



COMMONWEALTH OF AUSTRALIA

# Official Committee Hansard

## SENATE

SELECT COMMITTEE ON SUPERANNUATION AND  
FINANCIAL SERVICES

**Reference: Prudential supervision, global financial services and superannuation  
guarantee charge**

FRIDAY, 1 SEPTEMBER 2000

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**SENATE**  
**SELECT COMMITTEE ON SUPERANNUATION AND FINANCIAL SERVICES**

**Friday, 1 September 2000**

**Members:** Senator Watson (*Chair*), Senator Sherry (*Deputy Chair*), Senators Allison, Chapman, Conroy, Hogg and Lightfoot

**Senators in attendance:** Senators Allison, Conroy, Hogg, Sherry and Watson

**Terms of reference for the inquiry:**

For inquiry into and report on:

- (a) prudential supervision and consumer protection for superannuation, banking and financial services;
- (b) the opportunities and constraints for Australia to become a centre for the provision of global financial services; and
- (c) enforcement of the Superannuation Guarantee Charge.

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**Committee met at 9.46 a.m.****GRIMMOND, Mr Norman John, Senior Auditor, Performance Audit Services Group, Australian National Audit Office****WHITE, Mr Peter Frank, Executive Director, Revenue Branch, Performance Audit Services, Australian National Audit Office**

**CHAIR**—I declare open this public hearing. This is the seventh public hearing of the committee's main terms of reference. The aim of today's hearing is to take further evidence on two of the committee's terms of reference—namely, the prudential supervision and consumer protection of superannuation, banking and financial services, and the enforcement of the superannuation guarantee charge.

All of the witnesses who appear before the committee today are protected by parliamentary privilege with respect to the evidence given before the committee. This means that they are given broad protection from action arising from what is said and that the Senate has the power to protect them from any action which disadvantages them on account of the evidence given before the committee. The committee prefers to conduct its evidence and hearings in public. However, if there are any matters which you wish to discuss with the committee in private, the committee will consider your request. Welcome. I invite you to make an opening statement.

**Mr White**—Thank you for the opportunity to appear at this public hearing of the committee. If you agree, Mr Chairman, in the interests of brevity, we would be happy to have our opening statement incorporated into *Hansard* and to make only some brief introductory comments now.

**CHAIR**—Is it the wish of the committee that the document be incorporated in the transcript of evidence? There being no objection, it is so ordered.

*The document read as follows—*

**Mr White**—We conducted a performance audit into the administration of the superannuation guarantee by the Australian Taxation Office, tabling our report on 15 November 1999. We appear today in connection with paragraph (c) of the committee's inquiry terms of reference—namely, the enforcement of the superannuation guarantee charge. That said, our audit focused on superannuation guarantee and not specifically on the superannuation guarantee charge. The objective of the audit was to review the ATO's administration of the superannuation guarantee and to identify appropriate opportunities for improvement. We found that the ATO's administration of the superannuation guarantee is sound. Our audit noted that superannuation guarantee contributions by employers totalled approximately \$15 billion in the 1997-98 financial year.

Generally, the ATO had effective risk assessment, risk planning, risk treatment and performance monitoring strategies in place for superannuation guarantee. However, we identified a number of areas where improvements are possible and made eight recommendations to improve the ATO's administration of superannuation guarantee. The ATO considered that our recommendations had merit and were consistent with the ATO's general direction in relation to the superannuation guarantee administration. The ATO agreed to our recommendations, with qualification on one matter regarding options to reduce manual processing of superannuation guarantee forms. While we have not undertaken a follow-up audit of the ATO's implementation of our recommendations, we are aware from contacts since the audit that the ATO is making progress against each recommendation.

In particular, we note that the ATO has now developed a prosecution strategy for superannuation guarantee avoidance in accordance with the ATO's compliance model. Action has been taken, and is ongoing, to match existing superannuation accounts and unredeemed vouchers. Appropriate coordination between the ATO's Small Business Line and Superannuation Business Line, which have many employers in common, has been strengthened and performance indicators in relation to the levels of superannuation guarantee compliance are being refined.

As noted in our audit report, employers that do not make superannuation guarantee contributions at the required minimum level are subject to the superannuation guarantee charge. The superannuation guarantee charge comprises the amount of shortfall in contributions by employers plus nominal interest and administration components. With regard to the superannuation guarantee charge, our audit report noted that the ATO had collected some \$64.5 million in superannuation guarantee charge payments during 1998-99. The ATO had improved its superannuation guarantee debt collection performance between 1997-98 and 1998-99, and the ATO was considering possible legislative options to present to government concerning flexibility in the application of a superannuation guarantee charge. Those are the only comments that we wish to make. Thank you. Norm and I would be happy to answer any questions the committee has, or to clarify any points, relating to our audit.

**CHAIR**—At the bottom of page 3 of your opening statement it says:

... research ... has established that less than one per cent of employers are fully non-compliant with SG legislation ...

Can you confirm that, or is there a typo there?

**Mr White**—Sorry, I did not—

**CHAIR**—That is a fairly low level. We seem to get quite a few complaints when firms run into trouble, because there is up to a 13-month period when employers can make their contribution and people get left off. There seems to be a very slow follow-up by the tax office in that area. What work did you do there when firms run into difficulties?

**Mr Grimmond**—If we are talking about page 3 where we are talking about fully non-compliant employers, that figure comes from a survey that the Superannuation Business Line carries out in order to determine how their overall levels of superannuation guarantee payments are going.

In terms of the 13-month period that you mentioned, that is set under legislation where superannuation guarantee is not payable until 28 July of the year after payments are effectively due. In terms of the follow-up that the Superannuation Business Line conducts when they are following up complaints, we did a report on this at some length within our report. At the time, the Superannuation Business Line was moving toward more of a risk-treatment proposal in ways of dealing with those complaints. They were about to not follow up each individual complaint as it occurred, but to amalgamate complaints and other information that would become available through the superannuation guarantee surveys to identify particular industries, particular locations or particular employers that were not fully complying with the superannuation guarantee legislation. They would then conduct audits on those particular employers once they had been identified.

However, we understand that since the conduct of our audit, each complaint—called an employee notification—is now at least followed up with a telephone call to the employer saying, ‘We have received this complaint. What is the story?’ At the same time, there are still compliance activities going on at the employer level, where employers are identified through other means as well.

**CHAIR**—Doesn’t that seem a little bit unusual? I acknowledge the change in process, and you say you are doing a risk assessment. But in an area of very high risk, you are virtually only doing samples or collections of some. I would have thought almost 100 per cent would be appropriate in terms of cases where people are definitely not being paid their superannuation entitlement. I can understand that sort of approach being taken across the spectrum, but, in a high risk area such as I am referring to, I am disappointed that more detailed, individual work is not being done.

**Mr White**—Just to clarify: this is the follow-up of the ENs that are coming in. From memory, of the ones that the ATO was following up, over 50 per cent proved invalid, in that the contributions were being made. In terms of your saying that they represent a high risk, I think that, of the ones that were being followed up, around 50 per cent turned out not to be valid. In other words, the payments were being made by employers.

**CHAIR**—In full? Often in those cases they pay part of the superannuation guarantee, we have been told, but not the full amount and therefore it skews the result. While some money is coming in, a full entitlement is not coming in. Do you strike many of those cases? We find that particularly in the shearing industry, where they pay for some sheds and not for others.

**Mr Grimmond**—During the audit we did try and identify the extent to which there was partial payment, or partial compliance, if you like. Once again, the figures that became available to us came from the superannuation surveys that had been conducted within the Superannuation Business Line. They found a figure for partial compliance which was, from memory at the time, around 17 per cent overall. Once that partial compliance has been identified, then employers that had been identified by name would then be followed up by the Superannuation Business Line, through the issuing of what is called a superannuation statement. That results in a debt under the superannuation guarantee charge.

We understood that there were about 9,000 superannuation guarantee statements that were issued in the particular year that we were looking at. They would cover a range of employers that were either fully non-compliant or partially compliant. But, obviously, partial compliance means that perhaps they were paying five per cent of employees' wages into superannuation guarantee instead of seven per cent, as I think it was at the time of the audit. Then they would be subject to the extra two per cent.

**Mr White**—The information we have relates to the survey that was done in 1998. I am aware that Tax has undertaken surveys in 1999 and is probably undertaking a survey now in 2000. It might be that the Australian Taxation Office would be able to provide up-to-date figures on the level of full compliance and partial compliance, based on those surveys.

**CHAIR**—If the tax office has collected \$65 million, when what they collect is usually late moneys, that is a very high figure, isn't it? It must ring some alarm bells that it is probably not working as well as it should be.

**Mr Grimmond**—That \$65 million relates to a particular financial year when the Superannuation Business Line had issued around 8,000 to 9,000 superannuation statements, so you divide that \$65 million by about 9,000—I am not too sure what that figure comes out to be. There are quite a few people that are involved in that \$65 million.

**CHAIR**—That in itself would indicate that the ordinary process needs improvement, wouldn't it? To me, it would.

**Mr White**—There is always some scope for improvement in the processes.

**CHAIR**—None of your recommendations really got to the nub of it, as I see it, in terms of the long period in which superannuation is allowed to be collected. This committee has been very strong on the fact that we believe we should move to at least a quarterly collection period. What do you think that would do to the \$65 million figure?

**Mr White**—We did not comment on the terms of the frequency and the timing of payments—whether they be quarterly or not. We really considered that as more of a policy matter.

**CHAIR**—What measures do you think would be essential to get the \$65 million down to a more acceptable level?

**Mr Grimmond**—Moving to an earlier payment of the superannuation guarantee, you would think, would be quite feasible as a way of reducing that figure. Having said that, if you look at the overall figure for the superannuation guarantee payments already made that basically do not involve the tax office, you are talking about billions coming in every year. Sixty-five million dollars is a significant figure in its own right, but when you are talking about billions already flowing in it is a relatively small amount in terms of the money flow that is already taking place. Having said that, there was some comment at the time we were conducting the audit about whether quarterly payments would identify defaulting employers much more quickly and therefore enable the tax office to take action more quickly and more effectively. But that was not resolved at the time we were looking at the figures.

**CHAIR**—Do any other issues come to mind that you could identify in terms of reducing that \$65 million?

**Mr Grimmond**—I do not know whether I am touching on a policy matter, but one of the problems we identified, perhaps at officer level as opposed to a senior executive level, within the superannuation administration was the absence of returns, as it were, from employers saying, ‘This is the amount of superannuation guarantee payment we have made.’ They are required to put in, of course, income tax returns which provide the tax office with particular information about what is going on. Perhaps something along those lines is being considered in a policy area within the tax office or within government, but at the time we did not particularly comment on it in the audit report.

**CHAIR**—On the lodgment of your return to the tax office, in relation to what is eligible wages plus—

**Mr Grimmond**—I do not know whether it had been developed—certainly that sort of thinking had not been developed at the time we conducted the audit. I think even the press in recent times have talked about whether it could be included in this business activity statement that is required under the new tax system.

**CHAIR**—This is called a performance audit. The processes involved in the collection and payment are fairly cumbersome. If a person’s employer is late they must pay it to the tax office rather than the superannuation company. That process does seem very cumbersome. In terms of performance, couldn’t that procedure be streamlined somewhat?

**Mr Grimmond**—Certainly, yes. As we understand through some contact we have had with the tax office since the conduct of this audit, they have taken steps to truncate the issuing of superannuation vouchers, which was seen as part of the problem. The use of other data matching systems or resources that the tax office already has enables—to a certain extent—the tax office, when the superannuation guarantee charge payment is made, to determine on the basis of an individual where superannuation payments are already being made or where they are already being held and advise the person that the payment is going to be made directly to the fund as opposed to doing it through a voucher system. That has resulted in some efficiencies with the flow of money.

**CHAIR**—Do you detect a problem with the tax office insisting that, even when they are late and have paid to the company, they also make this identical charge to the tax office? There were complaints in that area.

**Mr Grimmond**—Yes, this is the double payment arrangement; that if an employer makes the SG payment after 28 July, they are still subject to the superannuation guarantee charge, which includes that late payment. At the time of the audit, we mentioned that there were some moves for the superannuation business line to discuss some legislative options with the government about that particular inconsistency, if you like. We merely noted that it existed and that perhaps some action would be taken legislatively after the conduct of the audit.

**Mr White**—We just note that that problem can perhaps be addressed with a legislative change.

**Mr Grimmond**—One of the options was that the Commissioner of Taxation should be provided with some flexibility in the application of the superannuation guarantee charge in those circumstances.

**Senator SHERRY**—I come back to a couple of points the chair raised. In talking about partial compliance, that can mean anything from an employer paying one per cent to 99.9 per cent of the legal requirement. I could not find in your report the number of employees and the outstanding periods for which moneys are owed. A partial compliance of 17 per cent could mean hundreds of thousands of individuals who are owed money for their retirement. Do you agree with that?

**Mr Grimmond**—I do. We thought there were some things missing, if you like, from performance information that the superannuation business line produced, and that was in fact one area where we considered there should be some different reporting, if you like, on the levels of performance and compliance, in general, with SG. We understand there has been some action along those lines since the conduct of our report but, because we have not done a follow-up study in any formal way, I must say that we are not aware of what the outcome of that particular recommendation was.

**Senator SHERRY**—So you were not able to identify X number of employees and the possible amounts that are owed for employees?

**Mr Grimmond**—That was one possible outcome from the superannuation guarantee surveys that were being conducted, that there would be a figure available that would produce that. We were saying at the time of the audit that some particular compliance figures were being pulled out of those surveys and reported. I understand there are some moves along those lines to change some of those performance reporting aspects.

**Senator SHERRY**—We can pursue that with the tax office.

**Mr White**—That is our recommendation No. 3 that we are talking about.

**Senator SHERRY**—Yes.

**Mr Grimmond**—There have been some moves that we are aware of, but it would probably be better to perhaps get the ATO to report on it.

**Senator SHERRY**—Yes. My concern is that, whatever the figure and whatever the number of employees—whether it is tens of thousands or hundreds of thousands—it is important to them, as individuals, if one or two years of outstanding payments are owed to them. It might not be a big amount of money in the overall scheme of total moneys collected, but it is very important to them, as individuals. I was pleased that, in your report and your statement today, you say:

The Superannuation Guarantee (SG), which came into effect on 1 July 1992, was introduced to reduce reliance on the age pension as a means of funding retirement for individuals.

For individuals this is very important. Do you have any comment to make on that general issue of reducing reliance on the age pension as a means of funding retirement?

**Mr White**—No. In that statement there, we are recognising that this is an important pillar of the government's superannuation policy. We are not necessarily commenting on the policy. We are just stating a fact that it has now become an important part of it.

**Senator SHERRY**—But you are recognising the overall principle that, with an ageing population and with people living longer, the difficulties of funding a basic pension system without superannuation for an individual puts an individual who is not receiving superannuation guarantee in a difficult circumstance.

**Mr White**—Yes. There is one other thing. I have just flicked over the report—and I do not know whether this will help your earlier question. On page 70 of the report, we talk about some of the results coming out of the superannuation guarantee 1998 survey in terms of the number of employers that are fully compliant and the numbers that are partially compliant. We have some figures in the report and, as I suggested to the chair earlier, it may be opportune to ask the ATO, when they appear before you, to give you an update on that.

**Senator SHERRY**—Yes, I pursued this issue briefly at estimates, and I certainly intend to do that with the ATO again. Going back to that previous answer where you agreed with my comments about the level of superannuation guarantee, effectively if an individual does not receive their contributions, or only receives part of their contributions, they are left in a position where their retirement income is effectively reduced. That is the difficulty those individuals face, isn't it?

**Mr White**—Yes.

**Senator SHERRY**—The level of collection, or the level of superannuation guarantee, can be quite critical for individuals for their retirement.

**Mr White**—Yes, we would agree with that. At the same time, and looking at the whole broad operation of a superannuation guarantee, what we are trying to recognise in our report too, in terms of what the ATO was trying to do, was that heavy emphasis on the education of

employees and employers. We have commented on that in terms of making them very aware of what employers' responsibilities are and what employee's responsibilities are.

**Senator SHERRY**—Senator Watson asked about this. You correctly identified 13 months—even if a person is paid after 13 months, or at the end of 13 months, they are missing out on interest. Interest on interest can be substantial over a period of time. You would agree with that particular issue?

**Mr Grimmond**—That is certainly true. The legislation was obviously set up in a particular way that perhaps had some business relationship, or something like that, I would guess. That is certainly quite true. On the other hand, as we were informed during the conduct of the audit, many employers already pay quarterly, fortnightly, monthly or weekly.

**Senator SHERRY**—I was just going to get to the point actually. I do not know whether or not you are aware, but most award provisions have a requirement for monthly or quarterly payment of superannuation guarantee. Are you aware of that?

**Mr Grimmond**—Yes.

**Senator SHERRY**—That is, effectively, why the vast majority of employers pay the money. There is a legal requirement for them to do that—

**Mr Grimmond**—That is right.

**Senator SHERRY**—which is superior to the act. My understanding is that, if the award provisions were removed and they did not exist, an employer could—some do at the moment, whether it is in breach or whether there is no award provision—pay yearly. Do you agree with that?

**Mr Grimmond**—Yes.

**Senator SHERRY**—If those provisions that tie an employer to paying monthly or quarterly were removed, it would be logical to expect to see an increase in employers paying yearly, wouldn't it?

**Mr Grimmond**—Speaking statistically, I would say, yes, that is correct.

**Senator CONROY**—That would affect their final benefits.

**Mr Grimmond**—No, it is not a matter that the ANAO examined at the time.

**Senator SHERRY**—No, I understand that.

**Senator CONROY**—That would reflect on their final end benefit though, wouldn't it?

**Mr Grimmond**—That is right.

**Senator CONROY**—Compounding interest works on each bit at a time by building. If they are only going for lesser time frames or greater time frames and lumping, then that compounding interest benefit, which is critical to the whole notion, is going to mean a lower overall outcome.

**Mr Grimmond**—That is true. I should say that the superannuation guarantee charge, as it is applied, does include a nominal interest component that is an attempt to address that problem.

**Senator SHERRY**—It is currently less than the average returns that I have seen being paid by superannuation funds over the last three or four years.

**Mr Grimmond**—That is right. I believe that at the time of the audit it was 10 per cent nominal interest. That could be quite true, depending on the performance of individual funds.

**Senator SHERRY**—I note that in your report you identify areas for improvement—this is probably the greatest concern I have; it is a very important issue—one of them being ‘developing an effective prosecution strategy for SG avoidance’. The implication is that there is not an effective prosecution strategy at the present time. What problems did you identify?

