally accepted (along with the concomitant issue of financial illiteracy mentioned above), there is no evidence of higher disengagement amongst members with no choice of fund compared with members in a default fund environment where other superannuation funds can be chosen.

### 6.1.2 Conclusion

In the above paragraphs, AIST has demonstrated that the problem the Final Report's recommendation sought to address does not exist. Lack of choice does not contribute to multiple superannuation accounts, or higher fees, and default funds listed in Awards generally deliver higher returns.

Therefore, beyond the Final Report's general statement of belief that everyone should be able to choose the fund that receives their SG contributions, the Inquiry has not made out the case in support of this recommendation. AIST calls on the Government to support its response to this recommendation with evidence.

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<sup>33</sup> ASIC, (2014). *Financial System Inquiry: Submission by the Australian Securities and Investments Commission*. April 2014. [pdf] Canberra: Australian Securities & Investments Commission, p.227. Available at: <http://tinyurl.com/pptq436> [Accessed 25 Mar. 2015].

## 6.2 FSI Recommendation 23: Facilitate innovative disclosure

***Remove regulatory impediments to innovative product disclosure and communication with consumers, and improve the way risk and fees are communicated to consumers.***

### 6.2.1 Our response

#### 6.2.1.1 Remove regulatory impediments to innovative product disclosure

AIST agrees with the FSI Final Report's recommendation to remove regulatory impediments to innovative product disclosure and communication. During the Financial Services Inquiry, ASIC has released Consultation Paper 224 *Facilitating electronic financial services disclosure* as well as draft Regulatory Guide 2221. In our submission to ASIC<sup>34</sup>, we have strongly supported the use of electronic disclosure as well as the opportunity to develop more innovative PDSs. AIST has estimated that between 25-50% per annum of current communication costs could be saved. AIST has recommended that a Working Group be established to help develop greater guidance, including consumer testing outcomes, defining e-addresses and electronic 'delivery', and refining storage, retrieval and archiving of electronic materials.

#### 6.2.1.2 Improve the way risk is communicated to members

AIST agrees with the FSI Final Report comments that (with the exception of the new standard risk measure – 'SRM') the law generally does not provide detailed requirements on how to disclose risk. In relation to the SRM, AIST notes that the measure's current label suggests that it gives a general indication of investment risk. In fact, the measure captures annual downside volatility, expressed over a 20-year period. This misrepresentation may be against the member's interest. AIST strongly recommends that the measure be renamed and suggest "Volatility Rating" or "Downside Risk Measure".

By itself, the SRM is misleading and inappropriate for members who are in a mandatory long term investment environment. The use of a downside volatility measure without full explanation and without the use of other risk measures would potentially encourage more consumers to reduce volatility, and therefore reduce long-term expected returns.

A measure of long-term risk is also needed to help members seeking long-term growth understand which investment option has a high probability of delivering this growth, and a low risk of not delivering it. At the same time, the SRM would also show that this option has a greater risk of short-term volatility and negative

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<sup>34</sup> AIST, (2015). *ASIC Consultation Paper 224 Facilitating electronic financial services disclosure 30 January 2015*. [online] AIST. Available at: <http://tinyurl.com/ncmf5jm> [Accessed 26 Mar. 2015].

returns. AIST has provided detail regarding these issues in its submission<sup>35</sup> to the *Better regulation and governance, enhanced transparency and improved competition* in superannuation discussion paper.

### 6.2.1.3 *Improve the way fees are communicated to members*

AIST agrees with the FSI Final Report comments that further improvements to fee disclosure could be made. AIST has welcomed ASIC's review of Regulatory Guide 97 *Disclosing fees and costs in PDSs and periodic statements*. In our submission to ASIC<sup>36</sup>, AIST has recommended that Regulatory Guide 97 could be further improved through clarifying interposed vehicles, disclosing actual performance fees, not carving out listed vehicles, prescribing calculation methodologies, and aligning disclosure with APRA reporting requirements. AIST also strongly supports better disclosure of related party payments and a separate review of insurance disclosure.

## 6.3 FSI Recommendation 24: Align the interests of financial firms and consumers

***Better align the interests of financial firms with those of consumers by raising industry standards, enhancing the power to ban individuals from management and ensuring remuneration structures in life insurance and stockbroking do not affect the quality of financial advice.***

### 6.3.1 Our response

#### 6.3.1.1 *Raising industry standards*

We agree with the Final Report's conclusions that by raising the standards of the industry, confidence and trust in the financial system will increase. AIST supported the creation of a central body to set financial adviser professional, ethical and educational standards, and believes that this model can be the basis for similar professionals throughout the financial services industry.

The *Interim Report of the Financial System Inquiry* highlighted a need to increase professionalism in financial advice. Submissions to the Inquiry noted quality of personal advice as an ongoing problem<sup>37</sup>, with the report citing relatively low minimum competence requirements applicable to financial advisers and varying standards of competence as key issues in advice.

<sup>35</sup> AIST, (2014). *Discussion Paper: Better regulation and governance, enhanced transparency and improved competition in superannuation* February 2014. [online] AIST. Available at: <http://tinyurl.com/knrq2uc> [Accessed 26 Mar. 2015].

<sup>36</sup> AIST, (2015). *ASIC Review of Regulatory Guide 97 – Disclosing fees and costs in PDSs and periodic statements* 27 February 2015. [online] AIST. Available at: <http://tinyurl.com/ogyg3fb> [Accessed 26 Mar. 2015].

<sup>37</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). *Financial System Inquiry Interim Report*. [pdf] Canberra: Commonwealth of Australia The Treasury, p.3-67. Available at: <http://tinyurl.com/n7wl3lb> [Accessed 24 Mar. 2015].

The *Final Report of the Senate Economics Committee Inquiry into ASIC* found standards to be inadequate and recommended minimum education standards of a relevant university degree and three years' experience over a five-year period for advisers, as well as minimum continuing professional development requirements<sup>38</sup>. Following this inquiry, the Commonwealth Bank announced new minimum education standards for Commonwealth Financial Planning Limited (CFPL) financial planners, supervisors and managers of planners<sup>39</sup>. This has now been emulated by most of the major banks.

However, standards remain low in the industry, with ASIC's shadow-shopping research pointing to advice not generally being of a "sufficiently high standard"<sup>40</sup>, as well as recent media exposure in relation to cheating on exams.

### **6.3.1.2 Enhanced banning powers**

AIST supports moves to provide the financial services regulator with enhanced powers to ban individuals from managing or holding certain offices within financial firms. However, this is subject to ensuring that there is sufficient resourcing available to ASIC in order to enable it to perform this function properly.

### **6.3.1.3 Amendments to remuneration structures in life insurance and stockbroking**

AIST supports the recommended amendments to commission arrangements in life insurance and stockbroking in principle; however, this must be viewed in the context in which they exist. Since the start of consultations on the FOFA measures, AIST has opposed commissions on financial products in principle, and notes that measures aimed at eliminating commissions from financial products were watered down to exempt insurance products and stockbrokers.

We note that in the case of life insurance and stockbrokers, the exemptions provided lead to odd outcomes which could (and does) lead to regulatory arbitrage. For example, life insurance on superannuation within MySuper products are banned from paying commissions, however, this exemption does not exist, for example, with individually underwritten non-super life insurance.

We also note the lack of protection for investors who are not retail investors. Presently, it is possible to be considered a "sophisticated investor" on the basis of the opinion of an accountant. This situation has

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<sup>38</sup> Senate Economics References Committee, (2014). *Performance of the Australian Securities and Investments Commission*. [online] Canberra: Commonwealth of Australia, Recommendation 42. Available at: <http://tinyurl.com/ob8vhk7> [Accessed 25 Mar. 2015].

<sup>39</sup> Commonwealth Bank of Australia, (2014). *Commonwealth Bank raises educational standards for financial planners*. [online] Available at: <http://tinyurl.com/mxh2osp> [Accessed 24 Mar. 2015].

<sup>40</sup> ASIC, (2012). *Shadow shopping study of retirement advice*. Report REP 279. [online] Canberra: Australian Securities & Investments Commission. Available at: <http://tinyurl.com/kfqhzo> [Accessed 24 Mar. 2015].

resulted in the absurd situation where wealth managers have been sending pre-written statements to accountants to sign, in order to protect their advisers<sup>41</sup>.