**Mr White**—There was not a prosecution strategy. We recommended that they have one, recognising that one would not go out and necessarily prosecute people for small amounts of money. In accordance with the ATO’s compliance model—I touched on the education part earlier—a key element of the compliance model is your enforcement strategies, including prosecution. We did not see a prosecution strategy in place. We are now aware from discussions with the tax office that they have developed a prosecution strategy. We will be incorporating that into some of their training programs and educating their staff on how to effectively use it. You would have to check with Tax as to where they are at with it.

**Senator SHERRY**—The absence of that is a pretty critical problem, isn’t it?

**Mr White**—Yes, it is a key enforcement tool and it is in the ATO’s compliance model.

**Senator SHERRY**—Let me give you an example. I know the chair—there may be others of us—has had complaints about nonpayment from individuals who have gone to the tax office. I know of two examples in my home state: a rubber plastics company that owes money going back five years and a shearing company in a similar situation with nonpayments of four or five years, and there has been a simple refusal by the employer to pay the money. In the case of those individuals who have complained to me and the tax office, four or five years is a long time for nonpayment of SG. You would agree with that?

**Mr White**—Yes.

**Mr Grimmond**—I certainly would.

**Senator SHERRY**—There should be effective prosecution in those sorts of circumstances.

**Mr White**—In the administration of the program whether you prosecute someone would become a high risk factor. Obviously, you just would not go out if there was a particular individual, but if there was a group of individuals involved and Tax had tried various other measures—education and talking to the employer—then prosecution might be an option.

**Senator SHERRY**—Certainly in the case of someone where the money is just not paid for a period of four or five years, it seems that it is more than enough time to be tolerant and reasonable and try to educate the employer.

**Mr Grimmond**—We would have to say that, at the end of a period such as that, we have exhausted the following up of administrative penalties, such as the superannuation guarantee charge, and it certainly would have to be considered.

**Senator SHERRY**—As an auditor, I hope you use a bit tougher language than ‘have to be considered.’

**Mr Grimmond**—We are the audit office.

**Mr White**—It is not our position to tell the ATO what to do in terms of that. Certainly, I would be thinking about prosecution.

**Senator SHERRY**—Surely the danger is that, if an employer is not paying amounts of money for that period of time—and say the business ceased to exist for whatever reason—and there are substantial amounts of superannuation outstanding, as I understand it, that is not provided for in any compensatory mechanism in terms of loss of entitlements. That is the problem, isn’t it?

**Mr Grimmond**—I do not believe that we actually examined that issue within the conduct of this audit. I have in mind that superannuation guarantee debts were somewhat down the line of what could be gained from the winding up of a business or when a business had gone defunct. Other than that, I did not really follow up on that.

**Senator ALLISON**—Could I pursue that point of prosecution strategy? If there wasn’t a strategy, what was the practice?

**Mr Grimmond**—At the time of the audit there had been no prosecutions conducted. I believe that we reported that in our report.

**Senator ALLISON**—What information did you gather about the experience of the complainants by the time they got to the ATO? Had they been through a number of processes? What happens when they ring the ATO? Do they get a recorded message and only sometimes they are responded to? Did you get a feel for what the consumers find in the approach?

**Mr Grimmond**—At the time of the audit callers were directed through the equivalent of a 1800 number—I think it was a 1300 number at the time. They were individually answered while the complaint was actually recorded.

**Senator ALLISON**—They record the complaint on some sort of answering machine—

**Mr Grimmond**—No, while there was an ATO officer on the end of the line effectively recording the details on a check list or whatever—

**Senator ALLISON**—You do not mean recording as in tape recording, but notes are taken?

**Mr Grimmond**—No, although there was provision to do that. I believe we sat in with a couple of people that were actually answering those calls and they could be recorded particularly for training and quality assurance processes.

**Senator ALLISON**—The callers knew that they were being recorded?

**Mr Grimmond**—I believe there was a check list of advice provided by the answerer, as it were, to the callers when they called in to say they could be recorded. That is pretty common practice nowadays with call centres. After the call had been made the details of that particular complainant would be entered into a database that was just being formed at the time when we were doing the audit—no doubt it has been extended since then—to record the details of things like employer name and details of what the complainant believed to be the case. From that database, plus some other information within the ATO, it would then be decided whether the particular employer would be followed up. We understand now that there is a slightly different process in that each complainant that comes to the notice of the ATO is actually followed up, at least with a phone call to the employer, to find out what the situation is. But that was not the case at the time of the audit.

**Senator ALLISON**—Can we just take two steps back? Did you get an understanding of where that complainant had been prior to getting to the ATO? What do you think people understand in terms of their rights to get follow up and have their payment made? Have they already rung the consumer centre, the Ombudsman or the Superannuation Complaints Tribunal? How do they get to the ATO?

**Mr Grimmond**—I must say that I cannot recall that we did follow up those sorts of issues. I would expect that in at least most of the cases the employee would have discussed the matter with the employer, or you would believe that they might have done that. I could not say that we actually identified percentages or areas that had been investigated prior to that. Having said that—

**Senator ALLISON**—And there is no record made in the process, then or now, about what else the complainant has tried?

**Mr Grimmond**—I just cannot recall the details of what was recorded by those people who were answering the calls at the time. It might be something that you wish to take up with the ATO representatives when they appear later.

**Senator ALLISON**—You make no recommendations about whether there should be a central service or whether there should be a consumer advice centre, for instance, that might be the first point of call for such people?

**Mr Grimmond**—No, we did not make a recommendation along those lines.

**Mr White**—I agree with Norm. If it were me, the first person I would approach would be my employer, and probably the next step would be to ring the tax office. From our audit point of view, that is where we picked it up—looking at the complaints coming into the tax office.

**Senator ALLISON**—I note that you support the so-called risk based approach—and there is a list of the characteristics that might be possible indicators of compliance risk. Having looked at the figures of complaints and non-compliance, does that suggest that the vast majority of those complaints come from those areas where there is high risk and, if so, what is the data? Are we talking about 50 per cent, 60 per cent or 80 per cent of non-compliance that can be identified in that way? Could you give the committee some sort of scale of the problem outside that group?

**Mr Grimmond**—I am not too sure that we can answer that in any detail. The audit was conducted, as we said before, at a time when they were changing from a purely complaints based approach, if you like, to this risk based management approach. Things have moved on since then and that area probably would be more able to supply that information that you are asking.

**Mr White**—If you have various complaints coming in, they would be fed into the compliance model, the risk model. You would be looking for whether or not you are getting complaints about the same employer and the like. From that, you would then determine your follow-up strategy.

**Senator ALLISON**—Isn't that a problem, though, for someone with a serious complaint against an employer who does not fit into the risk strategy? What happens to that?

**Mr White**—Inside the tax office there are three levels of complaint mechanisms that people can go through: level 1, level 2 and level 3. Level 1 is where you just talk to the staff member involved—this is on page 59 of our report—level 2 is where the supervisor handles the complaint and level 3 is the problem resolution service; the ATO has to handle the complaint. You can elevate your complaint up into the various hierarchy of complaints in the tax office.

**Senator ALLISON**—Does that assume that someone who goes in at level 1 has their problem dealt with, or they are sent to level 2? Is that how it works? Can we assume that anyone who does not go through to level 3 has had the complaint solved and payment has been made?

**Mr White**—One would hope so—if the person making the complaint is aware of the various complaint mechanisms that the tax office has. I have seen them discussed in various brochures and pamphlets that the tax office has put out. We assume that people might be aware.

**Senator ALLISON**—The committee has had correspondence and people appear before it saying that they ring the tax office and they are told that it is too small a problem for them, that the tax office does only systemic problems and they basically go away. You did not discover that kind of—

**Mr White**—Not so much that they go away. What we found was that definitely the most common subject of complaints coming in was a lack of communication from the tax office regarding progress on their ENs.

**Senator ALLISON**—So somebody makes a complaint and the tax office might solve the problem but it does not get back to the employee to tell them what it has done. Is that the issue?

**Mr Grimmond**—At the time of the audit I think an issue was raised about the secrecy provisions that applied.

**Mr White**—The privacy provisions.

**Mr Grimmond**—I am sorry, the privacy provisions. The tax office cannot tell a complainant anything about the progress of their complaint once it has been raised with the employer; they have to wait until the end of the process. For example, if an employer is found to be defaulting on payments or not making the right payments he is issued with a superannuation guarantee statement. He pays the superannuation guarantee charge and, at the time of the audit, the tax office prepares a superannuation voucher. It will come back to the complainant at that stage but that process might take quite a while to complete. In the meantime, the complainant is not able to be informed about the progress of the complaint.

**Senator ALLISON**—Did you have any recommendations about that process?

**Mr White**—Not in terms of the privacy provisions because that might have wider implications for the overall operation of the tax office.

**Mr Grimmond**—That is right.

**Senator ALLISON**—Could you make some suggestions about how we can overcome that problem?

**Mr Grimmond**—I do not know whether we want to make a recommendation along those lines.

**Senator SHERRY**—We are talking about a person making a complaint about moneys that they are to receive for their retirement; it is their money and it is not being paid by an employer. Complainants who have spoken to me about this issue are frustrated that they cannot get any information about what has happened to their complaint. They might wait one or two years and then a voucher appears in the mail. They might have rung the tax office and said, ‘What is happening? Can you give me some idea?’, but the tax office could not tell them anything.

**Mr Grimmond**—That is right.

**Senator SHERRY**—Surely that is a fairly absurd position in those circumstances.

**Mr Grimmond**—The position arises from the privacy requirements.

**Senator SHERRY**—Yes, I understand why it arises. In those sorts of circumstances, it is surely an absurd or unhelpful situation.

**Mr White**—I agree that it is not particularly helpful, and I can certainly understand the frustration of not knowing. It is a matter of sitting down and looking at whether you want legislative change in terms of the privacy provisions in the tax act. I hear what you are saying about the superannuation scheme, but I wonder whether that has wider implications for the overall operation of the tax office.

**Senator SHERRY**—It does not have to. I note you say in your report that the tax office is putting together some recommendations for legislative change.

**Mr White**—Yes.

**Senator SHERRY**—Given the concerns you have identified in your report and the discussion we have had this morning, I would have thought these sorts of legislative changes were important and should see the light of day.

**Mr Grimmond**—When you talk to the tax office representatives, I hope they will be able to provide you with an update on the sorts of provisions that are under way.

**Mr White**—Yes. To answer your question: in terms of the legislative issues that we discussed, we did not discuss the privacy provision probably because we thought that was a pretty significant policy issue.

**Senator ALLISON**—I want to ask you about the 50 per cent of complainants who get it wrong. Did you form any views about why this was the case? Why are they so ill informed?

**Mr Grimmond**—In the majority of cases that fall into this category, employees were not aware of where their payments were going. The employer has a duty of care to make sure that that does not happen. Employees should know where their money is going, and of course that would result in fewer complaints.

While we did not identify any particular percentage, I believe there were also vexatious or frivolous complaints made against employers by employees who had left under acrimonious circumstances, or whatever. They would be complaining about a particular employer. Around 50 per cent of complaints were not sustainable. Advice then would go back to the employees who did have payments made on their behalf to find out where their payments were being made. The tax office cannot actually inform them along those lines, it can just say that they were being made.

**Senator ALLISON**—I imagine it is in the tax office's interest to halve the number of complaints coming into the office. What did you find in terms of their processes or recommendations that would reduce that number of unwarranted complaints?

**Mr Grimmond**—There is always going to be an irreducible minimum of complaints along those lines, that people will just not make themselves aware, or there is a problem with the employer, no matter what the tax office does about it. We had a look at the education

information activities that were conducted within the superannuation business line for both employees and employers, and they are quite comprehensive. There is any amount of information that is available and, in fact, had been disseminated to employers in particular, but also to employees who had contacted the tax office. It is probably a fact that it will never be eliminated, for various reasons.

**Senator ALLISON**—I am sorry to pursue this point but 50 per cent seems to me to be extraordinarily high and a waste of the ATO's time and energy and a problem in terms of people's understanding. I think it would be useful if we could come up with some suggestion that would help alleviate it.

**Mr Grimmond**—On the part of the audit team that looked at this whole matter, we were not able to formulate any particular view on ways that the tax office should go that would eliminate or downgrade this problem. Having said that, there has been quite a bit of effort, one way or another, that had gone into education information flow from the tax office about superannuation guarantee requirements on the part of employers, and advice to employees. We understand that those sorts of efforts are continuing. I do not have a particular way of eliminating those particular problems.

**Mr White**—We did not make a specific recommendation on that and the only thing I can think of is the tax office's education strategy. They are educating employers and employees in terms of their responsibilities and their rights. The only recommendation we have made in terms of complaints is recommendation 4 where we recommend:

that SPR record and report regularly to the ATO Commissioners its performance against the ATO's commitment (as set out in the Taxpayers' Charter) to respond to clients within seven days of receiving a complaint.

By reporting complaints at that senior level in the tax office means that at least senior management can be aware of them in making strategic decisions on how best to address complaints coming in.

**Senator HOGG**—I have a couple of quick questions on the prosecution strategy and the practice. You found that there were no prosecutions, I understand?

**Mr White**—Yes.

**Senator HOGG**—Were you able to find out why there were no prosecutions? Was it simply that the cost to pursue would have far outweighed the amount recovered?

**Mr White**—In general, we put it down to two things. One was the heavy emphasis on the education strategy—educating—and the other was probably the amount of money involved, whether there were small amounts of money involved. I do not think we look at it in great detail.

**Senator HOGG**—You did not go into great detail?

**Mr White**—No, we did not.

**CHAIR**—Just to sum up: now that the Auditor-General is an officer of the parliament, reporting on improvements is an issue which really does not seem to be focused high on the audit agenda. We call this a performance audit, and when we look on page 28, at your audit priorities and your focus, we find it says to ‘identify appropriate opportunities for improvement’. The impression is given of a performance type audit, reporting on efficiencies, et cetera, where clearly they are administrative, although there are legislative provisions that make some aspects of this superannuation guarantee something of an ass. There are problems between the 65s and 70s aspects of the collection, the voucher system, et cetera. Yet the parliament is denied the opportunity because you say, ‘This is a policy issue.’ I would have thought a policy issue where you should stay away would be one like whether the charge should be nine per cent or 15 per cent. But the problems that arise and the administrative complexities involved in the 65 to 70, and the reporting processes, are not even touched on in this report. I just think the whole thing gives the parliament a misleading position. This is something that the Auditor-General might have to have a look at in terms of his responsibilities to the parliament.

**Mr White**—In terms of the focus of the audit, what we looked at was the ATO’s administration. We did not look at the policy issues. I agree, at times there is a fine line between—

**CHAIR**—Their administration is made much difficult by the cumbersome processes that are in place and have to be followed. I would have thought that would be something that had to be looked at.

**Mr White**—We have not commented on that overall policy environment. There are some suggestions in there in terms of legislative change that may help, but the main focus of the audit was on the administration. We came in there and we wanted to take a macro-snapshot of how the super guarantee was operating. The best way we thought of to look at that was to apply a risk management model, going through that to see whether or not there was a sound foundation there.

**CHAIR**—What I am saying is this: if, to get from A to B, the processes involve walking 100 kilometres, and we can identify a process where it is only half a kilometre, shouldn’t that be reported on? That is the issue I am raising. This is an issue that we might well have to look at. Thank you very much, anyway.

**Senator ALLISON**—I would like to ask a question we did not touch on. You do not make any recommendations about whether the ATO is adequately resourced in terms of compliance with SG. Did you form a view on that?

**Mr White**—No, we did not make a comment. We leave it up to the tax commissioner, in terms of how he allocates the resources. I come back to it in terms of what we are trying to do with the risk based approach. I am sure every area in the Public Service— or even in the private sector—might like some more resources to do things, but we looked at it from the risk management point of view that it is up to the tax commissioner, in terms of his management of the overall tax office, to allocate the resources as he sees fit. So we did not comment on whether or not they had sufficient resources.

**CHAIR**—Thank you very much.

**Proceedings suspended from 10.44 a.m. to 10.58 a.m.**

**HRISTODOULIDIS, Mr Con, Senior Manager, Public Policy, Financial Planning Association of Australia Ltd**

**PINTO, Mr Maurice, Chairperson, Superannuation and Retirement Incomes Committee, Financial Planning Association of Australia Ltd**

**CHAIR**—I welcome the representatives from the Financial Planning Association of Australia Ltd. Do you wish to make an opening statement?

**Mr Hristodoulidis**—Yes, Mr Chairman. I would like to give a quick, brief overview of the association and then hand over to Maurice to give you an overview of our submission and talk through the issues. We are here today to speak on two aspects of the terms of reference. The first is prudential supervision and consumer protection for superannuation. The second is the enforcement of the superannuation guarantee charge.

The Financial Planning Association is the peak professional organisation for the financial planning industry in Australia. We have over 12,000 members through a network of 31 chapters across Australia, and a state office in each capital city. The FPA is the only organisation that fully represents qualified financial planners and the principal financial dealers. FPA members advise on and/or manage the financial affairs of approximately 4.9 million Australians, with an investment value of \$156 billion.

At this stage, I would like to hand over to Maurice, who has been a member of the FPA superannuation policy committee and has recently been appointed as chairperson. He has been involved in the financial services industry for 10 years and six of those have been in superannuation, so he has a fair bit of experience with superannuation.

**Mr Pinto**—Our submission has focused on four key areas—namely, enforcement of the SGC, consumer protection, education and, finally, disclosure of commissions and bonuses. I will start by looking at enforcement of the super guarantee charge. In our submission we have sought to look at ways in which that charge would not need to be enforced by the tax office. Whilst we recognise that the super guarantee charge is payable by an employer to the ATO where that employer has failed to meet the minimum level of super support for its employees, we have considered ways in which the tax office, employers and their employees could all be assisted in meeting their minimum level of super support so that enforcement of the SGC would not be required or would be minimised.

What we are suggesting is that employers be required to meet their minimum level of super support on a more regular basis than simply once a year. This could be on a quarterly or a monthly basis. And it may well be in line with their group tax reporting obligations, so they could perhaps state, as part of those obligations, that they have met the minimum level of super support for that particular period. In this way, employers would be regularly reminded of their super obligations; employees' retirement benefits would join the retirement income pool earlier and, hopefully, there would be a larger nest egg at retirement; and the ATO's enforcement activity could potentially be reduced. We are mindful that we do not want to burden employers with onerous reporting requirements. But we are also mindful that members' super entitlements need to be protected, and of the stress to employees which arises through their employer not meeting the minimum level of super support, especially if that company becomes insolvent.

We also note that it was previously suggested that employees with incomes between \$450 and \$900 in any given month be given the opportunity to choose between receiving super contributions or receiving the equivalent in salary and wages. We believe that such employees should be given that choice of either providing for their retirement income or, alternatively, addressing any pressing needs to maintain their living standards.

Looking at consumer protection, we welcome the universal standards of conduct and uniform disclosure obligations for all financial service providers dealing with retail clients. But we believe that the current merely incidental advice provision in the Corporations Law and the proposed declared professional body exemption in the draft Financial Services Reform Bill would deliver a lower level of consumer protection in a super choice environment. A single licensing regime without any exemptions not only promotes competitive neutrality, but allows for clear operating standards and accountabilities for conduct, and consistent and comparable financial product information. We believe that this will, in turn, promote a high level of informed decision making by retail clients.

We are concerned that, by allowing various professional bodies with powers to licence financial service providers, this will only confuse consumers as to the appropriate channels to pursue for guidance, advice and redress. We suggest that it may also make it more difficult for government and the responsible regulator to monitor the practices of the professionals that are members of the exempt professional bodies.

Looking at education, we realise that there are many choices in the marketplace today surrounding super and that it is complex. Terms such as ‘reasonable benefit limit’, ‘eligible termination payment’ and ‘eligible service period’ are confusing to a number of fund members. In addition, the taxation laws surrounding superannuation do deter some consumers from making voluntary contributions. We believe the public education process should be twofold. Initially, we would recommend that the government, in conjunction with appropriate bodies, work towards introducing superannuation into the high school syllabus. At another level, we recommend that the government should fund a body, be it a new body or an existing body, to prepare as straightforward as possible material on superannuation which is readily available to the members. We also suggest that this body be equipped to research superannuation trends such as the number of consumers making voluntary contributions at any one time and the impact of the ageing population.

Finally, looking at disclosure of fees, commissions and bonuses, we recognise that, for consumers to make informed choices, they require, at a minimum, information on costs, fees and charges and the availability to them of a dispute mechanism process. We believe that critical to the effectiveness of disclosure and the ability of consumers to compare apples with apples between funds is the development of a standardised industry-wide disclosure regime that requires disclosure of all fees, commissions and bonuses. We do not support the proposition made by some in the industry and expressed in the Financial Services Reform Bill that, where the commission paid does not affect the return from a product, no disclosure is required. The existence of incentive payments payable for sales of risk protection insurance and other products may well be important information for a consumer to understand the motivations and behaviour of advisers promoting financial products in so-called non-advice situations.

What we are saying is that the likely impact of commissions on the return on a product is only one reason for disclosure in the product disclosure statement. Conflict of interest and potential bias are still important factors that should be made transparent. We support the disclosure in dollar amounts where practicable and, where this is not possible, in percentage amounts or in a written description of some form.

In conclusion, the FPA is committed to the universal disclosure of commissions and benefits for all financial products, including investments, life, super, risk, borrowings and real property. As an example, our practice guideline on disclosure of fees, commissions and benefits does not distinguish between different types of fees and benefits. Further to this, our code of ethics rule 106 does not differentiate or define commission into components. Therefore, it does not allow for sections of commissions to be excluded from being disclosed.

**CHAIR**—If there are no other comments, we will go to questions.

**Senator CONROY**—I will start with the section on consumer protection and your discussion about merely incidental advice. Can you expand on that? What are the problems with these sorts of exemptions?

**Mr Hristodoulidis**—If you had a single licensing regime, anybody who wanted to provide financial services advice would come under the same system. So if a consumer had a concern about advice, they would know where to go in terms of the complaints handling scheme: they would know who the industry regulator was. With the incidental advice, we are concerned—it is a particular concern in the superannuation choice environment—that a professional such as an accountant or a lawyer may, as part of tax advice or law advice, for example, say to a client, ‘Have you thought about maybe changing your superannuation fund from an industry-based fund to a private fund. If that comes under incidental advice and that advice is inappropriate to that consumer’s needs, given their lifestyle circumstances, it is very difficult for the consumer to seek redress. That is why we think provisions such as merely incidental advice should not exist in a superannuation choice environment.

**Senator CONROY**—Do you think there should be blanket abolition of incidental advice?

**Mr Hristodoulidis**—We think any business that provides that type of financial advice should seek a licence to do so.

**Senator CONROY**—How do you think that would work in practice? Would the lawyers and accountants that you were talking about take on the training that would hopefully come through under this regime or would they not be allowed to make comments like that?

**Mr Hristodoulidis**—There are two approaches. Under the current system, a lawyer or an accountant can seek to become a licensed dealer or a licensed investment adviser. Obviously, the hurdles are quite high in terms of trying to meet ASIC requirements. The alternative is that they can become a representative of a licensed dealer or a licensed investment adviser. The hurdles there are not as great. They are authorised to provide that advice as a representative of that licensed group and they fall within the net that currently exists for the single licensing regime. It is fairly simple for the consumer to follow the process.

**Senator CONROY**—An accountant would say that they know all an individual's circumstances because they are helping them do their tax. An accountant would argue that they are in a good position now: they have done their accountants' training and they know how to put numbers on different sides of ledgers.

**Mr Hristodoulidis**—No problems. Accountants have very good knowledge of the tax law and are very good at handling the tax affairs of their clients. However, the issue of providing financial advice is different because it is not just about tax: it impacts on a client's financial needs. They have to look at people's lifestyles, their family situations and their incomes. You have to look at their goals in terms of what they want to achieve in their savings horizon. All those issues need to be taken into account when you are offering financial advice and financial products.

**Senator CONROY**—So you can be an expert in tax law and be trained in tax law—as accountants presumably are—but not understand all of the products.

**Mr Hristodoulidis**—That is exactly right. We found through our education program—the Diploma of Financial Planning and the Certificate of Financial Planning—that a lot more accountants are now doing some sort of training and picking up the skills of a financial adviser or a financial planner because they recognise that as a separate skills set that they require when advising their clients. Both the CPAs and the institutes have also created their own pathways into financial planning. It is becoming a separate skills set.

**Senator CONROY**—Do you think that is a recognition by those bodies that, just because you are able to hang out the shingle that you are an accountant—whether it is a CPA or whatever—it does not automatically give you the knowledge to promote financial products?

**Mr Hristodoulidis**—I think so, yes. I think they have now realised that this is a specific professional service and that somebody who is an expert in law or accounting is not necessarily an expert in handling people's financial affairs. They have recognised that and they have created educational programs to accommodate their members' needs in terms of providing such advice.

**Senator CONROY**—Is that qualification comparable with what you provide? Is it identical? Are they just not prepared to accept it in an overt sense, but they have set up their own stream? How comparable are those two qualifications?

**Mr Hristodoulidis**—At the lower level of our diploma we have eight units. The programs offered by the accounting bodies would probably be aimed at the bottom two or three levels. It provides those professions with a basic knowledge of what they need to look at in terms of the financial affairs of the client. When you get into the more nitty gritty details and high wealth clients they probably need more training.

**Senator CONROY**—In terms of the government's original choice legislation where the employer would choose in a default circumstance which fund to recommend the members be in, would they, under your preferred model of FRSB, require training? If they are going to say, 'This is the super fund we think you should be in,' would they need training?

**Mr Hristodoulidis**—There is a role not only for employers to tell their employees what super funds they should go into in default, but also for associations like ourselves to work with employers to minimise their costs. Obviously, there is a significant cost to employers if they have an employment pool of, say, 50—like our organisation. You may have 40 different funds and it is quite difficult to administer those 40 funds and also have a default fund. There is a role for the association to work with employers to identify and minimise the costs in identifying the right default fund.

**Senator CONROY**—There has been a lot of concern. Even employers have argued that they did not really want to receive this power they were going to be given—being in charge of picking a default fund—because of potential liability down the track. Is that a fair concern?

**Mr Hristodoulidis**—Yes, and that is where there is a role for a financial planner or a financial planning association to work in conjunction with employers to try to overcome or redress some of those issues.

**Senator CONROY**—I always declare my interest—I used to be an employee of an industry fund. Do you think that someone promoting the one product, that is, the industry fund—even though many of them now have many other products—would need to be licensed? Would I, in my previous occupation, even though I was working for just the one fund and promoting and explaining the one fund and the benefits of the one fund, need to be licensed?

**Mr Hristodoulidis**—We have heard a lot about that. We have heard people say that employers would need to get a licence if they are promoting a fund. That is one of those issues that we as an association have not quite thought through. We can see the cost imposed on the employer of going through the licensing regime. There are also the cost imposts of even being an authorised representative. We are working through that at the moment to come up with an appropriate solution.

**Senator CONROY**—I used to, as you define it, provide retail financial product advice. I am interested in finding out whether advertising the fund that employed me would fall into the category of retail financial product advice. I am interested in your view.

**Mr Hristodoulidis**—I would have thought that the larger the employer, in terms of employees, the more they would be looking to outsource that service of identifying the appropriate super fund for their employees. When you get to smaller employers—ones with one to five or maybe one to 15 employees—there is a significant cost in trying to identify the right super fund, whether they do that themselves or even outsource it. They are the issues that we, as an association, the government and the industry we need to work through to make sure we get right so we do not overburden them with having to find the right super fund for their employees.

**Senator SHERRY**—You refer to minimising this cost. Why should there be a cost? What is the sense of changing a system to add to cost? There are extra obligations on employers to go around and annually look for a different fund, and the employees or employer can presumably change the fund if they want to. What is the sense in all that?

**Mr Hristodoulidis**—It gets back to the issue of empowering the consumer to have control of his or her own financial affairs. It gets back to the issue that Maurice touched on in terms of

education—to educate our people at a young age in the school system to have control of their financial affairs and to understand what they are doing with their money in terms of investment. It gets back to the issue of consumer sovereignty.

**Senator SHERRY**—Sure, but the nub of my question is that, whether consumers are informed or not, there is an additional cost. What is the sense of that?

**Mr Hristodoulidis**—Just to give you an example on the flip side of the current system: there are a number of examples that we have heard of through our planners, that their clients maybe started off in the workplace in the Public Service—at the federal or at the state level—and have now moved into the private sector. They have had their money locked into these super funds and they have not been able to take that money across into a private fund as they moved across in employment. So you have got that cost now on the consumers, where they have got this money—which may be just small amounts of \$3,000, \$4,000, \$5,000, \$10,000—sitting there earning only the CPI.

**Senator SHERRY**—Yes, but they are usually defined benefit funds in the public sector. There is a good argument that they are considerably better off than, certainly, SG standard.

**Mr Hristodoulidis**—The way the legislation currently stands, the consumer does not have that decision, that choice, to make as to whether they are better off under the defined benefit or whether they are better off the accumulation fund.

**Senator SHERRY**—Are you aware of what happened in the UK? The theory was advanced and implemented that public servants should be better off by freeing it all up and being offered choice, but it turned out to be an absolute disaster that they are still sorting out.

**Mr Hristodoulidis**—We are aware of that and we think there are a couple of different issues with respect to that. One is that in the UK the defined benefit funds were a greater proportion of the total superannuation pool; in Australia that is not as large. Our estimates say it is only about 20 per cent.

**Senator SHERRY**—I am talking about public servants.

**Mr Hristodoulidis**—Yes. What we have been promoting in terms of a super choice regime as part of our ethics and professional standards is that there is a rule that a planner who recommends to a client to change their investment has to produce a net benefit. We would propose some sort of rule in the legislation that actually sets that benchmark. Rule 118 says:

A Member shall not move a client or cause a client to move from an investment to another investment without explaining to the client, in terms that the client is likely to understand, the reasons for the move. The Member must demonstrate that the move is appropriate for the client.

We would expect some sort of check or hurdle being set in the legislation that achieves that type of outcome.

**Senator SHERRY**—Let me put one other point to you. Where there are fees and charges and commissions payable to an individual or a firm of individuals for giving advice, how would you feel if the payment of the cost, whatever it may be, of that advice were prohibited from being

debited against the contributions? In other words, the cost of that advice has to be paid separately and cannot be paid from the superannuation contribution itself—a separate accounting process. How would you feel about that?

**Mr Hristodoulidis**—That is happening more and more in the industry now, in that the industry is moving to a fee for service and away from a commissions base. Even if there is a commission in terms of the investment placement, the plan actually rebates that back to the client and charges them up-front fees. So that would be what is happening currently in the marketplace.

**Senator SHERRY**—There are still a lot of commissions and fees that are charged, not as a separate account, but as a cost against the member's account as a deduction from the contribution. What I am saying is this: you would prohibit that from occurring. The full contribution has to go into the member's account and any cost of any advice has to be paid separately. Effectively, that is what would happen in all circumstances?

**Mr Hristodoulidis**—Yes, and for us it would be more transparent if that occurred.

**Senator SHERRY**—Exactly. That was the point I was going to make.

**Senator CONROY**—I congratulate you on those guidelines. They are very worthwhile guidelines and standards to set in your industry. You would be pleased to know that a member of yours took me up at a breakfast over the question of risk products and why they should possibly not have disclosure. He was quite passionate about it, so your members are out there lobbying away merrily. He indicated to me that you guys do have some risk product sales people in your association and you have a way of disclosing your risk product commissions at the moment. I was going to speak to you privately, but perhaps you would be able to take it this on notice. I would be very interested in how you actually deal with those risk product issues within your guidelines and within your association.

**Mr Hristodoulidis**—We have an officer who has been developing those guidelines and has worked through that process. I am happy to take that on notice.

**Senator ALLISON**—Could I ask that we might have available the document that you referred to a moment ago with 'ethics' on the front.

**Mr Hristodoulidis**—Do you want me to send a copy to each of the members of the committee?

**Senator ALLISON**—Perhaps through the committee rather than to each of us.

**Mr Hristodoulidis**—I am happy to table this one today and will send additional copies.

**Senator ALLISON**—I have a couple of things that I want to follow up with you. Under your education recommendations, you include a consumer advice centre. I invite you to expand a bit on what role you think that centre would have. You say that it would possibly produce material on superannuation and do research. Is that the extent of the role that you envisage?

**Mr Hristodoulidis**—It is a twofold body. One role is obviously to provide the consumer with basic information about super requirements in terms of what has been legislated and to put it in a simple format so that consumers can understand—something like a booklet, like that one on ethics which is quite easy to follow, or as a flyer for the consumer to understand what the requirements are from their behalf and what the requirements are from the employers' behalf and what the requirements are, maybe, from the regulator or any dispute resolution scheme. On the other hand, the second component of our recommendation is that you need some sort of research centre because, at the moment, it is very hard to actually pull out the research in terms of the level of national savings that is occurring in the economy, the level of voluntary savings that is occurring and the level of contributions coming through the superannuation guarantee charge. It is very hard to find that in one consolidated form and that is why we are recommending that this body should have a research arm to it. It makes it easier for policy makers to actually make policy once that information is centralised.

**Senator ALLISON**—Is there a role for such an organisation to be the first point of call for, say, complaints—people not knowing where to go to find out whether their employer has made contributions on their behalf? Do you see that as being part of it?

**Mr Hristodoulidis**—Absolutely. In terms of making super choice easy for consumers, they need to have a one-stop shop where, if they have a complaint—or even if they are looking to, say, find a super fund—this body can refer them to an association like ours, where we have a referral service, or to some other association that may have a referral service. It has that sort of educative role in teaching consumers the requirements—for them to go to this body and to shop in terms of finding the right products for themselves.

**Senator ALLISON**—For instance, having a grasp of the sort of choice regime that is being offered in an ad hoc way now—could that also be a useful task?

**Mr Hristodoulidis**—We understand that a lot of enterprise bargaining agreements now provide choice for those who are on those agreements. That is why we think that the introduction of choice across the board would be a fairer way to go and to actually centralise the whole issue of choice and bring the rules of choice all together under the one piece of legislation.

**Senator ALLISON**—But this consumer centre as well—I am interested in what sort of a role they might have.

**Mr Hristodoulidis**—The consumer centre would obviously have a role in educating the community.

**Senator ALLISON**—What sort of level of funding would you envisage would be necessary?

**Mr Hristodoulidis**—We have not sat down and done the numbers, so that is something we would need to take on notice.

**Senator ALLISON**—If you could think about that, that would be useful. I have a question, too, about whether you think this could be just a central body that largely communicates via the Internet and telephone or whether you think that might be necessary in each state.

**Mr Hristodoulidis**—I think an office in each state is a good idea, especially early on in its formative years with super choice. There would be a fair bit of confusion in the marketplace. Obviously, using any possible means of communication would be an advantage, especially electronic communication where, these days, you can get information out quite quickly and at fairly low cost. I think that is important as well. Any channel of communication that improves the flow of information should be used.

**Senator ALLISON**—You have suggested that the government fund this, but is there not an argument for industry to share some of the cost burden? There would be benefits, would there not?

**Mr Hristodoulidis**—I totally agree. I would have thought that, in the early stages of super choice, there is a role for such a body to work with industry associations to actually educate consumers and, even from our perspective, educate some of the planners about what choice means for them in terms of the advice that they give. There is a role to work together with associations.

**Senator ALLISON**—If there were to be a non-government contributory system, how would you see that working—with a levy? Which parts of the sector do you think ought to contribute to such a centre?

**Mr Hristodoulidis**—In terms of from the private sector?

**Senator ALLISON**—Yes.

**Mr Hristodoulidis**—I would have thought that anybody who has a stake in superannuation has a role to contribute to the education program.

**Senator ALLISON**—You suggest that there should be more frequent payments, and I think there is general agreement about that. But I am interested in your suggestion that the payments ought to be monthly for larger businesses and quarterly for smaller ones. Do you have a suggestion for a cut-off? Is it the number of employees or turnover?

**Mr Pinto**—It could be either the number of employees or turnover. I would suggest turnover of above or less than \$10 million per annum.

**Senator ALLISON**—Concerning the people that you provide services to, do you think they would support that idea as well? Is that a view just from your direct members or an attitude that might have wider support?

**Mr Hristodoulidis**—Yes. Obviously our members have contact with the consumers who are seeking financial advice. That is the feedback we are receiving from our members—in terms of knowing that the super has been paid and not having the headache of the company going insolvent and not having that money in there, or even having that money working for them earlier rather than later. Yes, that is a big issue for them.

**Senator ALLISON**—Can you make any comments about the current mechanisms that we have for detecting or preventing fraud? Do you have a view on that?

**Mr Hristodoulidis**—I can comment from our association's point of view, if you like. We have recently set up a complaints resolution scheme in-house which has two components. Firstly, there is an investigation officer who handles any complaints against any of our members and, secondly, there is a compliance officer. We are just about to release a compliance program where this officer will be doing ad hoc audits across all our principal members to ensure that they are complying with ASIC rules and regulations as well as the rules and regulations of the association. If an error is found, there are a whole set of steps put in place to rectify that. If an investigation has found that a member has been fraudulent in the advice or in the placement of the investment, the association has powers to actually impose penalties on that member. We also refer them through to the FIC scheme, which is a Financial Industry Complaints Service. All our members have to be members of that FIC scheme and pay a yearly contribution to that scheme. We also refer any fraudulence that we have found on behalf of members to ASIC to investigate, as well. So we have a fairly stringent compliance program in place.