AIST continues to support the eventual removal of conflicted remuneration from all financial products in the interests of all investors. We would therefore support this recommendation as part of a broader plan to phase these out entirely.

## 6.4 FSI Recommendation 25: Raise the competency of advisers

***Raise the competency of financial advice providers and introduce an enhanced register of advisers.***

### 6.4.1 Our response

AIST welcomes the Government's commitment to a national register of financial planners which will include qualifications and membership of professional bodies. Disclosure of what qualifications financial planners have is important – but the level of qualifications financial planners are required to have is far more important.

AIST notes that the United States, the United Kingdom, Canada, Singapore and Hong Kong all have national examination approaches to adviser competency.

Superannuation in Australia has \$1.93 trillion in assets under management, and yet those giving consumers advice are not subject to consistent and transparent education requirements. And this leads to a lack of properly trained financial planners as well as an erosion of consumer confidence. To this end, AIST quotes an article by Adele Ferguson in *The Age* from 1 December 2014<sup>42</sup>:

*The banking sector has proved to be a powerful lobby group. It knows the planning industry needs to lift its game, as outlined in a confidential report sent to [then Acting Assistant Treasurer the Hon. Mathias] Cormann [MP] just over a week ago into the professional, ethical and educational standards of financial planners. The working party, which included the banks' lobby groups, agreed the existing minimum education and training standards were inadequate and a "lack of consistent ethics and conduct standards causes divergences of practices across the industry" but they couldn't agree how to do it, which effectively ensures it won't proceed.*

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<sup>41</sup> Ferguson, A. and Butler, B. (2014). Macquarie advisers cheated on competency test and exposed clients., *The Sydney Morning Herald*. [online] Available at: <http://tinyurl.com/pbns7f9> [Accessed 23 Mar. 2015].

<sup>42</sup> Ferguson, A. (2014). New battle looms as Treasury waters down financial adviser register. *The Age*. [online] Available at: <http://tinyurl.com/m82xtre> [Accessed 5 Dec. 2014].

This points to the need for legislative prescription regarding qualifications and ongoing training.

AIST also welcomes the Government's interest in a central body, which will set educational and competency standards for financial advisers, as recommended by the Parliamentary Joint Committee on Corporations and Financial Services. However, we believe that this resource could go further. We believe that in addition to a centralised advisers' exam and education and competency standards, the body could also set professional and ethical standards. Such standards setting would only improve the faith that investors can have when they see an adviser.

AIST supports improved industry standards in financial services. We note that the recommendation to implement an enhanced register of financial advisers is already in the process of implementation, and we support this measure.

Our submission to the recent inquiry into financial advice standards held by the Parliamentary Joint Committee on Corporations and Financial Services welcomed proposals to lift professional, ethical and education standards in the financial services industry.

## 6.5 FSI Recommendation 37: Superannuation member engagement

***Publish retirement income projections on member statements from defined contribution superannuation schemes using Australian Securities and Investments Commission (ASIC) regulatory guidance.***

***Facilitate access to consolidated superannuation information from the Australian Taxation Office to use with ASIC's and superannuation funds' retirement income projection calculators.***

### 6.5.1 Our response

AIST supports more widespread use of standardised projections to encourage greater member engagement. We have recently commissioned research on projections based on stakeholder consultations. We include suggestions resulting from that research.

### 6.5.2 Value of projections

Individual defined contribution superannuation fund members bear substantial responsibility for decision-making and also the risks resulting from those decisions. Important decisions include whether or not to make voluntary contributions and what investment option to choose. These decisions can have a substantial impact on the adequacy of retirement income.

Yet a lack of engagement and understanding around superannuation remain key issues in Australia. Investment products and pricing represent complicated and unfamiliar terrain for most workers, and few young workers are focused on planning for retirement. Tools to increase engagement and understanding, and promote positive action in retirement planning will deliver benefit to many workers.

Superannuation projections are such a tool. Funds can estimate the member's balance at retirement and the income it will generate in retirement based on some of the member's details, including their age, current balance and recent contributions. These estimates can be delivered to members along with periodic account statements. Cbus Super, for example, has surveyed members after offering projections on a trial basis in 2013 and found a high degree of member approval and a reasonable level of comprehension.

### 6.5.3 Current regulation of projections

There is currently some ambiguity as to whether projections sent to members on member account statements constitute personal advice, and consequently require a significant degree of verification and disclosure.

ASIC recognises the value of projections to members and the cost to providers of individual interaction with the member. In an attempt to facilitate greater use of projections, ASIC has issued class orders and regulatory guides (most recently CO 14/870 and RG 229) to give industry an indication of what it sees as conduct that would be exempted from the rules for disclosure around personal advice.

ASIC's approach emphasises simplicity, transparency and comparability. The model for projections described in this class order and regulatory guide is consequently prescriptive. It details the formula to be used, the values for a number of the variables in the formula, and how to generate the variables that relate to the individual.

AIST's stakeholders were supportive of having comparable and consistent projections; however, most were of the view that ASIC's guidance could be improved on in several ways. Suggestions included that the guidance should:

1. Accommodate legislated future increases in SG contributions;
2. Quantify investment risk such as through presentation of a range;
3. Allow comparative projections to give members an indication of how a change to their current behaviour – such as a voluntary contribution or a switch in investment option – might impact their outcomes in retirement; and
4. Include estimation of the public pension's contribution to retirement income over the whole of retirement, rather than just at the point of retirement.

### 6.5.4 Conclusion

Although well-intentioned, the current approach to projections has been ineffective. Our understanding is that relatively few funds offer projections, and only a few that do rely on the guidance provided by ASIC. Most funds that do provide projections are relying not on ASIC's exemption but instead on legal advice that projections are not personal advice. This advice gives those funds freedom to generate projections using a different formula and variables than those suggested by ASIC.

## 6.6 FSI Recommendation 40: Provision of financial advice and mortgage broking

***Rename 'general advice' and require advisers and mortgage brokers to disclose ownership structures.***

### 6.6.1 Our response

AIST supports the recommendation with respect to ownership structures, however we believe that the recommendation to re-label 'general advice' as 'sales' is based on invalid assumptions and is likely to mislead investors.

#### 6.6.1.1 Renaming 'general advice' as 'sales'

AIST is concerned with the proposed re-label of general advice as 'sales'. It should be noted that 'general advice' is a category of financial product advice, which refers to a specific definition in the Corporations Act. General advice is not designed to address any specific goals or objectives of a client's situation, and can make recommendations as general as a mere broad statement such as, "people need more super".

The re-labelling of conflicted advice as sales has its merits, but only in the instance that conflicts are allowed to continue. AIST has recommended throughout this submission that conflicted remuneration be totally phased out in all instances, and we would consider that this should extend to all inducements into financial products.

We note that there is still a need for non-conflicted general advice for superannuation fund members. The funds which AIST represents employ a large number of people, a considerable number of whom provide a general advice service to members. These professionals can be in such disparate roles as:

- Member education officers;
- Business development officers;
- Graphic and web designers;
- Investment managers; and
- Trustee directors;

Most of these representatives provide a general financial product advice service, which is not subject to conflicts, financial or otherwise. Referring to these representatives as providing a 'sales' service would therefore be a nonsense, as these services are usually provided in support of existing members. In addition, calling these services 'sales' would mislead and/or deceive fund members into believing that they are conflicted, where they are not.

In addition, the notion that retirement projections are conceptually sales tools is dangerous and cynical.

### 6.6.1.2 Ownership structure disclosure/independent advisers

Finally, with respect to ownership structures, AIST wishes to state the overarching commercial context within which financial planning within Australia operates:

- According to the Customer Owned Banking Association, Australia has the most concentrated banking sector of any G20 country<sup>43</sup>.
- Rainmaker notes that the four largest banks, their wealth arms and AMP have coverage of over 55% of all financial planners and 79% of all platform advisers<sup>44</sup>.
- Of the approximately 18,000 financial planners, less than one-third are certified financial planners<sup>45</sup>, which among other things requires an approved tertiary degree.
- Such conflicts of interest have detrimentally flowed onto consumers in various financial planning scandals, including in recent times the Commonwealth Bank and Macquarie Bank.