**Senator ALLISON**—You may not have been here before the previous witnesses. The Audit Office found that the ATO had no strategy for prosecution for non-compliance. In your dealings do you have any feel for whether the situation has improved or can you just simply comment on the Audit Office findings?

**Mr Hristodoulidis**—Our dealings tend to be more with ASIC, the regulator, in terms of financial services and investment advice. We think that their processes in terms of identifying and remedying any fraudulent claims are quite good and quite strong.

**Senator ALLISON**—But SG compliance is not really a concern for you.

**Mr Hristodoulidis**—Yes, that is right. We have not really been involved in the ATO side of things so it is hard for us to comment on that.

**Senator SHERRY**—On the opting-out provision and timing, you have mentioned the \$450 to \$900 a month income. If you follow the logic of that, shouldn't a person who earns less than \$450 a month, where there is no super payable, receive whatever that sum of money is as income?

**Mr Hristodoulidis**—But where they are not paying any super contribution?

**Senator SHERRY**—That is right.

**Mr Hristodoulidis**—Yes. I would have thought that in terms of the welfare net they would be able to claim some sort of social security payment as well at that low level of income.

**Senator SHERRY**—Yes, they would be, but they are missing out effectively on both super and income at the moment.

**Mr hristodoulidis**—I agree.

**Senator SHERRY**—Particularly when you are looking at amounts of eight per cent at the moment going to nine per cent.

**Mr Hristodoulidis**—Yes.

**Senator SHERRY**—On one other issue, you are talking in your education area about introducing superannuation and national savings into the school syllabus. It would take a long time to have an impact if it were introduced even tomorrow. What concerns me about this whole argument is that there are significant groups of people in our society who will not understand—and they could have all the education and training in the world.

**Mr Hristodoulidis**—Yes.

**Senator SHERRY**—For example, on functional illiteracy, I think the last figures were about 17 per cent of the population. You cannot reach those people. And I would argue that a much larger group of people are simply not interested in learning about RBL limits, defined benefits or annuities. Realistically, how can you educate people in these sorts of areas?

**Mr Hristodoulidis**—I will answer that in two parts. Firstly, in terms of the education, we are actually putting together a brochure which we are hoping to distribute to schools through the education department, which is trying to pick up this issue of educating at that school level. We have also received some literature from the United States from the equivalent, I think, of the financial planning over there that worked together with the department of labour. The brochure is called ‘Savings for fitness’, so it puts that sort of fitness-sporting connotation to it. It was promoted through workplace relations arrangements. We are also looking at trying to get something like that up and running as well in terms of an education process.

Getting back to the second issue, I agree with you. There will be a proportion of people in society that obviously are not interested for some reason or another in terms of their superannuation—whether they are getting paid any, where it is getting paid, how it is working for them. Obviously, that is why with the super choice scheme—and I think it is pretty much across the industry—that people support a default scheme for such people. I do not think, for that proportion of the community, we should then say that we should not have a super choice scheme. There are a large number of people—especially as people’s contributions are getting larger and it is now higher than the value, say, of a motor vehicle—who are taking an interest and they should not be restricted from being able to choose where they place their super funds.

**Senator SHERRY**—You have referred to the US. Of course, super is not compulsory in the US like it is here. We are dealing with compulsory contributions for 91 per cent—according to the latest figures—of employees and it is one of the few systems in the world where that happens.

**Mr Hristodoulidis**—Around the world, that system has actually been applauded by many governments as being a good way of trying to educate the community about taking an interest in their long-term savings habits. We would have no problem with keeping the compulsion in there. I think it is a good way, again, as another part of the education program to teach people.

**Senator SHERRY**—We had choice driven by tax incentives until the late 1980s.

**Mr Hristodoulidis**—That is right, yes.

**Senator SHERRY**—Effectively, that is what we had and we have still got some of those old products around the place. All the evidence that I see is that, in part, it was tax driven but there are a lot of complaints about fees and charges and commissions. These were supposedly from people who voluntarily went into the system; they were not compelled into the system.

**Mr Hristodoulidis**—I would have thought the industry had matured a lot more since then. There is a lot more competition in the industry to bring some of those fees and charges down, and I think, from the consumer's perspective, consumers now have a bigger stake in terms of the amount of money that they have in the schemes.

**Senator SHERRY**—Yes, but up until superannuation was compulsory we had tens of thousands of agents running around the country selling the products on a voluntary basis. I had these people argue to me that they were central to the capitalist system, as we understand it. Hundreds of thousands of individuals running around, buzzing around, telling people to 'buy this product, buy that product, this is better than what you have got'. Competition was running rampant, and you are telling me that there is more competition now.

**Mr Hristodoulidis**—I would have thought there are more products available on the market. The industry has developed and it has matured. It has undertaken detailed research in terms of being able to offer different types of financial products, depending on the needs of the clients—whether it is short term, long term or even medium term. It depends on what they are saving for as well—whether they are saving for retirement income or for the education of their children. I would expect that the industry is a lot more mature.

**Mr Pinto**—And not only that, but, because there has been this number of complaints, there has been a pressure on industry to maintain those fees and to reduce them.

**Senator SHERRY**—But surely one of those pressures is the fact that industry funds have been fairly effective in providing a cost-effective service? A lot of the agents simply would not survive in those circumstances.

**Mr Pinto**—True.

**CHAIR**—In terms of your dealings with the regulatory environment, how would you rate the performance of ASIC?

**Mr Hristodoulidis**—They have done a fairly sterling job, given the resources. Just in the last federal budget, they had \$7 million cut from their budget. And the introduction of the Financial Services Reform Bill, be it on 1 January or later, is going to throw more pressure on them in terms of trying to meet the new licensing regimes, plus all of the compliance that goes with that. In light of the resources they have got, they are doing a really good job.

**CHAIR**—Do you think there is a need to have more flexible arrangements for people over 65 who continue to work?

**Mr Hristodoulidis**—Definitely. The more we give people an opportunity to take control of their financial investments or financial circumstances, the better we are. As a society, we are getting older and living longer and we are finding more and more people over 65 wanting to

stay in the work force on some sort of basis, whether it is reduced hours or a part-time basis, so they do need to have some flexibility.

**CHAIR**—In terms of the superannuation guarantee arrangements?

**Mr Hristodoulidis**—Again, that is something that we have not thought of carefully, but we are happy to take that on notice and consider it.

**CHAIR**—Do you think the ATO needs to have more discretionary powers? Perhaps you could take that on notice as well.

**Mr Hristodoulidis**—Yes.

**CHAIR**—Thanks very much for appearing before the committee today.

[11.43 a.m.]

**PETSCHLER, Ms Louise Margaret, Senior Policy Officer, Financial Services, Australian Consumers Association**

**CHAIR**—Welcome, and thank you for coming to the committee this morning. We are always pleased to have representatives from the Australian Consumers Association. We invite you to make an opening statement and we will follow up with questions.

**Ms Petschler**—I would like to make a short opening statement. As you know, our submission to the committee was very brief and we also missed the opportunity to provide evidence in May due to a lack of resources at the time. We very much appreciate the opportunity to come along today and we are happy to talk about any issues that may have come up in the committee's other public hearings that you would like us to take on notice or, perhaps, provide comment on today.

I would like to talk about a couple of issues around banking in particular and, briefly, some superannuation issues that may be relevant to the committee's terms of reference. On banking, I think it might be useful to think about some of the things that we have seen over the past month alone in banking. Our perspective is that banking remains a seemingly endless source of consumer dissatisfaction and there are very serious concerns that are continuously raised with us and through other surveys about the quality of service that consumers receive from banking.

We can have a look at a few things that have happened in August alone. The Australian Bankers Association in evidence to the Joint Committee on Corporations and Securities stated that banks have no social obligations. We have seen every bank pass on the full interest rate rise to their home loan accounts but none of them has provided any increases to transaction deposit accounts. We saw GST cost increases passed on to pensioner deeming accounts by one of the major banks. St George announced its 'best bank' plan earlier this month which, from our reading, means essentially reducing services for consumers, less full service banking options, massive staff cuts and, potentially, higher fees, particularly for transaction accounts. The banks appeared before the fee disclosure hearing in Adelaide and told consumers that we would have to wait for another six years before we could have point of transaction disclosure for electronic banking services. The Commonwealth Bank appeared before another Senate committee to talk about their shadow ledger practices which are, reportedly, industry wide practices and, thankfully, it looks like there will be some change in those practices as a result of those hearings. We also saw a significant profit result for the Commonwealth Bank which included almost a billion dollars in revaluations from their Colonial acquisition.

From our point of view, when you have an industry association like the ABA saying on the record that banks do not have a special social responsibility, it highlights a serious gap between the industry's understandings of its responsibilities and its role and consumers' expectations from banking services. Given that, we think it is no surprise that we keep getting such terrible results in our bank satisfaction surveys. In our most recent survey at the end of 1999, we had 71 per cent of our 6,000 respondents telling us that, in their view, banks were only out to increase their profits and were not interested in consumers. More than a third of our respondents felt that their banks were treating them less well than they had five years ago.

We would like to raise a couple of those broader consumer protection issues for the committee's inquiry given that it includes looking at consumer protection in banking as well as in other financial service areas. There are two issues in particular that I would like to talk about: the first one is bank fees and the second one is the idea of community service obligations and how social responsibility might translate for the banking sector. In terms of bank fees, the point that we would like to make is the question about the regulation of bank fee increases and also the inadequacy of disclosure for consumers in terms of the charges that they pay for banking services.

In terms of monitoring, we note that there really is no effective government monitoring of fees, *per se*, at the moment and no mechanism by which consumers can get redress for what they perceive to be an unfair or undue fee increase for a particular service, unless you can show that it breaches competition law, essentially. The committee would be aware that the Joint Parliamentary Committee on Corporations and Securities is looking at the issue of disclosure on electronic bank services. Consumer groups, including ourselves and the Financial Services Consumer Policy Centre, the Consumer Law Centre in Victoria, Redfern Legal Aid, the Finance Sector Union and some other organisations prepared a joint submission in which we outlined where we saw some really valuable opportunities to improve disclosure to consumers in terms of these banking products. What we have asked for is disclosure of bank charges at the point of transaction. We are aware that there will be a lead time in terms of some of the technology and there will be a need to look at some changed systems. We have presented a range of options that go from immediate solutions through to a two-year timeframe for looking at ways of informing consumers of how they are being charged for those services.

We think that disclosure of fees is a fundamental consumer protection issue in banking and it is something that consumers tell us that they want. They do not understand the fee regimes that are imposed upon them. Our survey results show us that more than half of our respondents find it difficult to tell which bank account is best for them because they do not understand or are not informed about the fees and charges that they will pay on those accounts. Research by the Financial and Consumer Rights Centre in Melbourne prepared for that Senate inquiry also showed that most of the consumers that were surveyed were unaware of the costs that they were being charged for electronic banking services, including ATM, EFTPOS transactions, Internet and telephone banking.

ASIC's own research undertaken for its consumer advisory panel also showed that consumers are asking for improved information—clear, plain English, personalised information—on what fees they are being charged for their banking products. They are also looking for some up-to-date information as they use their services on where they are up to with fee-free transactions and minimum balances. We think that, even though electronic fees are being addressed through a different inquiry, the need for fee disclosure in banking is a really important consumer protection issue and we would like to emphasise it again for this committee.

The other point that I raised earlier is the regulation of fee increases generally for bank fees. There is no monitoring mechanism—no regulatory mechanism—that enables consumers to feel that they have redress for what they perceive to be an unfair or a very high fee increase. We are certainly seeing very high fee increases. In 1999 transaction fees increased by 30 per cent according to Reserve Bank data, and that is backed up by data from research house Cannex.

They are fairly substantial hits for consumers and they are certainly sore points in the issues that are raised with our association.

We know that ASIC is working very hard with the industry to look at fee disclosure. We are very supportive of that work and we are a member of their working group on fee disclosure, along with the Financial Services Consumer Policy Centre. We hope that we are going to get some significant gains through that forum, particularly in terms of statement disclosure. But we also believe it is important to keep the pressure on to see the industry take on point-of-transaction disclosure because they seem very reluctant to take that issue seriously. We think they might be presenting some unrealistic arguments about how much it is going to cost them to provide that basic information to consumers.

The ACCC is also looking at interchange and merchant fees, as is the Reserve Bank of Australia through their payment system review. We think that is going to be a very exciting development for consumers as we think we are finally going to see potentially collusive and anti-competitive fee setting practices exposed. We think we will finally get to open the black box on how these fees and charges are set and see just how much consumers are paying for what would appear to be a closed-shop practice that works to the detriment of industry and consumers.

While those are exciting developments, we would still like to emphasise that bank fees are a consumer sore point and we would encourage the committee to consider whether the monitoring of bank fee impacts and increases might deserve further attention as part of the regulatory environment. We also emphasise how important we feel fee disclosure is as a consumer protection issue.

The second banking issue that I want to comment on is the question of community service obligations, which have received some coverage over the past month and obviously have been a source of concern to the ACA for a number of years. I would like to outline why we think social obligations should be placed on the banking sector and what we mean by community service obligations. Our argument is that banks have a special role in our society. We view them as an essential service and we think that, like other essential services that also operate in competitive and profit-making environments, there is a valid argument for banks to operate with mandated community service obligations that provide minimum protections to consumers in terms of service standards and access.

We are not alone in that view. We believe that statements by the Prime Minister and the Treasurer in relation to the social responsibility of banks and their need to meet consumer concerns about access support our arguments. We are aware that organisations like the National Farmers Federation see this as a very important issue for their constituents. For example, the FSU is raising these arguments through campaigns at the moment. We have also looked at statements by some of the regulators. I will go back to the time of the Wallis inquiry and read a quote from the ACCC, which states:

... basic banking services have much in common with certain utility services like electricity, gas and water. Barriers to accessing such services due to branch closures can significantly detract from the quality of life and social standing of individuals and families.

We think there is a general consensus—it is certainly a view that comes through from consumers—that banks are providing an essential service yet they are managing to do that in a self-regulatory environment where they are not required to meet access undertakings or to provide universal service obligations—universal in the sense of being consistent across the industry—when other forms of essential services are required to do that.

We look at experience in overseas jurisdictions when the banks tell us that to meet such obligations would render them uncompetitive. In the United States the community re-investment act has operated for decades and, particularly over the past 10 years, has been a really powerful incentive to encourage the banking sector to connect with its communities and to take seriously the issues of access and branch services and the idea of community investment. Different state jurisdictions in the United States have introduced minimum service requirements around access to basic transaction accounts which require a certain number of fee-free transactions and minimum access in the sense that everyone should be able to access an account that will provide them with transaction services. Particular states set fee limits on those accounts.

We think also of developments in Canada in legislation that will go before their parliament. They are talking about similar issues in terms of consumer protection in banking and access to transaction accounts at a low cost, particularly for low-income consumers. They are talking about mandated provisions around branch closures, which require a set time frame and community consultation as well as proactive efforts by the bank that is withdrawing its service, to ensure that there will be full service banking options available to that community. They are also talking about revised merger approval processes that go to the heart of whether consumers will see less service as a result of consolidation in the sector. There are also examples in the UK, but I will not run through all of them. We think there are some powerful arguments in other developed nations that show that we could have similar requirements through a regulatory framework that would have some real benefits for consumers.

To summarise, we believe these sorts of obligations should apply in terms of basic banking services. There should be affordable and accessible accounts. In terms of access, it is about maintaining some forms of face-to-face banking for consumers and ensuring viable branch networks for the majority of communities. It is about commitments to affordable service options in areas where services are reduced or withdrawn by the banking sector. There must be some industry awareness about barriers to access for certain groups of consumers to different forms of banking, particularly new technology banking, and consultation on branch closures or service changes.

We believe there would be some value in a community investment argument, whereby, for example, we could use a public rating of how banks perform against particular lending requirements and deposit transaction services. That would focus their social obligations in terms of their financial services capabilities and how well they service their communities. We also think there would be benefit for consumers, and certainly more security for consumers in terms of their feelings towards the banks, if we could establish some minimum requirements regarding fairness in banks' treatment of customers, perhaps some general policies around fee increases and interest rate pass-throughs and some undertakings about the way that the banks relate to their customers and look at issues of redress.

The argument that we have heard from the Australian Banker's Association centres around the fact that banks are already good corporate citizens. They pay lots of tax and make valuable contributions to communities and charitable causes and, as such, they meet their social responsibilities. They argue that to regulate to require any form of minimum service standard or community service obligation particular to the banking sector would impose an undue and unfair burden on that industry.

We would make a couple of points in response. Firstly, we do not see a profitable industry paying its requirements in taxes as meeting a special social obligation or community responsibility. Secondly, I do not think anyone disputes that the banks can, and do, act as good corporate citizens—we do not think it is unreasonable to suggest that they should, when you look at their profit results. I am aware that the ABA has sent to the committee a list of the many charitable causes that banks contribute to, and we applaud them for that—that is an example of good corporate citizenship. But that is not what we are talking about when we talk about community service obligations. We think this highly profitable sector gets a lot out of contributing to the community. They do it for a variety of reasons, one of which is to enhance their profile and engender consumer loyalty and another may be to derive the benefits that accrue from the nature of those commitments. But that is not what we mean when we talk about community service.

**Senator CONROY**—If they gave it anonymously perhaps you would feel better.

**Ms Petschler**—That would be a different story. The other issue that the ABA has been talking about is the question of shareholder returns versus consumer service: if we ask them to meet minimum service standards, we are ripping off shareholders and, ultimately, consumers because the industry will be less profitable.

We are not convinced that the sorts of things that we are talking about would render the industry less profitable. In different hearings and evidence, the ABA has argued that banks provide these services and are willing to look at improved practices in a range of areas. So we think it would be an opportunity for the industry to take up the challenge—if it chose to do so—in terms of the way it connects to its communities and the way it provides services. We are not saying that we want the banks to bankroll regional Australia; we are not saying that they should have unfair or uneconomic conditions imposed upon them; and we are not saying that we do not want a strong, profitable and competitive banking sector. But we are saying that banking has a unique nature. It is an essential service and banks have essentially a captive transaction market that is not comfortable with the quality of service it is receiving and does not take comfort from service standards and its ability to access those services at the moment.

We think there is a powerful argument to make in terms of looking at some form of community service obligation—whether that be through perhaps an industry code that has strong oversight by the regulators, public reporting against certain requirements or perhaps attaching conditions to banking licences—that would cover some of these common consumer concerns. We would welcome the committee's consideration of those issues and perhaps some thoughts on whether it would provide better consumer protection results in banking. I am not sure whether you want me to touch on superannuation.

**CHAIR**—Yes.

**Ms Petschler**—We want to voice our present concerns about the way that choice appears to have entered the market before adequate consumer protection measures are in place. Our argument is that, if left unattended, the market forces around choice—we are already seeing marketing of choice and choice of funds, particularly in certain jurisdictions—will place consumers at risk because there is an absence of consumer protection standards and certainly no effort to look at widespread consumer education on superannuation.

We think market behaviour is changing. Consumers are being left without adequate protection while the debates around legislative measures to introduce choice and consumer protection are taking place. We think lack of consumer understanding, the numbers of multiple and lost accounts and expanding investment and fund choice practices are creating serious consumer protection issues. We would encourage whatever efforts can be made to look at the arguments we have been raising, and which have been brought before this committee and other inquiries, about the standards for consumer protection that we need to see as part of any choice environment.

Our argument is that consumer protection measures in a choice environment must be able to ensure that employees and consumers receive fair advice that takes into account their financial needs and lifestyle circumstances. We must see very strong prohibition of twisting or churning, particularly for low-income consumers who might be encouraged to switch funds in a way that would not be beneficial to their long-term retirement incomes. We would like to see a strong prohibition of misleading and deceptive conduct on the part of agents and advisers. We believe that would need additional resources for enforcement as we are not convinced that the current regime would be able to deal with those issues adequately. We would obviously like to see full disclosure of fees, charges and commissions, and I think we would endorse the principles outlined by the Financial Planning Association in their evidence before the committee.

We would like to see strong mechanisms to enable complaints in a super choice environment to be dealt with quickly and cheaply for consumers. We would like to see some low-cost options for combining accounts that would perhaps get us away from some of the problems we encounter at the moment when people's superannuation is spread across too many different accounts. We would also like to see some genuine protection against employers and sellers making deals that are not disclosed to employees, particularly when those deals might relate to the default fund option. We also have some issues around default funds, which we have outlined previously, about the importance of the insurance and income protection components of those funds and ensuring compliance.

In relation to superannuation, the only additional point I would make is that we are still concerned about the provisions of the Financial Services Reform Bill in terms of cold calling and pressure selling—which we think are real hot spots particularly in a super choice environment. We would welcome efforts to prohibit or ban those practices, and we think regulators could look to a range of options to restrict the risk of pressure selling in a choice environment.

The other point we have concerns about at the moment—I am sure they are shared by industry as well as consumer advocates—is the size of the lost members register. In June the tax commissioner referred to a figure of \$4.5 billion in the lost register account. According to some industry sources last week, that figure was \$6.9 billion in August—which would be almost a 48

per cent annual increase in lost member funds. There are clearly issues around the definition of a lost member and how the register is activated. However, there would seem to us to be enormous opportunities to reconnect consumers with their superannuation funds, and we would welcome any moves that perhaps would encourage an annual round-up of lost funds or some measures to inform consumers of how they could access the funds that they may have forgotten about, or perhaps not followed through on, that are sitting there and should be consolidated to earn them a stronger retirement income.

Consumer education in superannuation is critical and must obviously be tied to an effective disclosure regime. But we are also on record as supporting a superannuation legal service or resource centre. The consumer movement has been sending the consistent message that it would be beneficial to have resources that would enable consumers to receive independent legal advice about their superannuation and perhaps a central mechanism through which consumers' concerns around superannuation could be put forward.

The third issue relates to the superannuation guarantee charge—and I am aware that everything I am going to say I think you have heard already from other witnesses. The ACA would support more frequent payments of the superannuation guarantee, whether that be quarterly or monthly. We would see significant benefits for consumers for a range of reasons, which I am aware has been outlined to the committee.

We also think there is a consumer issue in terms of tracking down under- or non-payment of the superannuation guarantee. It seems unnecessarily difficult for consumers to find out what has happened and to follow through on whether the ATO is investigating or has managed to get the funds. It is slanted away from a consumer friendly perspective. We would welcome any moves to reform that process to enable consumers perhaps to follow through more easily on what is happening with the money they should have received and also perhaps see some improvements in collection mechanisms. I think I will finish there.

**CHAIR**—Have you had many complaints about the superannuation guarantee administration from people aged between 65 and 70?

**Ms Petschler**—No, we have not. I suspect those complaints would perhaps be made through community legal centres rather than directly to the ACA. But it is not something that has emerged in our feedback through our forums. We have not specifically gone out and asked consumers those questions in our surveys.

**CHAIR**—Do you think older people may feel somewhat inhibited about going to a consumer association with these sorts of complaints?

**Ms Petschler**—That could well be the case.

**Senator SHERRY**—I think it is correct to say that, at the moment, at least part of the superannuation industry is in a choice environment but another substantial part is not. If your concerns about so-called 'choice'—which I refer to as 'deregulation', by the way—are not met and the protections you propose are not introduced, should the deregulation of superannuation go ahead?

**Ms Petschler**—Our support for choice in superannuation has always been conditional on adequate consumer protection measures, so the answer would be no. But we are aware that the market has moved to a situation where there is choice. We do not think that is going to slow—

**Senator SHERRY**—Sorry, may I correct you there? The market has not moved to a situation where we have choice. Some legislative jurisdictions have—particularly WA, where we do not have good survey data on what has happened yet. However, no other jurisdiction has moved to effective choice on superannuation.

**Senator CONROY**—By ‘choice’, are you perhaps referring to investment choice rather than choice of fund?

**Ms Petschler**—I guess I am rolling them together. When I say ‘choice’ in this context, I am talking about choice of fund. I think investment choice is another area where serious consumer education issues are involved. The answer to your question is no.

**Senator SHERRY**—You painted a fairly accurate and depressing picture of the activities of banks. Banks are a great proponent of superannuation choice—I do not know whether you are aware of that. They have been very active in promoting this concept over a number of years, both before this committee and publicly.

**Senator CONROY**—I am sure they have a benevolent reason.

**Senator SHERRY**—Yes, I was getting to that: the benevolence of banks pushing this superannuation choice issue. It concerns me and I would like your response. Given the concerns you have outlined about the activities of banks, what confidence can we have that the banks will approach the superannuation issue with benevolence in the interests of low-income members, making sure that they are treated fairly and reasonably? I am concerned because this is a heaven-sent opportunity for banks: they can get their tentacles around compulsory contributions at a set level. Despite the caveats you put on it, I am concerned that your organisation is effectively advocating that the system be deregulated so that banks can move in—and they are primed; they are keen to do it.

**Ms Petschler**—Yes, I think they certainly are keen to do it. That issue goes to the heart of the regulatory regime you establish around choice. While we do see very serious consumer protection issues, we do not think they are insurmountable. We think we have the opportunity to learn from market failures in other jurisdictions and have a viable and very strong consumer protection regime that would operate to prevent any sector of the industry from taking advantage of consumers.

**Senator SHERRY**—Why should we have a deregulated system that effectively places the selling distribution in the hands of commission agents much more so than occurs at the moment? Why create that system and why extend it?

**Ms Petschler**—Our position on superannuation choice is essentially an issue of consumer sovereignty, and I think the ACA has been pretty consistent in maintaining that view. We think consumers have a right to make decisions around the investment of their funds. Superannuation

choice offers a number of benefits for consumers provided we can cross off our serious consumer protection issues.

**Senator SHERRY**—Doesn't investment choice resolve that problem?

**Ms Petschler**—To a degree.

**Senator SHERRY**—People choose where they want to invest their money as distinct from the vehicle through which it is invested.

**Ms Petschler**—That is right. But they do not have the choice of fund.

**Senator CONROY**—You have just made the straight statement that there are benefits. Do you do a cost benefit analysis?

**Ms Petschler**—We have not done a cost benefit analysis but we do see—

**Senator CONROY**—If you were able to say, 'They have a benefit of notional consumer sovereignty but it is going to cost them \$1,000 extra a year in their account', how would you do a cost benefit analysis? How would you make the call then?

**Ms Petschler**—I think the issues around how much extra it is going to cost are still quite open to debate.

**Senator CONROY**—I was just picking a figure: maybe it is only \$100 or maybe it is \$10,000; I picked \$1,000 out of the air. Are you able to make that judgment when you have not done a cost benefit? If you look at just one side and say, 'Consumer sovereignty; that is a good thing but we accept that there is going to be all these extra costs', at what point do those costs possibly outweigh the consumer sovereignty at a macro level? We are talking here about a macro consumer sovereignty benefit but they are paying the cost for the macro benefit at an individual micro level. So it is hard to measure them. How does your organisation do that?

**Ms Petschler**—My understanding—and I have not brought along the figures—is that the question around whether it will be an additional cost is still open to debate, and there is a variety of different views on that. So, in that sense, we are not convinced.

**Senator CONROY**—Do you think all that advertising with Bernie Fraser is free?

**Ms Petschler**—Marketing is certainly going to increase.

**Senator CONROY**—That is a cost. You have to lump that in with the cost because that comes off the balance of the individual. Bernie is not doing it for free and the TV stations are not letting him on for free—as much as he has become a cult figure. There are a lot of costs in marketing as well as in administration. You seemed to be implying that there was not much of a cost.

**Ms Petschler**—No, all I am saying is that I did not come prepared to talk about the costs either way. Different sectors of the industry certainly have different views on the cost savings that they will be able to make in different areas.

**Senator CONROY**—Not GST savings.

**Senator SHERRY**—This is a radical change in policy that will have a significant impact in terms of national savings and individual savings—which, in part, are to replace pensions. In light of the ageing demographic and those sorts of things, surely it is incumbent on an organisation like yours to look at what happened in the UK and Chile where this experiment has been tried with serious consequences.

**Ms Petschler**—Yes, and we have. Yes, there were very serious consequences. I guess we could refer to Poland as well. They are exactly the consequences that we do not want to see here. We have the benefit of having seen those experiences and those outcomes, which were ultimately poor for both governments and consumers. That is exactly the situation we want to avoid in Australia. I note that ASIC seems to be reaching perhaps a degree of comfort in terms of their ultimate ability to regulate the sector. We are not convinced at the moment that those measures are there.

**Senator CONROY**—They regulate the banks well too!

**Ms Petschler**—I certainly think it is comforting to know that the regulators are looking at those examples of market standards as well.

**Senator SHERRY**—But the regulators in the UK and Chile still have not got it right; they are still sorting out the mess.

**Senator CONROY**—It is now \$12 billion, isn't it?

**Senator SHERRY**—At last count, I think it was £12 billion.

**Senator CONROY**—Yes.

**Senator SHERRY**—Let's look at investment choice. It has been introduced and is quite widespread now through major sectors of corporate and industry funds. I understand that the take-up has been very low. There is an additional administrative cost to investment choice. The consumer is sitting down and making a choice. It is voluntary, that is fine. They have to be doing this pro-actively. But the take-up is still extraordinarily low. I do not have a problem with that concept, but why should we deregulate a system and effectively force people to make a choice about where to go when I think all the evidence is that they do not want to do it? The take-up will be very low if it is voluntary as distinct from people being forced to make a choice—a bit of a contradiction in terms—and the cost will higher.

**Ms Petschler**—Again, I am not familiar with the figures on the take-up of investment choice. I am more familiar with the issue that consumers are perhaps choosing poorly compared with their actual investment profile and with how the trustees would choose for them.

At the moment there is a profound lack of information amongst consumers about superannuation. It is a very poorly understood area. That might reflect consumer reluctance to look at investment choice as well, but we just do not know at the moment. I think one of the benefits from our point of view in terms of super choice is that it will operate effectively and be supported only if it is tied to consumer education. Informed and pro-active consumers will be able to make better choices about their superannuation.

It is a compulsory area. Any regulatory environment must recognise that fact. At the same time, there are enormous differences in returns. There are different sorts of funds that people might be attracted to for ethical reasons; they might choose to invest for a whole range of considerations. At the moment they are prohibited from doing that .

**Senator CONROY**—I do not know whether you remember, but when we introduced the SGC we ran a national television advertising campaign—depicting a little pot plant and a grown tree—that at least alerted people to what was happening. I do not think that would qualify as what you describe hopefully as an ‘education campaign’. The government spent \$4-odd million at the time—I am sure that would be a fair bit more in today’s dollars; it was nearly 10 years ago. If you were serious about consumer education—and given the \$4 million that we paid for the little pot plant—what sort of dollar figure do you think you would need to be satisfied that you were getting a decent education campaign?

**Ms Petschler**—It is a bit like pick a number from our point of view. We would start somewhere around 12 perhaps. We are talking about a comprehensive ongoing campaign. The exact nature of the resources and the way that the campaign would be rolled out are really critical issues because you need to reach a range of different population groups in the community and there will need to be different strategies.

**Senator CONROY**—You want to see a lot more of Bernie Fraser on television?

**Ms Petschler**—We think you would need to look at more than TV ads. There is going to have to be a whole range of education measures. Part of that may be looking at the school curriculums as the FPA suggested as well.

**Senator CONROY**—Given the government have been prepared to engage in a fairly major publicity campaign about a fairly significant tax shake-up, you would hope they would be willing to spend similar sorts of money on something that is a fairly radical deregulation of the existing system, as Senator Sherry has described it. You do not think of a figure of \$10 million? I think the final figure of the actual dollar advertising was \$50 million to \$60 million.

**Senator SHERRY**—That was propaganda.

**Senator CONROY**—Hopefully we would see more of an educational aspect to the super choice rather than what somebody told me after seeing the government’s original plan on choice was the Prime Minister sitting next to a fire telling everybody they now had choice.

**CHAIR**—Senator, you are trying to lead the witness.

**Senator CONROY**—I am just making some observations. Given that the government had been prepared to put their money where their mouth was to promote a radical change in the tax system, you would hope that they were prepared to put their money where their mouth was to the tune of at least \$10 million.

**Ms Petschler**—We would assume that the government would want to have a comprehensive education campaign as part of any super choice environment. We would hope that it would be resourced in a way that would mean it was effective for consumers.

**Senator CONROY**—But you have a benchmark there with the tax. That is their being serious about selling a radical change. You have a benchmark to test the government by it if they are really serious?

**Ms Petschler**—It is going to be a question for the government ultimately over what they are going to say.

**Senator CONROY**—It is a question for you as well.

**Ms Petschler**—The point we would make is the really low awareness in terms of superannuation.

**Senator CONROY**—Absolutely, less so than on tax.

**Ms Petschler**—Yes. It is a fundamental issue. It is people's retirement income and we would like to see a very well resourced campaign.

**Senator CONROY**—Regarding cold calling and prohibition, would you ban door-to-door sales?

**Ms Petschler**—Yes.

**Senator CONROY**—Would you ban door-to-door hawking of securities as well?

**Ms Petschler**—Yes, we would prefer to see a blanket prohibition of all forms of cold calling.

**Senator CONROY**—We currently allow door-to-door selling. What is the difference between a knock on the door and a phone call? If you ban one, to be consistent, you have to ban the other. Would you, therefore, start banning door-to-door financial service sales? You have cleared up where you are at on it. I still have to work it out myself.

**Senator HOGG**—Just following on from the questions Senator Conroy has put, you said super is very poorly understood. How long do you think it would take before there was a reasonable understanding of superannuation in the broad community? I know it is a fairly difficult question to ask. Is it a series of one-off campaigns, in which case there is a limited residual that people will keep out of each campaign? How long do you believe it would be before there is a reasonable understanding that would enable people to make a reasonable choice?

**Ms Petschler**—I think the issue of understanding of superannuation generally is going to require some form of continual education program. I have not thought through how education specifically and advertising and information around choice, in particular, link to that. Clearly, we would think that there are two sides to it. You would want a sustained and long-term campaign to improve the awareness amongst consumers of superannuation and the issues involved in superannuation. At the same time, if you were talking about a choice environment, it is a drastic change. It is a significant change and there would need to be some very effective awareness raising and education resources that I assume would be more time limited. That would then link to the longer term education measures.

**Senator HOGG**—I am not trying to pick on you, but you have used a number of words which concern me, like ‘long term’—which I used—‘sustained’, ‘very effective’ and ‘comprehensive’. They are not exactly measurable or quantifiable. Of course, this is where my real concern comes in. As Senator Sherry mentioned earlier, there are 17 per cent who are just functionally illiterate. I have seen figures that I think go as high as about 40 per cent who have a degree of numeracy and literacy difficulties that make it very difficult for them to understand even the basic and most simple of statements that might be made on issues such as superannuation. It seems to me—and I would welcome your view—that, unless this issue can be properly addressed, we are going to have the problems and the pitfalls. And unless someone can put down some sort of program or framework and some sorts of benchmarks which must be obtained before the whole thing unfolds and rolls out, it seems to me that we are just waiting to open Pandora’s box.

**CHAIR**—Is that a comment?

**Senator HOGG**—No, I am asking for a comment on that.

**Ms Petschler**—We do not disagree with the risks that are involved, which is why we come back to the question of what regulatory mechanisms need to be set up to prevent misselling and to provide sound default fund options for consumers. We think that if those protections can be put in place and can operate with the other issues we are talking about, which are increased awareness and understanding, then we would have less concern on that front.

**Senator ALLISON**—Can I go to the question of banking and ask you if you could just expand a bit on the sort of mechanisms that are in place for the Banking Industry Ombudsman and why, in your view, there are so few mechanisms for protecting consumers.

**Ms Petschler**—In terms of their ability to cover disputes?

**Senator ALLISON**—All of the issues that you raised: fees and making complaints about fees. Are you telling us that is actually not possible through the ombudsman?

**Ms Petschler**—Yes, that is right.

**Senator ALLISON**—What can the ombudsman do in relation to banking?

**Ms Petschler**—The ombudsman is constrained by the industry code of practice. That is under review at the moment and there would be scope for some of these issues to be

incorporated into the banking industry code and the credit union code if the industry chose to undertake that route. The Banking Industry Ombudsman, in our view, performs a very useful role for consumers. There is a very high level of awareness amongst consumers about the Banking Industry Ombudsman. In fact, the Banking Ombudsman acts as a referral point for all the other financial services alternative dispute schemes that we have and, in a sense, they are looking to beef up that referral role because everyone knows that they exist. They will then be referred to the relevant program.

The question of fee increases comes back to the notion that the industry operates under market mechanisms and a self-regulatory model, at least in terms of fees and charges. The Banking Industry Ombudsman does not have jurisdiction. We would probably see it as more of a policy issue in the sense that perhaps the banks could agree to some form of policy or principles around how they will apply fees or fee increases rather than specific issues for the Banking Industry Ombudsman.

**Senator ALLISON**—I think you were here earlier when the FPA said that what we need is a consumer advice centre or a legal centre which deals with superannuation issues. You are a consumer organisation. Are you constrained in what you can do? Do you support the idea of a government funded organisation or set of organisations to do this work, leaving aside the choice environment for a moment?