We also note the structural conflict of interest arising from not having a clean separation of banking from wealth management.

Additionally, Australia has a predominately defined contribution system where the burden of fees and risk (including investment risk) is borne by the consumer.

Consequently, we support the clearer labelling of both the aligned nature of advisers and the broader conglomerate which is being represented by a financial adviser, together with strict rules on whether an adviser is independent or not. This should extend to whether an aligned adviser holds themselves out (either explicitly or implicitly) as an independent adviser.

## 6.7 Our recommendations

**Increasing standards:** AIST supports the creation of a central body to set financial adviser professional, ethical and educational standards, and believes that this model can be the basis for similar professionals throughout the financial services industry.

AIST supports enhanced banning powers of ASIC subject to increased resourcing measures:

- 1. Increased education and training standards for financial advisers.** AIST recommends a minimum relevant degree qualification for advisers giving personal advice, together with a national exam,

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<sup>43</sup> Williams, M. (2014). Too-big-to-fail banks getting bigger. *AB+F*. [online] Available at: <http://tinyurl.com/pvbdmfl> [Accessed 5 Dec. 2014].

<sup>44</sup> Rainmaker's Financial Planning Report, Volume 3, No.1 February 2014

<sup>45</sup> Ferguson, A. (2014). New battle looms as Treasury waters down financial adviser register. *The Age*. [online] Available at: <http://tinyurl.com/m82xtre> [Accessed 5 Dec. 2014].

mandatory continuing professional development (CPD) requirements and mandatory monitoring and supervision for all new financial advisers.

- 2. Improving professionalism within the industry.** AIST recommends that all forms of conflicted remuneration are banned, the advisers' best interest duty is principles based (similar to that for trustees), a uniform and compulsory code of conduct, enshrinement in law of the term "financial adviser/planner" and clearer labelling of independent advisers.
- 3. Improved minimum education, professional and ethical standards set by a central body.** Such a body must be independent from government and professional associations, however would have representation from these entities as well as consumer organisations, education providers and other relevant stakeholders.

#### Recommendations on innovative disclosure:

- 1. AIST strongly endorses ASIC's work to facilitate electronic disclosure and more innovative PDSs.** AIST has recommended that a Working Group be established to help develop greater guidance, including consumer testing outcomes, defining e-addresses and electronic 'delivery', and refining storage, retrieval and archiving of electronic materials.
- 2. AIST strongly recommends that the Standard Risk Measure be renamed** and suggests "Volatility Rating" or "Downside Risk Measure".
- 3. A measure of long-term risk** is also needed to help members seeking long-term growth understand which investment option has a high probability of delivering this growth, and a low risk of not delivering it.
- 4. AIST strongly supports the work ASIC is undertaking to improve fee disclosure.** AIST has recommended to ASIC that Regulatory Guide 97 could be further improved through clarifying interposed vehicles, disclosing actual performance fees, not carving out listed vehicles, prescribing calculation methodologies, and aligning disclosure with APRA reporting requirements. AIST also strongly supports better disclosure of related party payments and a separate review of insurance disclosure.

AIST endorses FSI recommendation 37 that facilitates greater use of standard projections, including through estimation of combined multiple accounts with ATO input.

We note that review of the definition of general advice (as per recommendation 40) may have implications for the current guidance around projections.

We support standardisation of projections for the sake of transparency and comparability. However, consultation with our stakeholders indicates that the projections would be more useful for members and more widely used by funds if the standard calculation took into account future SG increases and the value of the public pension over the whole of retirement, allowed a presentation of risk and alternate projections based on basic changes to a members' current settings.

AIST recommends that the term 'general advice' be allowed for professionals who provide financial product advice where such advice is non-conflicted.

AIST supports the relabelling of general advice as 'sales' but only where this is conflicted, such as the current situation with banking or general insurance products. AIST does not support conflicted sales roles in financial services.

AIST recommends clearer labelling of both the broader conglomerate which is being represented by a financial adviser, together with strict rules on whether an adviser is independent or not. This should extend to whether an aligned adviser holds themselves out (either explicitly or implicitly) as an independent adviser.

AIST recommends that financial planners:

- Be tertiary qualified where giving personal advice.
- Complete a national exam for new and existing financial planners with mandatory competencies including ethics and conduct.
- Satisfy mandatory Continual Professional Development requirements.
  - AIST supports widespread use of standardised projections to encourage greater member engagement, and therefore endorses FSI recommendation 37 (publish projections on member statements based on ASIC regulatory guidance). We also note the relevance of recommendation 40 (reconsider the definition of general advice) as to how projections are regulated.

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## 7 Retirement incomes

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### 7.1 FSI Recommendation 11: The retirement phase of superannuation

***Require superannuation trustees to pre-select a comprehensive income product for members' retirement. The product would commence on the member's instruction, or the member may choose to take their benefits in another way. Impediments to product development should be removed.***

#### 7.1.1 Our response

AIST supports the development of clear retirement solutions to benefit the members of Australian superannuation funds.

However, AIST submits that there are four main structural principles upon which a robust and fair system of retirement income solutions should be built. In addition, there are significant questions of a tax nature that need to be addressed with respect to retirement incomes.

AIST also notes that existing retirement products provide an adequate retirement solution for many people, and are a comparatively simple and easy to understand product. Existing income stream products are already provided by most not-for-profit funds in the form of account-based income streams and are appropriate for many, especially those with lower income balances.

The superannuation system is still maturing. The Superannuation Guarantee only reached 9% in 2002, having commenced at 3% in 1992) and will only reach 12% in 2025 under current legislative stings. Superannuation coverage is not universal and many people, especially women, have extended career gaps. As a consequence, average retirement balances are not high. AIST has member funds whose average retirement benefits are considerably less than \$50,000. It may not be in the best interests of members with lower account balances to be placed into a longevity product.

Finally, AIST is not aware of evidence to support the mandating of a single retirement income strategy for all superannuation fund members.

It is AIST's recommendation that these concerns be addressed prior to any hasty implementation of product design.

#### 7.1.2 AIST statement of retirement income principles

AIST submits that there are four structural principles around retirement income objectives, member best interests, adequate disclosure and management of longevity that must underpin any recommendations regarding retirement income streams. These principles were also raised in our submission to Treasury's retirement income review in 2014.

AIST strongly argues that an industry-wide strategy for the retirement stage of superannuation needs to be developed on a bipartisan basis, with this then used to construct a regulatory framework for retirement. While AIST recognises that product manufacturers can make a useful contribution to the debate, the design of specific products should not determine the shape of the retirement system. Rather, product design should be focused on fulfilling the requirements of the overall retirement strategy.

#### **7.1.2.1 Principle 1**

There must be a clear set of objectives for retirement incomes against which the specific issues surrounding retirement income streams are measured. AIST believes these objectives include:

- Support for the three pillars of retirement income saving.
- Support for community support, aged and health care.
- Broad and adequate retirement income system.
- Appropriately dealing with investment risks, longevity risk, and inflation.
- Equity between generations.
- Sustainability.
- Consumers adequately protected through disclosure, regulatory prescription, and that products are easy to understand.

#### **7.1.2.2 Principle 2**

The best interests of members must be taken into account when a fund determines its retirement income stream products and services. In this regard, AIST recommends the Government adopt the concept of trustees developing their own strategic framework for retirement income products and services – similar to the prudential requirements for MySuper insurance and investment policies. This approach would assist with ensuring that trustees provide products and services which meet the particular member demographics of that fund, rather than having prescription regarding which products and services are to be provided.

#### **7.1.2.3 Principle 3**

Members in their retirement phase should be provided with disclosure which ensures that all matters fundamental to their understanding of the product are disclosed. This is in line with *OECD Consumer Protection Principles*.

#### **7.1.2.4 Principle 4**

AIST notes the impact of increasing longevity on the Australian superannuation system. The Longevity Index released by the Government in 2009 assists with understanding the changing costs in retirement funding and, in particular, examines changing interest rates, inflation and longevity risks and assists with building markets to help manage longevity risks. AIST recommends that the Longevity Index be reviewed and promoted to assist members.

### 7.1.3 The need for a broader review of retirement incomes

AIST notes that the recommendation to pre-select a retirement income product is limited to a single strategy to form a default for adoption by all superannuation funds. We note that for disengaged members, any default provided to them by their trustee is an implicit recommendation. This could be perceived as such by members even if the opinions of the trustees were that there was a better approach to retirement incomes for the majority of their members.

A situation where trustees might be forced to recommend against their own default retirement income stream product would be regrettable, yet for funds containing members with shorter life expectancies or low account balances, this could be a reality.

We believe that this is short-sighted and strongly recommend that a broader review be undertaken. At an absolute minimum, this broader review must examine the following:

- The sustainability of taxation arrangements in retirement income streams and whether there is any real advantage of retirement income products over amounts invested in competing non-superannuation investments;
- The sustainability of superannuation restrictions and whether these form a barrier to retirement savings;
- The adequacy of social security arrangements, and what is accomplished by means testing parity between non-superannuation and superannuation products; and
- The issues associated with longevity risk as part of a larger basket of financial risks which include greater exploration of investment risks, as well as mortality risk.

At Appendix A, we have attached issues which AIST believes should form part of such a broader review. AIST also notes the forthcoming Taxation Review, and firmly believes that any review of retirement incomes legislation or policy consultation on the matters contained in the Treasury paper should be deferred.

### 7.1.4 Pre-selection of a comprehensive income product

#### 7.1.4.1 Requirement to mandate a single retirement product

AIST contends that there is no single answer to which type of income stream product would enable retirees to better manage risks in the retirement phase. AIST makes this comment based on its fundamental recommendation that funds should develop a strategic framework for retirement incomes that takes into account a fund's member demographics.

AIST proposed in our interim submission to the Financial System Inquiry<sup>46</sup> that trustees were the most appropriate entities to make decisions about what is in the best interests of their members:

*AIST recommends that superannuation funds be required to develop a strategic framework that examines how they address retirement incomes for their own members. Such a framework would consider:*

- *Rules, fund features, retirement income strategies, reversionary arrangements and tax;*
- *Whether a default transition from accumulation to drawdown phase is appropriate to members of a superannuation fund; and*
- *Trustees opting to provide alternative retirement income strategies (including additional investment options) upon request for members who do not prefer default arrangements.*

Although our recommendations for a retirement income strategic framework extend to superannuation trustees, we would welcome equivalent measures for life companies that offer retirement income streams to their customers. We believe that it is in the interests of both competition and consumers that the best possible retirement income policies are available for all, whether an investor is part of a superannuation fund membership, or a life company's customer base.

Whilst we understand the need for default actions to be taken on behalf of members who do not - or are unable - to make a decision, it should be up to trustees as to whether the provision of a default strategy is appropriate for their members at all. It should also be up to trustees as to what form their default strategy takes on, whether this is a longevity-based product, an account-based product, a hybrid or 100% member choice. Trustees may also prefer that their members are subject to different default strategies (or none at all) based on their account balances, or part thereof.

#### **7.1.4.2 Comprehensive Income Product for member's Retirement (CIPR)**

Comprehensive income product for members' retirement (CIPR) appears to match the 'group self annuity' (GSA) product that is referenced in the submission by the Australian Government Actuary (AGA) in their submission of March 2014<sup>47</sup>.

It should be noted that, although AIST has no specific position regarding the merits (or otherwise) of such a product, we believe that a significant amount of attention should be dedicated to various areas that are not covered at length in the AGA's submission.

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<sup>46</sup> AIST, (2014). *Response to Financial System Inquiry Interim Report*. [pdf] Melbourne: Australian Institute of Superannuation Trustees, pp.39-43. Available at: <http://tinyurl.com/n4ozc4> [Accessed 2 Sep. 2014].

<sup>47</sup> Australian Government Actuary, (2014). *Towards more efficient retirement income products*. [pdf] Canberra: Commonwealth of Australia. Available at: <http://tinyurl.com/ka9g98e> [Accessed 26 Feb. 2015].

#### **7.1.4.2.1 Higher and longer incomes come at cost of commutability**

The GSA contained in the AGA submission is built on the premise that on average, 31% of retirement income streams in account-based products are “wasted”. These amounts are put to work in a GSA to earn a larger amount of income in both the short term, and indefinitely. ‘Waste’ is implied by the notion of efficiency used within the AGA’s submission: Anything left over at death is not considered to be efficient. To counter this, 31% of the retirement balance is effectively put to work immediately in the short term, resulting in a retirement balance that is effectively funded by the retirement savings of the pool who pre-decease their life expectancy. This results in a higher, but non-commutable, income stream.

AIST supports an all-encompassing retirement policy (see principle 1 above) which has an approach to aged care and health care. Given the costs of these in retirement, the unavailability of funds due to non-commutability needs to be carefully considered.

#### **7.1.4.2.2 Mortality risk and the gender gap**

The AGA submission makes the distinction between systematic and idiosyncratic mortality risk, suggesting that the members of a pool bear members’ idiosyncratic mortality risk. This appears to be at odds with the commonly understood definition of mortality risk which can be best understood from the perspective of an investor: If a member of one of these products was to be killed a year after commencement (and well before life expectancy), it represents a demonstrable loss of value brought about by the early death of the annuitant. It is, thus the inverse of longevity risk.

AIST believes that the levels of mortality risk to investors associated with these products have not been disclosed sufficiently in review papers to date. In addition, in the case of couples, we note that males typically have much larger superannuation accounts than females. Due to their reduced life expectancy compared to females, this imposes a greater level of mortality risk on couples, with surviving females considerably disadvantaged.

#### **7.1.4.2.3 Selection risk**

The requirement to impose such a product on a fund with a reduced life expectancy amongst its members imposes selection risk upon the fund. That is, where a fund’s members have reduced life expectancies, this represents value to members with longer life expectancies, who might take advantage of the better priced income streams available. In other words, healthier Australians with longer life expectancies due to genes, lifestyle, previous occupations and other reasons could theoretically profit from members of a ‘blue collar’ fund, whose early deaths are able to fund more lucrative and longer pensions for the surviving members of the pool.

#### **7.1.4.2.4 Artificial commercial advantages**

Finally, it should be noted that the provision of pooled longevity products offers a clear commercial advantage to SMSFs which would be in a position to largely reduce the mortality risk to members, whilst offering very little in the way of longevity management. Further to this, it would appear to exacerbate the

ability of SMSFs to engage in inappropriate estate planning. We note that this was one of the reasons given for the prohibition of defined benefit pensions being offered by SMSFs in 2004.

## 7.2 Our recommendations

AIST recommends that a broader review of retirement incomes be set up to review the principles upon which these products are built. We have built a suggested scope for this review in Appendix A.

We also recommend that this broader review consider questions related to retirement incomes, including questions related to sustainability and adequacy of taxation and social security arrangements in addition to the larger basket of financial risks that are present in retirement income products.

Finally, we contend that there is no single retirement income product that is appropriate to members of all superannuation funds. To this end, AIST recommends that superannuation funds should develop a strategic framework for retirement incomes which takes into account a fund's member demographics.

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## 8 Innovation

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### 8.1 FSI Recommendation 14: Collaboration to enable innovation

***Establish a permanent public–private sector collaborative committee, the ‘Innovation Collaboration’, to facilitate financial system innovation and enable timely and coordinated policy and regulatory responses.***

#### 8.1.1 Our response

AIST supports the establishment of an Innovation Collaboration Committee. A single point of contact for innovators will aid efficiency and international competitiveness.

We believe the superannuation industry and its technological collaborators must be represented on the committee given super’s role within Australia’s financial services sector and the significance of the implementation of ecommerce through SuperStream and Single Touch Payroll.

As the ATO has facilitated the implementation of much technological change in superannuation, and is integrating this other technological solutions, such as Standard Business reporting, it should also be represented on the committee.

### 8.2 FSI Recommendation 15: Digital identity

***Develop a national strategy for a federated-style model of trusted digital identities.***

#### 8.2.1 Our response

AIST supports a centralised model for digital identities, rather than a federated model. A centralised model would be cheaper and more efficient. Individuals and business are able to have single sign-on access to public and private sector services under a centralised model. As the inquiry noted, some countries have centralised models with high-assurance, government-issued credentials incorporating biometrics designed to enable digital service delivery.