**Ms Petschler**—Yes, we do support the idea of a superannuation legal service or consumer service and we would see there would be some options in terms of who might provide that service. The consensus is that perhaps a legal aid body would be able to undertake those functions or we might set up a different organisation but the key factors would be independence, the ability to provide quality advice and consumer representation on a board of management or committee that would oversee the operations.

**Senator ALLISON**—What about the need for research for tracking trends or, say, collecting information about the sorts of products being offered? Do you see that as being part of this role or is that something that could be dealt with in another organisation?

**Ms Petschler**—Conceivably, yes, it would be. Certainly, when we have talked about a superannuation centre, we had in our minds an organisation that would be able to undertake some of those broader functions or could act as a clearing house for information that is prepared by industry and regulators.

**Senator ALLISON**—Is it a consumer issue for you that the ATO has, at least thus far, not prosecuted employers who fail to make their proper SG contributions? Have you been involved in this discussion?

**CHAIR**—I am not sure that that is correct. I think the difference is a prosecution policy. I think there are cases where they have prosecuted.

**Senator CONROY**—They definitely said they have not prosecuted anybody.

**Senator ALLISON**—They had not until a certain point in time when the audit was done.

**Ms Petschler**—That is how I understand it.

**CHAIR**—I am not sure that that is correct though.

**Senator ALLISON**—In any case, if I can rephrase the question, do you get complaints from people who have tried to go through the complaint process? I was trying a little earlier today to establish what a typical case study might be of someone who thinks they are not being paid their SG. Who, in your experience, do they come to first? What is their experience when they get to the ATO? Is the call centre approach, ‘We might call you back, but we cannot tell you what we are doing in terms of investigating’? How problematic is that for you as a consumer organisation?

**Ms Petschler**—We do have concerns with that. They are the issues I was trying to flag just briefly in my opening statement. We do have some case studies that we could provide to the committee that I would be happy to send in. They would be non-identified. Consumers find it very frustrating in terms of their inability to find out what is happening with the monitoring. They are concerned that the ATO may not be following up on what they perceive to be small amounts of funds but which, for consumers, are significant amounts. An amount around \$4,000, for example, is a significant amount, particularly for a younger person and to lose those funds is a major issue.

We would welcome some further examination of the overall effectiveness of the ATO’s monitoring and enforcement. We would like to see perhaps some more transparent reporting on how they are going about those practices and what they are achieving.

**Senator ALLISON**—You say that the banks are still resisting the idea of electronic transaction fees being disclosed. Is there better practice in another country? Are those disclosures already operating somewhere?

**Ms Petschler**—It varies in terms of the products. ATM disclosure is a sensitive issue. We have seen surcharge disclosure—surcharges are not an issue yet in Australia, but potentially could be. We do see surcharge disclosure in other jurisdictions. But in terms of the technology being able to show the cost for the service at the time, that really does not operate yet. Our view is that the technology is advancing to the point now where, according to the reports from the manufacturers, we will be able to buy concert tickets and personalise our ATM screens. We see it more as an issue in terms of the advances that are possible through the technology. We appreciate that there will be changeover issues for the banks but in areas like Internet banking, for example, we do not see any obstacle, other than a start-up cost, to providing consumers with a personalised option to see the fees that are applying. My understanding is that providers in parts of the United States do provide that information much more freely than currently in Australia.

**Senator ALLISON**—Isn’t there a regulatory regime anywhere that requires the provision of that disclosure over time? Where should Australia look to for best practice in terms of the regulatory regime on fees?

**Ms Petschler**—If the committee agrees, I would like to provide a section of our joint submission that we made to the Joint Committee on Corporations and Securities and which

outlines international developments and trends. I think that might perhaps be the best way to address that question.

**Senator ALLISON**—If you have made the submission, we can follow that up ourselves.

**Senator SHERRY**—There is one issue I would like you to take on notice to think about, if you could—a bottom line issue in respect of so-called choice in superannuation. Fees and charges are disclosed to APRA. I have looked at the APRA document which shows the moneys flowing into funds, and it gives an all-up figure on the level of charge for particular categories of funds. But, again, do you think that, as a bottom line, much more detailed information should be provided in any sort of deregulated environment in respect of super; for example, what the level of fee and charge is for persons earning less than \$20,000, \$30,000, \$40,000—each income? Should we have access to that sort of information to determine what is going to happen in the market?

**Ms Petschler**—Would you like me to take that on notice?

**Senator SHERRY**—Yes.

**CHAIR**—Thank you very much for appearing before the committee this morning. I think a representative of the Audit Office made a factually incorrect statement which has the potential to get a headline, and I am concerned about that. I ask that someone from the tax office correct that, please. The audit report referred to a lack of policy in relation to prosecution, and I think a further statement was made about there not being any prosecutions. I ask that Mr David Diment from the tax office speak briefly to the committee, if he would not mind. I understand that details of how many will not be able to be provided; that will have to be taken on notice. But I think that, for the record, we should at this point have a comment from Mr Diment.

[12.37]

**DIMENT, Mr David, Assistant Commissioner, Superannuation, Australian Taxation Office**

**CHAIR**—Please proceed.

**Mr Diment**—Being here for the evidence earlier today, it was true that, up until the ANAO did their audit of superannuation guaranteed administration, we did not have a strategy for prosecution. But always—every year—we have undertaken numerous prosecutions under the SG act, both around section 77 of the act, which is about prosecuting employers if they do not provide us with the information, and section 36. In addition, we have undertaken hundreds of prosecutions around the nonpayment of super guarantee. When I come before the committee again, I will be happy to elaborate on the fact that it is never the case where it is just an SG debt. Very rarely is it an SG debt that an employer owes us; it is always part of a larger, composite debt owing to the Commonwealth. We do hundreds of those prosecutions a year, and I am happy to supply the details to the committee. But thank you for the opportunity to correct the misinformation given by the National Audit Office. We do prosecutions but we just did not have a prosecution strategy. We now have a strategy; it is in place and it is operating.

**CHAIR**—We would appreciate some statistics when you appear later on.

**Senator HOGG**—There was a follow-up question from Senator Allison. If there was no prosecution strategy, was there a practice in place? If so, can you make available to the committee what your general practice was?

**Mr Diment**—The general practice is part of the ATO compliance model, where prosecution is the very last step that we undertake. We start with education; we start with self-regulation; and we move up to the prosecution strategy as a last resort. But the strategy is very helpful, because it now allows us to target that activity. The activity always happened, but the strategy gives us a target for that activity.

**CHAIR**—That you very much, Mr Diment, for appearing before the committee.

**Proceedings suspended from 12.39 p.m. to 1.33 a.m.**

**FERGUSON, Ms Jane, Director, Public Affairs, Institute of Actuaries of Australia**

**KNOX, Dr David Montgomery, President, Institute of Actuaries of Australia**

**MARJORIBANKS, Ms Christa Jane, Member, General Insurance Practice Committee, Institute of Actuaries of Australia**

**CHAIR**—I welcome representatives from the Institute of Actuaries. David, do you have any comments to make about the capacity in which you or your colleagues appear?

**Dr Knox**—Christa Marjoribanks, who is a member of our general insurance practice committee, is involved in preparing submissions on prudential regulation in that area.

**CHAIR**—Would you like to speak to your submission?

**Dr Knox**—I would like to make a few opening remarks and then be available to discuss matters and answers questions. We will be concentrating on your first term of reference, dealing with prudential supervision and consumer protection. Perhaps not surprisingly, we believe that the actuarial profession has much to offer you in this area. We have appeared before you before and, I hope, have added value to your deliberations.

In particular, in terms of prudential regulation, the relevant expertise of the actuary is looking at the identification, assessment and analysis of financial risk—and I mean financial risk in all its forms—and, in that sense, the introduction and application of control cycles or feedback loops to managing financial entities who are subject to these risks. Another characteristic of the actuarial profession is that we have a future-looking perspective. We clearly look backwards in terms of experience and data, but we are very much concerned with what will happen in the future. Of course, in prudential regulation that is an important component of your concerns.

I will make a couple of remarks in the area of prudential regulation generally. We all recognise that the financial services landscape is changing rapidly, with the convergence of products and, indeed, institutions; new technology; increasing consumer empowerment; globalisation; and, in the superannuation area, ongoing changes in that environment. The Institute of Actuaries of Australia believes that the principal objective of prudential regulation is to maintain a low or very low probability of institutional insolvency. You can never get rid of that probability. There will always be a possibility of it, but it needs to be kept low, and therefore you need to minimise the possible consequential loss to the institution's ultimate consumers. Therefore, we suggest that regulators need to do three things: (1), to promote prudent and proper behaviour within those institutions; (2), to ensure the effectiveness of an institution's system for identifying, measuring and managing the various risks; and, (3), to ensure the adequacy of capital as a buffer against unexpected losses. Of course, the use of each of these goals must be balanced against the need to maintain a viable, competitive and progressive financial services sector.

The institute also suggests, with regard to APRA's operations, that, firstly, APRA continues to develop a uniform approach to the provision and supervision of financial service entities; and,

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secondly, that APRA continues and extends the successful use of qualified professionals appointed to regulate its entities for internal risk management, monitoring and reporting. What we mean by professional individuals is that these individuals, within the organisations or outside them, have a better understanding of the operations of those institutions and are therefore better placed to respond to them than solely relying on the reactive systems of a regulator.

We could go on about prudential regulation but let me move on to the second area we want to talk about, and that is superannuation. We have noted from other submissions that a number of issues have arisen in respect of the regulation of superannuation. Some of these issues may be relatively minor, but most have a link into the role of superannuation within the Australian retirement income system. The Institute of Actuaries of Australia has recommended that a thorough review of superannuation be undertaken as part of a broader review of Australia's retirement income policy. Such a review needs to consider such issues as the purpose of superannuation, the role of the regulator, the extent of any promises and, in so doing, the expectation of the members of the funds—in other words, the expectations of the community. After all, as we move into greater member investment choice and the possibility or, dare I say, the probability of fund choice, it is essential that fund members understand their responsibility and the responsibilities of the government and the regulator.

I can give you a couple of examples. Some have raised the issue of the over-65s in the system. Should people over 65 be able to contribute to superannuation? Should they be able to take some of their benefit, then come back into the system and contribute and go through a phased retirement period? With an ageing population, we must encourage greater employment and saving opportunities for those in their 60s and 70s. Of course, the answer to how you do it should be placed in the context of a broader retirement income policy. You cannot tackle that as a one-off piece; you need to see it in the broader picture.

A second example in terms of superannuation from the members' perspective is: how do they identify the difference between a superannuation investment and a non-superannuation savings investment? It is apparent that super is different because it is compulsory and it is preserved. Therefore, there are clear differences in the government's motivation. But as we move to member investment choice and fund choice, from the members' perspective, many of the risks are similar. How does prudential regulation contrast and compare those two areas? Therefore, we suggest that if we move in that direction, as part of the review we need to revisit that area. In terms of fund choice—we may wish to explore this in a couple of moments—disclosure of information is absolutely critical. Information—perhaps it is stating the obvious—must be easy to understand in whatever form it is presented, accurate, reliable and consistent between funds. Comparing different super funds is not easy but we have to do it as best we can in a consistent manner.

In conclusion, the institute recommends that there is need for a full review to be undertaken, within which we include the role of prudential regulation within the super system. The review should not be piecemeal. After all, the role of prudential regulation and consumer protection must be consistent with the purpose of superannuation within a retirement incomes policy and must lead to clear expectations and understanding within the community. That ends my opening remarks and, naturally, we are very happy to take questions.

**CHAIR**—I am interested in your review of superannuation because I could see some conflicting goals there. For example, I would have thought that a lot of consumers of superannuation products would be rather worried about another review, another major change to superannuation, because the message appears to be that they want to stop all the legislative changes and they want certainty and they are starting to get a little bit worried about sovereign risk. Would you like to comment on that?

**Dr Knox**—That is a good question. We acknowledge that there have been a lot of changes in the last 15 years but we also recognise that there are a number of uncertainties in the system. Putting to one side the tax issues, in terms of the tax changes with the low income tax rate through the GST changes and so forth, at the moment there are changes in terms of the superannuation environment, whether it be fund choice, whether it be member investment choice or whether it be changes to the superannuation structure. There is a growing retailisation or commoditisation of superannuation. I think there is a little bit of uncertainty about where super fits in. I acknowledge that we have a three pillar system. We are not advocating that be changed. It is a solid system. I suggest you need to add the fourth pillar—that is, an encouragement for part-time employment for people in their 60s and 70s—for a broader, more robust system.

There are issues and I have touched on a couple of them. If you are going to look at people in their 60s and 70s and how we bring them into the super system and make it more flexible, it starts to raise questions of what we want out of the super system: how much is enough? Should there be tax incentives at particular angles or should we limit issues? It is really raising the question: where are we going in terms of retirement income policy? Let us make that very clear: what are the expectations of members, of employers, of governments and of regulators? I think there is a fair bit of fuzziness in all of that. As the SG system has matured over the last 10 years, let us say, we have now got to a position where there is an element of maturity, but where do we go from here?

**CHAIR**—Tax deductions have been seen as a carrot that Australians respond to very readily. In any reform, people are wanting a massive move to simplicity. It has been suggested that perhaps we should allow deductibility of contributions as far as members are concerned—members in the widest context. You would maybe have to have a caveat in terms of an age related limitation and taxation at the full marginal rates at the end. Would that involve a lot of loss of revenue? How does that appeal to you, because that would be a very simple process, wouldn't it?

**Dr Knox**—I think moving the tax position from the point of contributions to the point of benefits, which I think is part of your question, has a lot of attraction to it in terms of equity, because at the moment the super tax system cannot really be considered as equitable because we are taxing people along the way—we are not taxing them at the end when we know how much they have got. In terms of equity, taxing at the end has an advantage. Another advantage is that it generates revenue when we are going to need it with an ageing population. We are going to need more revenue in 10, 20, 30 years time. This gives us a source of revenue.

However, as you have hinted at, there would be loss of revenue at the point of change, because you would be forgoing tax on contributions. My view is that you could simplify the tax on contributions at the front end, perhaps even remove it, and move it to the back end, either in

a gradual approach over a period of five years or in a one-off approach. The institute has done some work in looking at a big bang approach, if you like—drawing a line in the sand and saying, ‘Let’s start again. Let’s try and quantify the tax owed by each individual now and let’s jump a hurdle into a new system.’

Perhaps another thing I would say on the taxation of contributions is that as the labour market changes and we have more part-time workers and casualisation, people in and out of the work force for family reasons or other reasons, we actually need the whole thing to become more friendly and looking at it as a one year snapshot may be the wrong way of looking at it. We are encouraging people to save money for 20, 30, 40 years. If I am out of the work force for five years because of family responsibilities and I have the capacity to make that up over the next five years, why shouldn’t I be encouraged to do so? There may be an opportunity to, in a tax system, not just look at it as a one-year snapshot but broaden it into a little bit more of a lifetime approach, with appropriate caps.

**Senator ALLISON**—I am interested in pursuing item (c) in your executive summary, which says:

...APRA should consider:

(c) making maximum use of its powers to influence the development of international regulatory regimes...

In this time when globalisation and world economic forums are with us, can you expand on what you think the need is in Australia to make sure we influence the direction of those regimes.

**Dr Knox**—I think, in a global world, it is much better that you have consistency in prudential regulation in the developed economies, otherwise you are going to start to get arbitrage. In that sense, my understanding is that APRA is playing its role in groups such as the International Association of Insurance Supervisors and through the Basle Committee on Banking Supervision where APRA is making input and is influencing the development of standards of models. We want to make sure that what we develop in Australia is consistent with the best world practice. I do not know whether Christa would want to add to that from a general insurance perspective.

**Ms Marjoribanks**—From a general insurance perspective, in the future you might well buy your motor insurance policy over the Net and there will be an increasing need for global regulation, so that when you are purchasing that insurance over the Net there is a sort of global understanding of what is sitting behind that policy and the amount of capital. In that sense, it is very important that Australia is able to be consistent in terms of the stringency of what is required from a regulatory perspective. Otherwise they risk becoming uncompetitive in that global market.

**Senator ALLISON**—So your argument is that we should keep pace rather than trying to influence?

**Ms Marjoribanks**—I think it is a combination of keeping pace and also participating in the development of best practice globally.

**Senator ALLISON**—Where do we look to for best practice?

**Ms Marjoribanks**—I think best practice is a moving target. Australia certainly has probably a greater sophistication in the financial services sector than is indicated by its size on the global map because it is quite a sophisticated market. I think that, despite our size, we have certain elements of best practice here in Australia that we can use as examples for the rest of the world. We can also look to other countries and what they are doing. We can look at our system, take what we think is best from our system and use that to influence what happens globally.

**Dr Knox**—Perhaps I can add to that. As you are aware, APRA is what we might call an ‘integrated regulator’: the banks, insurance companies and the superannuation funds are under the one regulator. One of the things that APRA tries to do is regulate like risks in a like manner. So if there is a risk in the banking sector and in the insurance sector, the amount of capital needed to protect that risk should be similar. We have gone down an integrated regulator route, which is considered now to be world best practice. A number of other countries have gone down that path—Canada, UK, some Scandinavian countries and Korea, I think. That is one example of how our regulatory framework is considered to be up there with the best of them. Therefore, we are developing practices in terms of prudential regulation—particularly in the insurance and banking sectors—that are also world best practice. If you then extend that to our links into Asia and other export areas, it helps the world perception of Australia as a financial services market because we have a very good regulatory system.

**Senator ALLISON**—That leads me to the other term of reference for the inquiry, which you do not address in your submission: the prospects of Australia being a global financial centre or a centre in this region.

**Dr Knox**—I think those prospects exist. Only this morning we were talking to someone—if I may sidetrack for a moment—about the Institute of Actuaries of Australia. Our actuarial qualification in Australia is now recognised worldwide and is on par with that of the Americans and the British—we have signed mutual recognition agreements along those lines. That means that through Asia—whether it be Singapore, Malaysia, Thailand or Hong Kong—our Australian qualification is recognised as being in the leading league of actuarial qualifications. That is a great bonus in terms of exporting our professional services. I have deviated from your question a little, but I wanted to give that example.

Strong professional services and a strong regulatory system in this country are part of the framework that is necessary for a global financial centre. You clearly must do other things in terms of infrastructure, getting into markets and so forth, but there are some other elements that you must put in place first. I think we saw some of the benefits of that during the Asian financial crisis when we benefited from having a good banking regulatory system.

**Senator ALLISON**—On that point, is there any room for criticism of the different roles that ASIC and APRA play in terms of regulatory environments? The committee has received quite a bit of criticism of the defining of those roles and their performance when there are grey areas. Do you share those concerns?