## 8.3 FSI Recommendation 19: Data access and use

***Review the costs and benefits of increasing access to and improving the use of data, taking into account community concerns about appropriate privacy protections.***

### 8.3.1 Our response

AIST supports a Productivity Commission inquiry into the costs and benefits of increasing access to and improving the use of data, subject to privacy considerations.

AIST notes that the March 2014 changes to the *Privacy Act* effectively prohibited credit reporting bodies from providing data matching services to superannuation funds. Prior to these changes, many superannuation funds used these services to locate lost members, advise them of their superannuation accounts and assist them to consolidate their super into their active account. This new prohibition is not in the best interests of superannuation fund members and the efficient operation of the superannuation system.

One credit reporting body, VEDA, has described the changes in the following way:

*Over the past decade, we've provided over 3.4 million updated member records to super funds. Over the past two years alone, by leveraging Veda data assets – including CRB data – funds were able to reunite more \$1.3 billion in superannuation with the rightful owners. This has been an important service to help proactively and regularly identify and address data issues at a whole-of-fund level. Under the amended Privacy Act, super funds no longer have access to a service that was proven to be hugely successful in connecting members with their superannuation accounts. The changes mean funds have very limited third party data sources to find and update member details<sup>48</sup>.*

Any Productivity Commission inquiry into data access and use should consider how better use of data may reduce unnecessarily duplicated accounts, facilitate account consolidation, and whether there are legislative impediments to this.

While AIST supports the current regulatory framework, we agree with the FSI report that regulators need to be better able to balance the benefits and risks of innovation and take a system-wide view.

While regulators are generally well-placed to recognise and respond to emerging risks, they need to have a corresponding requirement to assess the impacts of their policies on competition, innovation and efficiency.

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<sup>48</sup> Smith, C. (2014). Opinion: Push for Privacy Regulation changes to ease super load. *AB+F*. [online] Available at: <http://tinyurl.com/qev94v3> [Accessed 25 Mar. 2015].

AIST notes that in November 2010, APRA wrote to superannuation fund trustees about considerations when using cloud computing services<sup>49</sup>. While the letter set out reasonable requirements for the management of risk, it (and other APRA publications) did not include any corresponding encouragement for the use of innovative technology solutions. AIST notes that APRA has no statutory obligation to promote innovation and efficiency, but we recommend that it be given.

AIST nonetheless comments regarding the steps that have been taken by regulators to facilitate innovation. ASIC released CP 224 Facilitating electronic financial services disclosures in November 2014<sup>50</sup> seeking feedback from financial product and services providers and consumers on a new approach to the electronic delivery of financial services disclosures.

ASIC was seeking to facilitate default electronic delivery of financial services disclosures and to facilitate the use of more innovative Product Disclosure Statements. The consultations on these matters are continuing and AIST and the superannuation industry generally welcome these initiatives.

## 8.4 Our recommendations

AIST recommends: A permanent public–private sector collaborative committee on innovation should include representation from the superannuation industry.

AIST recommends: The Government should develop a centralised model, rather than a federated model, for digital identities.

AIST recommends: A Productivity Committee inquiry into the use of data should include measures to facilitate superannuation account consolidation and encourage member-focused innovation.

AIST also recommends that Superannuation regulators should be given an explicit requirement to encourage innovation by regulated entities in a way that also manages prudential risk (APRA) and provides consumer protection (ASIC).

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<sup>49</sup> Sim, P. (2010). *Outsourcing and offshoring: Specific considerations when using cloud computing services*. [letter]. Letter to all trustees on behalf of APRA dated 15 November 2010.

<sup>50</sup> ASIC, (2014). *Consultation Paper 224 Facilitating electronic financial services disclosures*. [pdf] Canberra: Australian Securities & Investments Commission. Available at: <http://tinyurl.com/nr486rn> [Accessed 25 Mar. 2015].

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## 9 Resilience

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### 9.1 FSI Recommendation 5: Crisis management toolkit

***Complete the existing processes for strengthening crisis management powers that have been on hold pending the outcome of the Inquiry.***

#### 9.1.1 Our position

AIST notes that the Final Report - in examining how to improve resilience in the Australian financial system – focuses primarily on the Australian banking system. While good governance and regulation of the Australian superannuation system is strong and well regarded, AIST as a leader in governance and regulatory issues, believes that the system could continue to improve further.

AIST strongly applauds the work APRA has done in both setting risk management standards, and in progressing the review of crisis management in the financial system.

Nonetheless, AIST believes that there are four key issues that need to be addressed:

- For the most part, individual entities are still being treated separately within the system.
- There is a high degree of interconnectedness of institutions within the superannuation system, including administrators, group life insurers, custodians and investment managers.
- APRA's framework should include defining 'systemic risk' within the Australian superannuation system.
- APRA's Probability and Impact Rating system should be reviewed to include, for example, the degree of interconnectedness of the superannuation system and its components.

In addition, AIST strongly supports the Final Report's recommendations that the existing processes for strengthening APRA's crisis management powers be completed and also that the general prohibition on direct borrowing by superannuation funds be restored.

AIST returns to the topic of systemic risk later in this document.

## 9.2 FSI Recommendation 8: Direct borrowing by superannuation funds

***Remove the exception to the general prohibition on direct borrowing for limited recourse borrowing arrangements by superannuation funds.***

### 9.2.1 Our response

AIST supports the removal of leverage in superannuation for a number of reasons.

Firstly, as outlined elsewhere in this submission, the key objective of superannuation is to provide income in retirement. We agree with Final Report's conclusion that the essence of a savings vehicle for retirement income, together with the "strengths and benefits the superannuation system has delivered to individuals, the financial system and the economy" could be lost if the original prohibition on borrowing is not restored<sup>51</sup>. The report further notes that this would limit the risks to taxpayers.

In recent times, a case has been made for direct, albeit limited, leverage in superannuation. This was cemented in 2007, when the SIS Act was amended to allow investment in instalment warrants, a derivative instrument that allows for piecemeal investment in assets. Previously, these were limited to shares, however, since these were allowed under the Act, a variety of funding solutions have been created, most notably over real property. Leverage itself was generally only allowed in situations where liquidity in the form of very short term cash flow was required to be addressed.

The Final Report also points to the fact that risk is magnified across the financial system by leverage. The submission of the Reserve Bank of Australia (RBA) drew special attention to this, singling the low level of leverage out as being a stabiliser on the Australian economy<sup>52</sup>. This was due to the fact that low leverage reduces the chance of defaults and subsequent "wealth shock[s]" to households.

However, the RBA also drew attention to the role of superannuation in national savings, noting that compulsory superannuation now forms 35% of gross national savings today. However, the submission noted elsewhere that savings are undermined by debt, noting that household savings in the decade following the Wallis Inquiry dropped nearly as low as 5% of GDP<sup>53</sup> due to household borrowing.

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<sup>51</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia The Treasury, p.88. Available at: <http://tinyurl.com/n7wi3lb> [Accessed 23 Feb. 2015].

<sup>52</sup> RBA, (2014). Submission to the Financial System Inquiry. [pdf] Sydney: Reserve Bank of Australia, p.184. Available at: <http://tinyurl.com/mhp599v> [Accessed 23 Feb. 2015].

<sup>53</sup> RBA, (2014). Submission to the Financial System Inquiry. [pdf] Sydney: Reserve Bank of Australia, p.114. Available at: <http://tinyurl.com/mhp599v> [Accessed 23 Feb. 2015].

Types of financial risk impacted by leverage include market risk, credit risk, manager risk, and liquidity risk and are increased at both an investor level, as well as a macroeconomic level. The interconnectedness of our financial system means that should failure in the form of defaults by borrowers become widespread, the spill-over effect may be unable to be contained by ordinary provisioning. This type of risk was noted in the Interim Report, and – we argue - falls within the definition of systemic risk.

We point to the fact that the size of the superannuation industry – currently \$1.93 trillion in assets under management, with only \$6.2 billion in borrowings in 2012 – is now so large that exogenous shocks, such as the global financial crisis, or shocks created within Australia, may be cushioned to a large extent by the passive investment in unleveraged assets. This stabilising influence is reduced as leverage increases.

Superannuation’s unleveraged nature meant that the GFC was not as pronounced in superannuation. This, in turn, acted as a stabilising influence on Australia’s financial system and the effect of interconnectedness was not magnified.

We contend that an unleveraged superannuation sector assists management of systemic risk. AIST supports a return of a prohibition on leverage in superannuation.

AIST returns to the topic of systemic risk later in this document.

### 9.3 Our recommendations

AIST supports the completion of the process to strengthen crisis management powers.

AIST supports the FSI recommendation to remove the exception to the general prohibition on direct borrowing for limited recourse borrowing arrangements by superannuation funds.

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## 10 Regulatory system

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### 10.1 FSI Recommendation 27: Regulator accountability

***Create a new Financial Regulator Assessment Board to advise Government annually on how financial regulators have implemented their mandates.***

***Provide clearer guidance to regulators in Statements of Expectation and increase the use of performance indicators for regulator performance.***

#### 10.1.1 Our response

AIST strongly supports the OECD's Best Practice Principles for Regulatory Policy<sup>54</sup>, which includes regulatory role clarity, preventing undue influence, accountability and transparency, engagement, funding, and performance evaluation.

AIST agrees with the observations in the FSI Final Report that regulators should continue to increase their use of outcomes-focused performance indicators. Such indicators should be developed with stakeholder input, in line with the Productivity Commission's Framework<sup>55</sup>.

AIST strongly endorses the work already done to date by APRA and ASIC in developing overarching indicators, as well as program indicators. Further work could be undertaken – for example, assessment of the quality of regulator administrative practices as well as identifying costs imposed on regulated entities. Such further improvements would be in line with OECD recommendations<sup>56</sup> that regulators should develop meaningful indicators including metrics as to the impact and costs imposed.

In particular, AIST believes that greater transparency should be delivered regarding the impost of financial supervisory levies. While a new Cost Recovery Impact Statement (CRIS) has been prepared, and new Government Cost Recovery Guidelines have been issued, there is still a lack of transparency regarding levy raising methodologies. AIST has provided more detail in its 2015-2016 Pre-Budget Submission<sup>57</sup>.

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<sup>54</sup> OECD (2014), *OECD Framework for Regulatory Policy Evaluation*, June. Available at: <http://www.oecd.org/regreform/framework-for-regulatory-policy-evaluation.htm>; OECD (2014), *OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators*, July. Available at: [http://www.oecd-ilibrary.org/governance/the-governance-of-regulators\\_9789264209015-en](http://www.oecd-ilibrary.org/governance/the-governance-of-regulators_9789264209015-en)

<sup>55</sup> Australian Government, Productivity Commission, (2014). *Regulator Audit Framework, Productivity Commission March 2014*. [online] Australian Government. Available at: <http://tinyurl.com/obssvtv> [Accessed 26 Mar. 2015].

<sup>56</sup> OECD, (2014), *OECD Best Practice Principles for Regulatory Policy: The Governance of Regulators*, July 2014. Available at: <http://tinyurl.com/pf7v3gl>

<sup>57</sup> AIST, (2015). *2015-16 Pre-Budget Submission 6 February 2015*. [online] AIST, pp.13-19. Available at: <http://tinyurl.com/oe2g6ny> [Accessed 26 Mar. 2015].

Also in line with the OECD recommendations is the development and ongoing review of ministerial statement of expectations to regulators. While this process is already in place in Australia, AIST agrees with the FSI Final Report that clearer guidance is needed in areas such as government tolerance for risk, or how to balance the regulator's various objectives.

As to how the overall performance of regulators should be evaluated, AIST queries the FSI Final Report's recommendations that a new Financial Regulator Assessment Board be created. At this point in time, there are a number of new initiatives focussing on both Regulator oversight and performance management within government which need bedding down. Within such a context, AIST believes it is inappropriate to create a new Board which may – or may not – fit within the implementation of very recent guidelines and legislation.

## 10.2 FSI Recommendation 28: Execution of mandate

***Provide regulators with more stable funding by adopting a three-year funding model based on periodic funding reviews, increase their capacity to pay competitive remuneration, boost flexibility in respect of staffing and funding, and require them to undertake periodic capability reviews.***

### 10.2.1 Our response

AIST has recommended in previous submissions (and in other areas within this submission) that the regulators should be better resourced to do their jobs, and offer qualified support for this recommendation. We support this for the regulators as entities themselves, as well as the staff who work for them and the environment in which they work.

However, AIST has concerns regarding the methodology for resourcing the regulators, which we have outlined below.

### 10.2.2 Funding principles

The Final Paper contains the following principles for funding of the regulators<sup>58</sup>, drawn from the Financial System Inquiry Interim Report:

*The Interim Report set out the following principles for funding the regulators:*

- *Funding should have a high degree of stability and certainty.*
- *Total funding should be proportionate to the task.*

<sup>58</sup> Murray, D., Davis, K., Dunn, C., Hewson, C. and McNamee, B. (2014). Financial System Inquiry Final Report. [pdf] Canberra: Commonwealth of Australia The Treasury, p.247. Available at: <http://tinyurl.com/n7wl3lb> [Accessed 23 Feb. 2015].

- *Regulatory costs should be borne by those contributing to the need for regulation.*
- *Funding should promote the independence and accountability of the regulators.*

We welcome these principles. However we note the absence of discussion that draws the link between consumer behaviour and increased transparency. The OECD made this point in their *High-level Principles on Financial Consumer Protection*, where they wrote that:

*The principle of responsible business conduct is important in order to ensure that financial services providers and authorised agents act fairly, honestly, professionally and with due skill, care and diligence when dealing with consumers. Duty of care is necessary in addition to improved transparency because consumers have bounded rationality and therefore cannot be expected to always make decisions that are in their own best interest<sup>59</sup>.*

Transparency was one of the principles that was promoted by the Government during their election campaign in 2013. The then Opposition noted that:

*Under Labor's own rules, government departments and agencies are required to prepare Regulation Impact Statements for regulatory proposals that are "likely to have a regulatory impact on business or the not-for-profit sector, unless that impact is of a minor or machinery nature and does not substantially alter existing arrangements.*

AIST welcomes these funding principles. However, we have also noted in our submissions to date on the financial supervisory levies that transparency regarding this has been hard to come by. Indeed, for several years running, we noted the lack of updated Cost Recovery Guidelines (CRGs) as well as a new Cost Recovery Impact Statement (CRIS). In our Pre-Budget submission of this year<sup>60</sup>, we welcomed publications of new CRGs as well as a new CRIS.

### **10.2.3 Lack of transparency and accountability**

Since our submission on financial levies was lodged in June 2014, we note that a new CRIS has been issued<sup>61</sup>. Additionally, we note that the Department of Finance has issued new CRGs<sup>62</sup>.

We note that the new CRGs state categorically, at paragraph 15, that:

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<sup>59</sup> Chapman, M. (2013). *The G20/OECD High-Level Principles on Financial Consumer Protection*. [presentation] Geneva: Organisation for Economic Co-operation and Development.

<sup>60</sup> AIST, (2015), *2015-16 Pre-Budget Submission*, [pdf] Melbourne: Australian Institute of Superannuation Trustees. Available at <http://tinyurl.com/oc98bbb> [Accessed 27 March 2015].

<sup>61</sup> APRA, (2014). *Cost Recover Implementation Statement - Financial Institutions Supervision*. [pdf] Canberra: Australian Prudential Regulation Authority. Available at: <http://tinyurl.com/p2ot29b> [Accessed 22 Jan. 2015].

<sup>62</sup> Department of Finance, (2015). *Cost recovery*. [online] Available at: <http://tinyurl.com/pjfv69t> [Accessed 22 Jan. 2015].

*Government entities should aim to minimise cost recovery charges through the efficient implementation of cost recovered activities, in the context of the specific policy outcomes and legislation. The cost recovery framework is underpinned by three principles that must be applied across all stages of the cost recovery process:*

- *efficiency and effectiveness*
- *transparency and accountability*
- *stakeholder engagement.*

AIST believes that the standard of transparency and accountability has demonstratively not been met by the new CRIS and recommended in our pre-budget submission of February this year that the new CRIS be reviewed.

We stand by the conclusions that we arrived at in our submission: That conclusions regarding any changes in methodology around levies collected need to have a case made that is based on a costing model which is well-documented and transparent, with better alignment of expenses and levy revenue.