**Dr Knox**—I think it is fair to say that those roles are evolving. The process started only two years ago and there was always going to be a period of bedding down between those roles and a

review of how they work together. I think the two bodies do work together, but that needs to be finetuned in some areas. Christa do you want to comment on that? You are probably closer to it than I am in some ways.

**Ms Marjoribanks**—No. I think what you have said is right.

**Senator SHERRY**—Dr Knox, a number of ministers have commented recently about reviewing superannuation. That has not come to anything so far. Do you think this is an appropriate time for that—I am talking about not just tax issues but some of the matters you referred to earlier? If so, why do you think it is an appropriate time?

**Dr Knox**—We have called for a full review. We believe it is an appropriate time for several reasons, one of which is that we have a new tax system in place. From an individual's perspective, the income tax rates have changed but super tax rates have not changed, so that the comparison has altered. We have the business tax review going through the system. Admittedly, that is not yet complete, but we have a fair idea of where that is going. We have the SG system that is now moving towards its maturity, at least in its stage one, the current stage of nine per cent. Should that go another stage? I do not want to comment on that, I just want to raise it as a question. If it does go another stage, in which direction should it go? There have been questions raised with an ageing population in terms of health costs or other costs associated with an ageing population.

For all those reasons, and for the fact that there are issues in terms of the regulation through SIS or other parts of super, it is appropriate for everybody to put their cards on the table and to have a good look at this in a public forum. We are not suggesting a behind closed doors operation, but a public forum that might take 12 months or longer, and hopefully end up with a bipartisan approach because this issue is so important that you do not want it to become a political football.

That is what we advocate. We acknowledge the difficulties in pursuing a bipartisan approach, but we have gone some way towards that in recent years with the commitment of all parties to the SG, to a nine per cent commitment, to elements of prudential regulation and so forth. We are suggesting that the review should not be a half-baked review, but a full comprehensive one.

**Senator SHERRY**—You mentioned the ageing population issue as one of the factors. Do you see this as a major public policy debate, or discussion?

**Dr Knox**—Yes. The ageing population has all sorts of consequences, not only in terms of cost of pension and health, but we have labour market issues in terms of how we make it more appropriate for people to use their human capital, if you like, the experience, the skills, that people in their 60s and 70s have got. We have not even touched on genetics yet. The future of genetics and where that is going is going to have an impact on population development, on longevity, on the needs for retirement income, health costs and so forth.

So when I talk about a major review I am talking about a significant one that tries to cover the full spectrum. We suggest you would need a panel of diverse experts which has the capacity to bring in, to synthesise, everybody's submissions, to explore the issues and, subsequently, to issue a report.

**Senator CONROY**—I want to touch on the genetics question. I understand my office has spoken recently with the institute about this. Could you explain to me that the concept of a risk pool?

**Dr Knox**—In a normal insurance arrangement, the pricing is based on the risks you take on. A very simple example would be life insurance where males or females will have different prices. Smokers or non-smokers would have different prices. By age there will be different prices. None of those we see any problems with, we take that as a given.

**Senator CONROY**—But there is a large enough pool.

**Dr Knox**—You price according to the risks that you are aware of and then you bring them to the pool, which is sufficiently large as well, but the important thing is that the price that the consumer has paid has been based on the expected risk that that—

**Senator CONROY**—Of the average pool?

**Dr Knox**—Of the average, taking into account the characteristics of that individual, whether they be male or female, their age, their smoking, et cetera. What that is saying is that the insurance company is able to price according to the risks that are known about that person, gender, age, et cetera.

If we are willing to price ignoring some of those risks, then we move from a normal insurance pool towards what I will call a social insurance pool. The example that we have had recently is health insurance, where, up until recently, the price has been the same for everybody unrelated to age. Health insurance has moved a little back along the continuum. We still do not price based on our health condition, only based on our age, although there are some pre-existing conditions.

I can perhaps predict a question with regard to the genetics issue. If I have some information about my genetics which I know and the insurance company is not aware of, then I am aware of my susceptibility to a risk but they are not aware of it and therefore they cannot price according to that risk. In some cases, if it is a very small number of the total pool, it may be relatively insignificant, but it means that the insurance company is not pricing according to the risks that are present. And, in the end, what that means is other policy holders are paying for that extra risk.

**Senator CONROY**—Yes, that is the point of a risk pool—it is spread across a pool.

**Dr Knox**—It is spread across the pool—

**Senator CONROY**—If insurance is simply about pricing everybody at their own risk, what is the point of having a pool? If you take the risky bits out of a pool, it really does not seem to have much point. I accept you can calculate it, but the whole point of a pool is so that risk is spread and shared.

**Dr Knox**—You are correct that risk is shared in the pool. We can never predict exactly. Even though because I am male, not female, I am more likely to die, some females of my age will die

before me. We cannot be specific in the individual. What we can do, though, is price according to the most likely event or the expected—

**Senator CONROY**—That is based on an average.

**Dr Knox**—It is based on an average position.

**Senator CONROY**—To me, this argument seems to be about finding and identifying the most risky and removing them from the pool. And this is on a predisposition; this is not even on an existing ailment.

**Dr Knox**—In terms of genetics, our recent press release highlighted the distinction I have just made between voluntary, risk based insurance and social insurance. What we have called for is a forum on genetics and insurance, so everybody can understand the issues more clearly and the consequences of going down one route or the other route. The Institute of Actuaries is not suggesting—

**Senator CONROY**—I am not suggesting that you are. It is more that the underlying principles of risk, which is where your expertise is—

**Dr Knox**—Yes.

**Senator CONROY**—mean that you can say, ‘If you go down that path, this is how it will happen, and if you go down—’ but I am trying to get down to the concept that a risk pool is there to spread risk and that if you remove people who are the risky ones then there are actually two effects. The first is that the people who actually need it will not be able to afford it because the premiums will be prohibitive. The whole point is that this is why you have a community pool—to spread it, because individuals cannot afford to be charged at their actual risk.

**Dr Knox**—Let me take an example—and forget genetics. If somebody comes in at the moment—

**Senator CONROY**—It is just that user pays defeats a risk pool.

**Dr Knox**—With user pays, the pricing is linked to the likely risk of the individual. I will take the example of a person who is a smoker, male, overweight and has a couple of ailments. At the moment they are charged more than a person of the same age, and even the same gender, because they have a higher likelihood of dying earlier.

**Senator CONROY**—Most of those you described, other than the gender, are choice. They are things you can change yourself. You can do nothing about your genetic code.

**Dr Knox**—Correct. You are quite right, Senator—

**Senator SHERRY**—So far!

**Dr Knox**—So far.

**Senator CONROY**—*Gattaca* is approaching, but we are still a few years away from *Gattaca*.

**Dr Knox**—I agree and we made the point that genetics is different from the examples I have given you. The point that we did want to make though was that if you could not rate price on the known genetic make-up, then you will have an outcome that moves you down the continuum towards a little bit more of a social insurance example. We are not saying that is right or wrong; all we are saying is that it is a likely outcome. I also want to add that in terms of genetic testing, some genetic tests are more predictive than others and I do not want to bring them all together in the one example. This is a developing and evolving issue and we are getting more and more information virtually every week.

**Senator CONROY**—My question to you is more about the theory behind having a pool and if you segment it enough; if people are made to pay because of what their own actual risk is, there is no point in having an insurance pool.

**Ms Ferguson**—They will self-insure, you mean?

**Senator CONROY**—You make the decision, ‘No, I can’t afford to pay for life insurance, because I’ve got a genetic code that says I’m going to get Huntington’s disease,’ which is the one I think we have talked to you about, ‘in five years time.’ Whereas, if you are very healthy and your genetic code says you are fine, why would you bother anyway?

**Ms Marjoribanks**—What you are getting at is quite right. If you took all of the uncertainty out of when people were going to die, then each person in this room would have a date and it would become part of your personal record as to when you were actually going to die, fall ill or whatever it might be. Maybe in 50 years time medical science will have evolved to the stage where that might be the case.

**Senator CONROY**—Hopefully not.

**Dr Knox**—We still want some uncertainty.

**Ms Marjoribanks**—I think it is unlikely.

**Senator CONROY**—There is still risk aversion and you can still get knocked over on the road.

**Ms Marjoribanks**—That is right, yes.

**Senator CONROY**—Therefore, you cannot. But they are random events and the pool affects more than just random events, though, and that is what I am really concerned about.

**Ms Marjoribanks**—That is right, and if you look at, say, 50 years ago, the evolution over the last 50 years has been that there has been a greater ability to identify risk factors and to, I guess, allocate people to the correct pool for their risk, and this is really just another factor. It is information that is starting to become available and it is very complex in terms of insurance. It

is a social issue as to whether you allow that to be an insurance rating factor, obviously. One of the problems is that once the information is out there, you cannot put it back.

**Senator CONROY**—Doctor-patient privacy is always a good issue—that is to come.

**Ms Marjoribanks**—That is right, exactly. I guess what I am saying is the individual then has that knowledge.

**Senator CONROY**—They have knowledge of a predisposition; they do not have knowledge of an ailment.

**Ms Marjoribanks**—No, that is right.

**Senator CONROY**—But these are not issues for you. I readily accept that.

**Ms Marjoribanks**—That is right. What you get in an insurance context is antiselection. People can choose to insure or not insure based on the information that they have about themselves, and so that can affect, I guess, the prices of insurance and, going forward, it is very important from a technical viewpoint to be able to assess the risk of a pool, however you define that pool, so that you can get the prices correct.

**Senator CONROY**—I guess where I get to here is, yes, you can segment the pools and each pool gets a different price, but the larger the pool, the lower the average cost, if it was just over genetics. By having the genetic pools created, some people are going to pay less, obviously. Some are going to pay a lot more.

**Dr Knox**—Yes. You are talking about subpools. That is absolutely right, but it is also important to realise that although you have got these subpools, and whether they are pricing for genetics, or smoking, or some other action, they are part of a bigger pool within the insurance company. The insurance company is looking at its total portfolio, if you like—all its insurance policies. Whilst we might price for genetics here or smoking status there—

**Senator CONROY**—That is like the argument where you are 55 or 60—they are going to charge you a prohibitive amount and if you have got a genetic code that says you are going to get some fatal disease when you are 35, you are going to be charged a prohibitive amount.

**Dr Knox**—At the moment—

**Senator CONROY**—Even if it never actually happens, you are still going to be charged a prohibitive amount, because they do not want to insure people who are going to die. This is a game: it is about you betting me that I am not going to die, me betting you that I am going to die.

**Dr Knox**—As you said, there is a predilection, if you like, or a suggestion, that there is a high probability if you have this gene make-up: I have a higher probability of suffering from it than you do if you do not have it. That does not guarantee I will die before you, because of other random events. As Christa has said, over the last 30 or 40 years in insurance, we have actually

started to identify other risks, not only in life insurance, but in motor vehicle insurance and other insurance. We have got better, if you like, at identifying the risks, because the data has got better.

**Senator CONROY**—That is what I am worried about. I am worried about it getting better and segmenting. That is what I am actually worried about.

**Dr Knox**—I accept that, but people are now saying, ‘If you have got this information that this postcode is safer to live in than that postcode because there are less burglaries, then I want a cheaper insurance policy because I live in a safer suburb.’ You have got to look at it the other way round.

**Senator CONROY**—That is the way the ACCC are looking at it.

**Dr Knox**—What we are saying is that, if the information is available from the consumer’s perspective and the insurance company is or is not allowed to act in the case of that, there will be different outcomes. We are not advocating—

**Senator CONROY**—I appreciate you are not advocating anything. I am really just exploring the issues.

**Dr Knox**—It is a really important issue and we are not trying to shy away from it, and that is exactly why we have called for a forum, because we believe that there needs to be confidence in the community. We are very interested in developing something similar to what they have in the UK, where there is a forum of genetics in insurance, where experts from the consumer movement, ethicists, geneticists and actuaries can come together, talk around the issues, and advise the government accordingly.

**Senator CONROY**—The UK have adopted a different system from what IFSA have adopted here, haven’t they? They seem to have introduced a £100,000 rule. So there is almost a social pool attached to a more risk related pool. Whereas IFSA here in Australia is advocating essentially—

**Dr Knox**—Zero.

**Senator CONROY**—that, if you know it, you have to tell it.

**Dr Knox**—That is my understanding.

**Senator CONROY**—Which is essentially a segmented pool rather than one pool on top of itself.

**Dr Knox**—My understanding is that the forum in the UK has adopted the £100,000 for mortgage policies. I am not sure whether it is a recommendation or an adoption at the moment, but there has been this discussion. I guess in our currency, that would be \$250,000 for the same.

**Senator CONROY**—Equally, insurance companies are entitled to protect themselves against somebody who maybe knows they have a genetic code and they are going to die at 35 and wants to take out \$10 million worth of insurance. Equally, people are entitled to have some sort of preventative mechanism for that exploitation in reverse.

**Dr Knox**—Sure. That is a good issue.

**CHAIR**—Would you like to comment on the penalty regime at the present time. It has been alleged by some that there are excessive penalties and there is no discretion allowed in at least five of the six penalty regimes outlined in the pact—up to twice the superannuation guarantee charge, not deductible et cetera?

**Dr Knox**—I am not an expert on that.

**Ms Ferguson**—I noted that the institute put in a submission to this committee about the issue of the penalties changing in the SIS Act. It was going to strict liability. Is that the issue you are raising?

**CHAIR**—No, it is the—

**Dr Knox**—Size of penalties?

**CHAIR**—fact that the superannuation guarantee charge is not deductible. There are other penalties which can be twice the superannuation guarantee charge, and there is no discretion at all there.

**Dr Knox**—This is, in fact, about enforcement if people do not pay the SG.

**CHAIR**—That is right.

**Dr Knox**—Can we take that on notice and get back to you?

**CHAIR**—Okay. How do you view a simple tribunal system to investigate member claims of unpaid contributions? At the moment, people have got to go basically through the tax office and there are questions of privacy and there is a lot of dissatisfaction—even if a voucher is handed over—as to whether it is the right amount, because there is no reconciliation, there are no dates of payment et cetera on that. Would you like to comment on that?

**Dr Knox**—At face value, I would have thought that if there are unpaid SG contributions for particular members then you would want a fairly simple system for the member to be able to pursue the unpaid contributions, notwithstanding the legal issues that might be surrounding it. Can we get back to you on that one? A tribunal at first instance appears perhaps a simpler way of proceeding, but I would not want to—

**CHAIR**—There is also a lack of flexibility. For example, if an employer discovers there has been a shortfall in terms of meeting the superannuation guarantee obligations, that shortfall

must go through the sort of voucher system. There is absolutely no discretion there. Would you like to comment on that, or get a simpler and better system?

**Dr Knox**—If there was some non-payment I would have thought that some discretion would make sense. I will take that trifecta of questions on notice and get back to you.

**CHAIR**—Can you comment also on the apparent lack of monitoring by the ATO of an employer's superannuation guarantee performance?

**Dr Knox**—We will get back to you on that.

**CHAIR**—You might also like to comment on the difficulties that we have when an employee within a group transfers from overseas, that if the payment is made to an overseas fund it is not deductible, it can give rise to fringe benefits situations, and also its unavailability until you turn 55.

**Dr Knox**—I know there are some real issues.

**CHAIR**—We would like your views there.

**Dr Knox**—Sure.

**CHAIR**—Thank you very much.

**Dr Knox**—In summing up, thank you very much for your questions. We found them stimulating, as always. We will get back to you on those comments. Thank you for your time and if any of the senators would like to contact us, please feel free to do so.

**CHAIR**—Thanks very much for the invitation.

[2.17 p.m.]

**GRABOSKY, Dr Peter Nils, Director of Research, Australian Institute of Criminology**

**GRAYCAR, Dr Adam, Director, Australian Institute of Criminology**

**CHAIR**—Welcome. I invite you to address the committee on those matters that you feel are of relevance to our terms of reference.

**Dr Graycar**—Thanks very much for inviting us today. The Australian Institute of Criminology, as you are no doubt aware, is a federal government agency. We are Australia's national centre for the analysis and dissemination of criminological data and information. Superannuation is not our core business, crime is. The institute aims to be responsive to the needs of government and the community with respect to policy in the fields of justice, prevention and the control of crime in a whole range of areas. As such, we are here today to talk about some aspects of protecting superannuation from criminal exploitation.

We ran a conference four years ago. Senator Watson spoke at that conference and made the very significant and profound point that underpins a whole lot of criminological activity, that fraud is a combination of opportunity and motivation. In the area of superannuation there is certainly a considerable amount of opportunity and motivation.

Within the institute itself we have four research groups, the one headed by Dr Grabosky is devoted to the study of sophisticated crime. Within that research group we look at things like fraud, regulation, computer crime and a whole range of activities. I have a brochure here that describes that in a bit more detail.

We also have a group that looks at public policy issues. Within that public policy area we have a couple of people working on crime against older people. When we start to combine issues of fraud, issues of opportunity and issues of crime against older people, the potential of superannuation to criminal exploitation becomes very significant. We have not done any empirical work on the area. We could not tell you today who is doing the scams or where they are or if, in fact, they are taking place, but we see it as a very significant potential research area.

If we are talking about protecting superannuation against criminal exploitation, essentially there are three areas to look at it, as in fraud generally, or in most crime. The first of them is to try to reduce the supply of motivated offenders, the second one is to protect and educate suitable targets and the third one is to limit opportunities by making crime more difficult to commit.

If you are trying to protect a newsagency against burglaries, there is a pretty clear strategy that you can follow. You can warn the person to keep the property reasonably secure and you can put in alarms. You can try to get locals to understand that robbing the local newsagency is not a good way to go. When you are dealing with superannuation, however, it is a very different sort of issue. First of all, the offender is usually motivated by greed on a major scale and it is different from any other sort of predatory criminal activities. That is a very hard part of the equation.

Protecting and educating targets is a very significant area of activity because clearly we are moving into an area where the amount of superannuation money invested is very large, the number of funds is very large and people are not well aware of where their money is or how it has got there. So there is a whole strategic area in developing education and protection. In the third area of limiting opportunities by making crimes more difficult to commit, there is a range of regulatory activities that I am sure that you are aware of.

Both Peter and I often use the old saying of a famous American bank robber, Willie Sutton, who was once asked why he robbed banks. He said, 'I rob banks because that's where the money is.' Today, if you rob a bank, you get a bunch of paper or a bit of plastic. The money is not always there physically. Today, there is an enormous amount of money in retirement investments and we are looking at it as a future set of crime areas. There are very great opportunities. We know from our conference back in 1996—and it was shortly after the British Maxwell case—that the reported rate of criminal exploitation of superannuation in Australia was very small. There was not very much of it, but it still ran into hundreds of millions of dollars. In the scale of the amount available, it was negligible, but nevertheless, any good crime prevention approach will try and limit opportunities; it will try and make the crimes harder to commit.