### **10.3 FSI Recommendation 29: Strengthening Australian Securities and Investments Commission's funding and powers**

***Introduce an industry funding model for Australian Securities and Investments Commission (ASIC) and provide ASIC with stronger regulatory tools.***

#### **10.3.1 Our response**

##### **10.3.1.1 ASIC resourcing and funding model**

Given the widespread nature of recent financial planning scandals and the impact on consumers' retirement savings, AIST notes with concern recent ASIC comments that 'we remain concerned about the culture of financial services business, and the incentive structures they use ...' 'The welfare of their customers should be at the heart of their business<sup>63</sup>.'

AIST believes that in part ASIC's slowness to act has been caused by a lack of resources. AIST is therefore extremely concerned that the Federal Government is cutting funding to ASIC - \$120 million over the next five years. The Federal Government has signalled that it wishes to reduce the regulation of the financial services sector (including superannuation). AIST emphasizes its earlier points that given the risks placed on consumers and the inherent structural conflict of interest in the non-separation of banks and wealth

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<sup>63</sup> AAP, (2014). ASIC to monitor financial advice industry, concerned at culture. The Australian. [online] Available at: <http://tinyurl.com/mbluf2y> [Accessed 5 Dec. 2014].

management, prescriptive legislation and a well-resourced regulator is essential to having a strong, sound, and well-functioning financial sector.

AIST therefore believes that ASIC needs to be better resourced, and therefore better funded. However, AIST strongly agrees with the OECD<sup>64</sup> that ‘clarity about regulators’ sources and levels of funding is necessary to protect their independence and objectivity. Transparency about the basis of funding can also enhance confidence that the regulator is efficient, as well as effective.’

The OECD has noted funding sources may include consolidated revenue, cost recovery fees from regulated entities, monies from penalties, and interest earned on investments – and further that the mix should be appropriate to the particular circumstances of the regulator. To promote efficiency and equity, the IMF 1999 (as quoted by the OECD) states that the regulator should disclose why each funding source is paid in the way that it is.

While AIST agrees that ASIC does need to be better resourced, further debate around the method of funding is needed. Because of the lack of evidence so far, AIST does not at this point either agree or disagree with a user-pays funding model for ASIC.

Additionally, AIST highlights these issues, which also underpin the need for a greater debate regarding the ASIC funding model:

- The Cost Recovery Impact Statement<sup>65</sup> (CRIS) does not provide sufficient information to determine, for example, whether levies are being applied to what appears to be insufficient resources for, eg. ASIC, to properly carry out investigations and enforcement activities.
- Comparing the CRIS with the government’s Cost Recovery Guidelines identifies a number of gaps, which are outlined in AIST’s Pre-Budget Submission<sup>66</sup>.
- As stated on page 2 of the government’s Cost Recovery Guidelines, “A cost recovery levy ... differs from general taxation as it is ‘earmarked’ to fund activities provided to the group that pays the levy.” AIST notes that the imposition of such a levy therefore requires documentation of clear levy calculation methodologies. AIST therefore questions how a user-pays model impacts on the division between taxation and levies.
- AIST has commented earlier in this submission that it would welcome further development of regulator performance indicators. AIST believes that this work would also assist a greater

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<sup>64</sup> OECD (2014), “Funding”, in *The Governance of Regulators*, OECD. [online] Available at: <http://dx.doi.org/10.1787/9789264209015-11-en> [Accessed 26 March 2015].

<sup>65</sup> APRA, (2014). Cost Recover Implementation Statement - Financial Institutions Supervision. [pdf] Canberra: Australian Prudential Regulation Authority. Available at: <http://tinyurl.com/p2ot29b> [Accessed 25 March. 2015].

<sup>66</sup> AIST, (2015). *2015-16 Pre-Budget Submission 6 February 2015*. [online] AIST, pp.13-19. Available at: <http://tinyurl.com/oe2g6ny> [Accessed 26 Mar. 2015].

understanding of funding requirements – an increased outcomes focus helping to better gauge funding requirements.

- Coverage of a user-pays model also needs debate. We are unaware, for example, what contribution SMSFs are making towards ASIC funding (while, presumably, SMSFs do use licensed advisors).

#### **10.3.1.1.1 Does ASIC need stronger regulatory powers?**

AIST supports ASIC having stronger regulatory powers, but believes that the setting of clearer objectives, identifying the resources needed and a review of a funding model is needed first.

### **10.4 FSI Recommendation 30: Strengthening the focus on competition in the financial system**

***Review the state of competition in the sector every three years, improve reporting of how regulators balance competition against their core objectives, identify barriers to cross-border provision of financial services and include consideration of competition in the Australian Securities and Investments Commission's mandate.***

#### **10.4.1 Our response**

AIST agrees with the FSI Final Report that competition is a useful tool for assisting efficiency and innovation. By itself, AIST believes that competition is not the only way to assess whether good benefits are being delivered to stakeholders. In the case of the Australian superannuation system, members need to know that they are receiving transparent information, good net returns, advice which is not compromised through structural conflicts, and that their best interests are being met. Members also need to know that their superannuation money will be there, when they need it.

Any review of the financial sector needs to take into account not only issues of whether the system is competitive, but whether it is delivering beneficial outcomes to Australians. These issues should be taken into account in any review conducted by ASIC.

From a barriers-to-entry viewpoint, AIST believes that the ACCC has the most experience to review this issue periodically and therefore should form part of the Council of Financial Regulators.

### **10.5 FSI Recommendation 31: Compliance costs and policy processes**

***Increase the time available for industry to implement complex regulatory change.***

***Conduct post-implementation reviews of major regulatory changes more frequently.***

### 10.5.1 Our response

AIST notes its appreciation for the level of consultation which is undertaken by the regulators throughout any regulatory change program.

Elsewhere in this submission, AIST has mentioned the Australian Government *Regulator Performance Framework 2014*, the Productivity Commission *Regulator Audit Framework 2014*, and the OECD 2014 *Framework for Regulatory Policy Evaluation*. Information on the implementation of regulatory policy as a precondition to assess impacts on outcomes underlies these respective guides. The transparent process of defining clear strategic outcomes for regulatory process at the beginning and evaluating whether these have been delivered is key.

In either developing both the strategic outcomes and conducting an evaluation of whether these outcomes have been delivered, AIST believes that a number of impacts should be assessed, including administrative and compliance costs, impact on member engagement, timeliness of being able to implement, and economic benefits.

### 10.6 Our recommendations

AIST's recommendations on the regulatory system are as follows:

1. AIST does not believe that a new Financial Regulator Assessment Board should be created. Instead, an evaluation of the recent processes required from the following should be conducted as part of the government's ongoing review of regulator oversight and performance management systems, which includes the:
  - Australian Government Regulator Performance Framework 2014<sup>67</sup>. This Framework already includes a process of both internal and external reviews.
  - Productivity Commission Regulator Audit Framework 2014, which will require an audit plan with reporting against high level principles for good performance.
  - Australian National Audit Office *Better Practice Guide: Administering Regulation 2014*. This Guide includes guidance on managing regulatory performance.
  - Australian National Audit Office's pilot project *The Australian Government Performance Measurement and Reporting Framework*.
  - Implementation of the *Public Governance, Performance and Accountability Act 2013*, which will introduce new reporting requirements for regulators and departments.

These processes need time to be implemented and evaluated, rather than creating a new Board.

2. AIST would be pleased to be part of stakeholder consultations regarding the development of any new indicators.

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<sup>67</sup> Australian Government, (2014). *Regulator Performance Framework*. [online] Australian Government. Available at: <http://tinyurl.com/nudhs8v> [Accessed 26 Mar. 2015].

3. Any development of new indicators should gather feedback from stakeholders regarding how superannuation funds may need to report any data which may be required for reporting indicator outcomes.
4. That regulator key performance indicators include the development of Cost Recovery Impact Statements regarding the imposition of financial supervisory levies which are in line with the government's Cost Recovery Guidelines<sup>68</sup>.
5. Whilst AIST supports well-resourced and well remunerated regulators, flaws in the funding and levy model need to be addressed prior to the implementation of new methodologies.
6. While AIST agrees that ASIC requires further resourcing and therefore funding, AIST believes that further debate regarding an ASIC funding model is needed. In particular, the following issues need to be addressed:
  - a. What mix of sources of funding best meet OECD regulator funding objectives.
  - b. The production of a Cost Recovery Impact Statement needs to be undertaken which clearly identifies how levies are currently being applied.
  - c. How the government's Cost Recovery Guidelines impact on possible funding models, including with regulator activities may be considered to be 'taxes'.
7. AIST supports ASIC having stronger regulatory powers, but believes that the setting of clearer objectives, identifying the resources needed and a review of a funding model is needed first to better understand the relationship between resourcing and enforcement.
8. The ACCC periodically review the existence of barriers to entry into the Australian superannuation sector.
9. The ACCC be part of the Council of Financial Regulators.
10. AIST supports ASIC having 'competition issues' in its mandate, provided that this specifically includes whether the entities are competing in the best interests of members.
11. AIST agrees that further time to implement complex regulatory change would be beneficial.

AIST agrees that an evaluation of regulatory changes should be conducted, but that this should take into account not only timeliness and cost, but also broader impacts such as impact on member engagement and general benefits to the economy.

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<sup>68</sup> Department of Finance, (2015). Cost recovery. [online] Available at: <http://tinyurl.com/pjfv69t> [Accessed 26 March. 2015].

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## 11 Systemic risk: The missing chapter

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### 11.1 The problem

While at page xiii of the Final Report, the Inquiry includes ‘Strengthening the economy by making the financial system more resilient’ as one of five major themes, the chapter on Resilience refers to superannuation only in terms of improving resilience as follows:

*Recommendation 5: Complete the existing process for strengthening crisis management powers that have been on hold pending the outcome of this Inquiry.*

*Recommendation 8: Remove the exemption to the general prohibition on the direct borrowing for limited recourse borrowing arrangements by superannuation funds.*

Superannuation represents over 105% of Australia’s GDP and there is a high degree of interconnectedness of institutions within the Australian superannuation system.

Accordingly, AIST recommends that while Australia receives high international recognition for good governance and regulation<sup>69</sup>, there is room for further improvement. One such improvement would be a greater focus on the monitoring and management of systemic risk within the Australian superannuation system.

#### 11.1.1 Introduction to this section

AIST’s vision is to advocate for a better retirement future for all Australians. A core element of a better retirement future is to examine the stability and safety of Australia’s superannuation system. Superannuation holds 21% of the assets of Australia’s financial institutions<sup>70</sup>. While Australia’s superannuation system is very well regarded, AIST believes that further improvements could be made in terms of system resilience, so as to better protect the retirement savings of Australians.

#### 11.1.2 Systemic risk needs monitoring given its contribution to the economy

As noted in the Final Report, the Financial Stability Board defines a systemic event as once which has the potential to have serious negative consequences for the real economy and which is a disruption to the flow of financial services. In this respect, AIST notes:

- Australia’s superannuation system represents over 105% of Australia’s GDP.

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<sup>69</sup> Australia received the 2<sup>nd</sup> highest score for Integrity (regulation, governance, consumer protection and costs) in the Mercer and Australian Centre for Financial Studies, (2014). *Melbourne Mercer Global Pension Index*. [online] Mercer and ACFS. Available at: <http://tinyurl.com/omuvjxo> [Accessed 24 Mar. 2015].

<sup>70</sup> RBA (2012), *B1 Assets of Financial Institutions, October 2012*. Sydney: Reserve Bank of Australia (data at 30 June 2012).

- The Australian superannuation system primarily exists to provide retirement incomes to Australians. In Australia, those over the age of 50 represent nearly 32% of our population<sup>71</sup>, which indicates the level of a more immediate impact to the economy if a systemic failure occurs.

### **11.1.3 Australia has a predominately defined contribution system, where the risk is on the consumer**

As at June 2012, defined benefit balances in Australia stood at only 21% of accumulation scheme balances<sup>72</sup>. AIST submits that Australia's focus on defined contribution schemes (where members bear the investment and operational risks) prioritises the focal point to managing 'systemic risk' from the macro level (top down, looking at sectors or market themes). For example, concentrations of interconnectedness within the Australian superannuation system should be one of the key potential focal points.

### **11.1.4 At the macro level, the interconnectedness of the Australian superannuation system should be included in APRA's risk management framework**

While seemingly there is diversity in Australia's superannuation system there are many links within Australia's superannuation system which create an underpinning structure with less diversification. Donald et al<sup>73</sup> demonstrate this through linkages to service providers such as custodians, investment managers, group life insurers and administrators.

### **11.1.5 What outcomes does our superannuation system want?**

Ultimately, Australia wants the superannuation system to provide an adequate level of retirement income, relieve pressure on the Age Pension, and increase national savings. At the individual level and in very basic terms, Australians want their super to be there for them when they need it.

APRA's mission statement includes that it is to establish and enforce prudential standards to ensure that financial promises made by institutions are met within a stable, efficient and competitive financial system and that they play a role in preserving the integrity of Australia's retirement income policy. The ratings of Australia's superannuation system as highlighted above – coupled with Australia comparatively faring well during the GFC – all point to a well-regulated system.

However, as Australia's superannuation system continues to evolve – and as the demands of an ageing population impact the system even more – AIST certainly believes that the management of systemic risks within an increasingly complex environment should be examined.

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<sup>71</sup> ABS, (2014). *3105.0.65.001 - Australian Historical Population Statistics, 2014*. [online] Australian Bureau of Statistics. Available at: <http://tinyurl.com/ojvyyaw> [Accessed 25 Mar. 2015].

<sup>72</sup> Bateman, H. and Kingston, G. (2013.). Restoring a Level Playing Field for Defined Benefits Superannuation. *SSRN Journal*. [online] Available at: <http://tinyurl.com/pj5qzur> [accessed 25 March 2015].

<sup>73</sup> Donald, M. (2010). *What contribution does trust law make to the regulatory scheme shaping superannuation in Australia?* [online] APRA. Available at: <http://tinyurl.com/nlsczks> [Accessed 25 Mar. 2015].

## 11.2 Our recommendations

AIST presents the following recommendations to assist the management of systemic risks:

1. AIST recommends that APRA's charter include:
  - a. APRA developing a framework for identifying systemic risks within the superannuation system.
  - b. A definition of systemic risk.
2. AIST recommends that the Probability and Impact Rating System be reviewed to include, for example, the degree of interconnectedness of the superannuation system and its components.
3. AIST recommends that the data collected by APRA be used by APRA to help identify the degree of interconnectedness of the superannuation system.
4. AIST recommends that APRA's jurisdiction include examining all areas of superannuation systemic risk, including SMSFs and any major, systemic themes which could give rise to market failure.
5. AIST agrees with the Final Report's recommendation 5 that the existing processes for strengthening crisis management powers be completed, and recommends that:
  - a. A timetable for consultation processes be issued.
  - b. The consultation scope be extended to include how systemic risk within the Australian superannuation system be defined, monitored and managed.
6. AIST agrees with the Final Report's recommendation 8 that the general prohibition on direct borrowing by superannuation powers be restored.

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## 12 Appendix A: Recommended scope of retirement income review

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As part of our recommendations regarding retirement incomes, AIST recommended that a broader review of retirement incomes must be undertaken.

At an absolute minimum, a broader review of retirement incomes must examine the following:

### Part A - structural

- The objectives for the retirement incomes policy.
- How current policies are delivering the retirement incomes policy objectives – now and into the future.
- A review on the developments and trends in retirement incomes both within Australia and internationally.
- The interaction between the three pillars of retirement savings, including the respective roles that each play in Australia’s retirement incomes policy.
- The focus of the Intergenerational Reports to determine, for example, whether any additions are needed to better understand retirement incomes adequacy, longevity and sustainability issues.
- The sustainability of taxation arrangements in retirement income streams.
- An examination of taxation of superannuation and non-superannuation retirement investments.
- The interaction between retirement incomes policy and encouraging people to stay at work.

### Part B – specific issues – making retirement incomes work better

- An examination of how the legislation governing various retirement incomes policies address adequacy, sustainability and longevity.
- The sustainability of superannuation restrictions and whether these form a barrier to retirement savings.
- The adequacy of social security arrangements, and what is accomplished by means testing parity between non-superannuation and superannuation products.
- An examination of retirement product options compared with spending patterns in retirement.