That is what we at the Australian Institute for Criminology would like to work on. We have not got the answers now because we have not done the work. We are here today really to ask you what you see as the issues and how we might be able to respond to them. How can we develop the protective infrastructures from a criminological point of view and work in partnership with others who have other regulatory responsibilities to make sure that we can limit any potential criminal activity? For people who have saved for a lifetime, if something goes wrong, the devastation is monumental. They cannot rebuild; they do not have opportunities to get it all together again. The losses are both emotional and financial. There are all sorts of shattering events.

I have a few things I might table with regard to what we have done in addition to that conference. We do send all senators a copy of our trends and issues papers. We did one on superannuation crime a few years ago, but in the last 12 months we have done one on fraud and financial abuse of older people. We have also done one on substitute decision-making and older people, which is about enduring power of attorney. I have spare copies of all of those if anybody would like them. I am happy to table this bunch of papers now.

**CHAIR**—Is it the wish of the committee that the documents be tabled? There being no objection, it is so ordered.

**Dr Graycar**—And there are brochures on the institute, if anybody wants them. Basically, I thought I might outline some of the things that we see as significant from a criminological point of view. But, before doing that, I might get some response from you as to what you see as being the issues and how the Australian Institute of Criminology, which is an agency whose prime interest is not in superannuation but which is clearly interested in the issue, can assist you in your work.

**CHAIR**—Thank you very much. One issue of concern is: if there is a major loss, is there provision under the act for all superannuation funds to be levied in order to compensate the members for that loss?

**Senator SHERRY**—That is theft and fraud loss.

**CHAIR**—In the case of smaller funds, do you think there is adequate provision, for example, for compensation to be made where perhaps there might be 20, 30, 100 or 200 people as opposed to 10,000?

**Dr Graycar**—I do not know the answer to that question, because the industry sees itself as spreading risk. One of the significant things that we noted in the earlier work that we did was that the vast bulk of money is in a very small number of funds. There are many hundreds of thousands of funds, but the vast bulk of money—you would know the figures—is held by a very small number of funds. So the risk assessment of dealing with loss, one would assume, would be taken not by a proportion of the funds but in proportion to the holdings that they have. That is the way I would see it, but this is, I suppose, not terribly dissimilar to the way in which other insurance insures against burglary, loss or whatever—all the premium holders, all the people who hold policies, end up paying something towards it and I suppose this is a way of spreading the risk.

**Dr Grabosky**—There is a slight difference there in that, if superannuation funds were required to insure with an insurance company rather than with their industry, presumably that insurance company would be in a position to exercise a degree of surveillance and control over the activities, whereas the competitors of a superannuation fund are not in a position to dictate certain prudential practices or whatever.

**CHAIR**—Would you recommend outside insurance, and what sort of costs would a fund be looking for?

**Dr Grabosky**—I must confess I have not give a lot of thought to that particular issue, but it seems to me that, by mobilising the vigilance and surveillance capacity of an external institution like an insurer, that would help prevent or minimise the risk of fraud by the principals of a superannuation fund.

**CHAIR**—To date, most of the problems that APRA has come across and where ASIC is involved in prosecution do not appear to be fraud as such. Do you think the law is perhaps a little bit weak there in that most of the difficulties apply in the smaller type funds—for example, aggressive secretaries or chairs, managers taking it upon themselves to do certain things which might be outside the members' best interests?

**Dr Graycar**—To a very large extent, the issue depends on how well management of both large and small organisations deal with quality of their work and their best practice. At the conference that you attended, Senator, what came across very strongly was not that there was a great deal of criminal fraud but that there was a lot of incompetence, there was a lot of ignorance in superannuation funds. There were people at the margin of taking risks that were not, on the face of it, fraudulent but could have ended up as losses. The key thing that came through was to try and pick out a set of early warning indicators, not only for fraud but to make

sure that funds had pretty tight standards of accountability, of safeguarding, of recording, of authorisation. These were real, important, front-line activities. Then there were a range of second-line activities: reconciliation and verification, review and monitoring.

There was also some discussion about the sorts of signals that indicated that something might be going wrong—domineering trustees or domineering senior management. But there is not always a mechanism to be able to say, ‘Hey look, you’re being too dominant, you’re being too pushy.’ Clearly, when you are talking of a couple of hundred thousand superannuation funds, there is not that level of scrutiny and nobody would want a regulatory authority to be sticking its nose in at that level of detail. I suppose that this is always an issue in any form of crime prevention. In most cases, things do not go wrong, but at least have the early warning signals for when they do go wrong. One of the things that we could look at is a crime and loss prevention strategy with a set of early warning signals that somehow can be triggered early on. In a lot of cases, it is ignorance and incompetence rather than malicious theft that causes problems.

**CHAIR**—In the industry, safeguards are essentially based on the division of responsibilities—you have got trustees, investment managers, custodians and so on, each with clearly defined roles and responsibilities. Ultimately, it comes back to the trustees who are liable. Are you happy about the operation of the trustee system?

**Dr Graycar**—I do not know enough about it to be able to answer that question.

**Senator SHERRY**—We recently had a piece of legislation before us—APRA were one of those who gave evidence and there were differing views—to tighten up some of the penalties relating to trustees who have a guardianship of superannuation funds in this country. I asked APRA to give us a document—I do not think that what they gave us was satisfactory initially—outlining where the problems are, as the regulator, and to identify, on an annual basis, the types of funds, the amounts of moneys involved, the numbers of members involved, where there have been problems. This is not just in respect of fraud but also in respect of bad management, poor management, that was serious in the sense that you would have to do something about it. You might like to liaise with APRA. It would be very useful if your organisation did some analysis of what has been happening in recent years to identify areas of theft and fraud particularly.

What struck me in looking at the latest APRA document was that I could not see an example of a large fund—and by ‘large’ I mean more than 200 or 300 members. It tended to be in quite small funds or middle ranging funds—but that was just a suggestion. The latest figures available from APRA show there is \$450-odd billion in superannuation now, I think it is 60-odd per cent of gross domestic product; we are dealing with remarkably large sums of money. There is a significant debate in the country at present—certainly here in the parliament and amongst players of the superannuation industry—about the structure of superannuation and how people should join superannuation funds. At the moment, many people are in a particular fund and they are bound to that fund by their workplace. There is a proposal to deregulate that—some people use the term ‘choice’.

I would be interested in you having a look at the implications of that from a theft/fraud point of view. You may not know enough about it to make any comments here today. It seems to me that where the individuals who we are effectively asking to make much more sophisticated

financial decisions are not adequately educated or trained to make those judgments, there is a greater capacity for theft and fraud. You might have a look at that particular proposal; the committee secretariat can provide you with some information about what is planned. We have not had any material or evidence from the point of view of potential for theft and fraud as a result of this so-called choice debate.

**Dr Graycar**—It is an interesting proposition; we would be very interested to have a look at it. Until we assemble information, it is always difficult to identify the trends. Right now, in a different area, we have one of our senior research analysts doing a project on fraud in general, with the various state police. He has got access to the actual fraud files, and he is doing a whole range of case studies very laboriously, to try and identify things like what the circumstances were, what went wrong, how it happened, whether there were loopholes, what the size was, whether it was covered up, whether anybody found out, how it was investigated, what the outcome was, et cetera.

The only way to do it in areas like fraud is to go case by case, because every story is different; every situation has its own different complexity. Given that Dr Russell Smith is doing this work at the moment—he is the one who did that other paper on fraud against older people—it is something that we would be very keen to talk to APRA about, if we could get access to a number of case records of situations that have gone wrong. We would essentially try and identify the criminological component of it, so that we could look at prevention mechanisms to identify whether there are generalisable issues or whether there were specific issues in that case. The most important part of all of our work is crime prevention, to make the crimes harder to commit and to reduce the supply of offenders.

**Senator SHERRY**—The level of cases so far, and the seriousness of cases, I think has been generally less when people are within a superannuation fund; when they are employed. What concerns me—and I have had a couple of individuals come to me about this particular issue—is when they cease work and leave the fund, and receive a lump sum. They then reinvest the lump sum in some particular product, particularly the elderly, who are more vulnerable. People are receiving a significant lump sum—and to some people \$20,000 is significant; to others it is \$200,000. They take the lump sum, and theft and fraud occurs in terms of the way in which that money is invested. It has left the superannuation system, in other words.

It seems to me that that is a significant area in which I seem to be getting more complaints and concern. It is not superannuation money anymore. It goes into the hands of some sort of adviser who then, in some cases, does not invest it at all; they spend it, steal it or whatever. Again, it might be worth while having a look at some research about what people do with superannuation lump sums when they leave a system, which I think is pretty well protected, and then, having left the system, their level of vulnerability and the way in which we could improve safeguards to protect that lump sum when they on-invest it, if you like.

**Dr Graycar**—That is a very important issue. Earlier this year the AIC ran a conference called ‘Crime by Professionals’. In that, we looked at the range of areas, mostly in health and financial services, where professionals gave bad advice or were complicit in illegal activities. There are some pretty significant issues here that relate both to regulation and to codes of practice. It becomes very hard when one moves from a protected environment to a non-protected environment. The analogy, in a way, is: somebody withdraws some money from the

bank and if they get mugged inside the bank, the bank will take responsibility; if they are outside the door, the bank might take responsibility; if they are 50 or 100 metres down the street, it becomes very murky. It is a very important issue, because it follows that very basic theme that Senator Watson pointed out: crime follows opportunity. If somebody has a lump sum of \$20, \$200 or whatever number of dollars they see as very significant and people are eyeing it, that is pretty important. I have come across cases in a previous job that I worked in where unethical financial advisers would churn money, and they would get people to move their investments all the time so they would be taking a cut all the time. Although one could say it is not illegal, the nature of the movement, the sort of investment—they were tying up the money of 70-year-old people for long periods of time, et cetera—is very much a regulatory issue for that industry. We would be very keen to look at the criminal opportunities that do occur at the margins.

**Senator SHERRY**—I will finish on this point. The source of the money that people have when they retire, up to date anyway for the vast majority of people, has not been significant in terms of superannuation. But, with compulsory superannuation and growing account balances, the proportion of the funds they have available when they get that lump sum on retirement will increasingly—and I think ultimately—be dominated by the moneys that are sourced from the superannuation saving. As I say, I have had a number of quite disturbing cases. I think you pointed out that, if you are elderly, there is no opportunity to rebuild, and it is quite devastating. There is a public policy issue here too. Effectively, compulsory private sector superannuation is there to build up retirement savings and reduce dependency long term on the traditional pension. A pension is absolutely safe; the government guarantees it. But when you transfer part of that to the private sector, there is an ethical issue about protecting people beyond what would normally be expected, given that it is their retirement income.

**Dr Graycar**—It is an important piece of work in mapping out the various risk areas and the areas in which there could be danger but at the same time not wanting to frighten people, because, as you say, the track record is generally pretty good. There are not large numbers of cases of people being ripped off. The opportunity may be there in the future, and building that set of protective measures is very important. While not being alarmist, at the same time it is making sure we can have that balance. It is an area of work the Australian Institute of Criminology is certainly very interested in.

**Senator ALLISON**—If I could go to Professor Freiberg's issues paper No. 56, which must have been written in 1996: is it possible to run through the problems that were identified back in 1994 to see whether those problems are still with us? They include:

improper registration and use of fund assets;

collusion between trustees and fund managers improperly to divert assets;

collusion between trustees and managers in overcharging fees or paying unauthorised expenses;

falsification of records;

misappropriation of assets;

improper or bogus loans to interested parties;

failure to pay benefits.

Is that pretty well still the list?

**Dr Graycar**—Yes. While there might have been some structural changes, I think what we are talking about when people behave in a criminal manner and collude, falsify or misappropriate—they have been doing that for centuries or millennia in terms of whatever activity is around—is that if we start to take each of these individually, we might be able to identify some protective measures, and these were identified at that time. I do not know whether Dr Grabosky has a comment on that.

**Dr Grabosky**—The question that Senator Allison raised could be answered by the kind of postmortem analysis of the problems that recur under the auspices of the regulatory authority. The postmortem analysis would want to identify whether these particular problems are recurring or whether they are patterns that are changing over time.

**Dr Graycar**—And we do not know how widespread they are. One or two cases could receive a lot of the publicity and have a very devastating effect. This is not to say that it happens all the time but going through the postmortem, a set of case records, would at least give us some understanding of the trend over time.

**Senator ALLISON**—I know you said you are not properly across the question of trustees and the arrangements for them but, in a more general sense, this committee has to deal on a regular basis with questions about whether trustees are sufficiently educated and what kind of person a trustee is. I think we are about to agree on legislation in the Senate which will move the trustees into probably a more professional realm, with strict liability penalties for instance. The advice we are given from industry and corporate funds is that you will lose a lot of the ordinary trustees—and I am a bit uncertain as to who will take their place. If you professionalise that group and ask it to be more qualified and educated in this realm, is it creating greater or less risk? In other words, if I were serious about committing a crime in superannuation, how would I try to enter the field to put myself in a strong position to be able to perpetrate crime and fraud? Would it be through the trustee system? Is it financial advisers? Where are the risks that we should be trying to look at?

**Dr Grabosky**—That question could best be answered by systematic research based on the problems that have emerged. I have not concentrated my mind too closely on the question of how I would perpetrate a fraud but I suspect that I would seek to obtain the requisite qualifications and expertise that would place me well and truly in the professional camp. I would not approach it as an amateur.

**CHAIR**—I was just going to follow that. Would it be possible for the institute to do a study? We all recognise the benign approach to regulation, as said in this document, and we are aware of the industry's vulnerability to fraud. I know the cases are limited but it would be interesting to see whether a group such as yours could help identify some of the risks so we could seek to minimise them in some way.

**Dr Graycar**—We would certainly be keen to pick that up. I might follow on from Senator Allison's question, which I think is important. The issue of professionalism is hard, and I think it goes back to the changing nature of the industry, where a significant proportion of retirement

income now is in the private sector as opposed to the public sector. The risks are significant. While the amounts were small, it might have been okay to have a strong element of amateur management by people who were doing the right thing. As you move into more professionalisation there is a cost, but the risks are greater. While some professionals may wish to position themselves to rip off the system, we have always had the occasional crook solicitor, doctor, accountant or whatever.

The overwhelming majority of professionals are reasonably professional and do the job well. It would be very hard to assume that by professionalising it you would necessarily make the situation more vulnerable. But this is where—as Peter has been saying—doing the analysis of where the chinks are, looking at the regulatory arrangements, all of the accountability regimes, the early warning signals and so on, means a preventive mechanism can then be put into place. With greater professionalisation in the situation, the penalties can be so much more severe for anybody who breaches them.

**Senator ALLISON**—There is one problem with simply relying on case studies, and the statistics and information from what has happened in the past, and you hinted at this earlier: that probably since 1996 we are in a completely different environment in terms of the electronic transfer of moneys. I know people have been able to perpetrate fraud using the chequebook as well, but does this hamper us in trying to make sure that we have got detection systems in place that are adequate to pick up the fraud in time?

**Dr Graycar**—I will defer to Peter. Just before he starts, I would like to point out that a couple of years ago, he and Russell Smith wrote a book called *Crime in the Digital Age: Controlling Telecommunications and Cyberspace Illegalities*, which was a world first on electronic crime. Now, with Cambridge University Press, they have a manuscript called *Electronic Theft* that covers these very issues, which will be published in a few months time. So far be it from me to muscle in on your turf, Peter.

**Dr Grabosky**—I think that the situation involves conducting analysis that is based on contemporary cases rather than historical cases. In other words, to undertake the kinds of post-mortem analysis that we have been suggesting might be useful, we would focus on the most recent couple of years—well and truly in the digital age—as opposed to cases that might be of mere historical interest. One would then be able to identify the extent to which problems have emerged in an electronic environment, or whether the basic pathologies in question were more basic or low-tech, so to speak.

**Senator ALLISON**—Are you in a position to be able to say whether APRA's detection mechanisms and practice are likely to pick up on electronic crime?

**Dr Grabosky**—I am not able to pass judgment on APRA's regulatory performance, although it does, from what I understand, enjoy a very favourable worldwide reputation.

**CHAIR**—Given that most of the problems occur in the smaller funds whose auditors usually come from the smaller audit firms, do you think that the parliament should be more prescriptive in terms of its requirements of auditors?

**Dr Grabosky**—I should observe that this phenomenon of small players being the problem performers is not unique to this industry. It is fairly common across most forms of corporate crime and misconduct. Usually, it is the smallest players that do not command the knowledge, expertise or resources to invest in a compliance regime that will keep them on the right side, so to speak. To some extent, it is the small player that is going to require the most attention. How that attention is delivered—whether it be delivered through mechanisms of regulatory scrutiny or through the energies and resources of third parties, such as insurance companies, through liability insurance mechanisms—and how it can be leveraged in furtherance of achieving compliance are important questions.

**CHAIR**—The concept of an annual meeting of members is an interesting one. If that were made compulsory, maybe there could be some early warning signals given if it were a requirement to have meetings of members in a number of centres. Is that feasible in the same way that a company has its shareholders meeting? If the fund is an incorporated trustee, it has an annual meeting. The concept that I am looking at—it was raised by a university lecturer from Queensland—is annual meetings of members. I thought it had some attraction.

**Dr Graycar**—It might have an attraction if the flow of information on both sides is equal. I think that if there were an unequal flow of information, basically the members could get snowed if somebody wanted to snow them. If, on the other hand, it was a situation of having certain information sent out to members and members being able to comment on that information and having the questions thrown back rather than just a pretty bland balance sheet put out once a year, or if it was like a web site chat room where members could come back and forth asking questions and people following on from the questions, that, in a way, might be more useful—something interactive rather than a two-hour meeting where the people with all the information are on one side and people with not much information are on the other.

**CHAIR**—If it came back in printed form though, you would need a locked bag or something because if the perpetrator is likely to be the manager who opens the mail, the relevant ones might be sidetracked. That would be the problem, wouldn't it?

**Dr Graycar**—Yes. There are issues, generally, in terms of fraud detection—whether you have things like fraud hotlines where people can relay a concern to somebody other than the person who deals with the concern. Very often, people have to know what the problem is before they can raise the concern. What happens in the small number of cases where there have been problems in superannuation is that it seems to be too late when there is not a mechanism for quick redress. This can cause tremendous anguish if somebody has discovered that there has been fraud and there was not a quick response. There was a case in one of your earlier hearings that I read in the *Hansard* of a man who had in fact died by the time they resolved the case. Situations like that are very difficult and very messy. It is being able to know what the questions are, being able to act on them and having somebody other than the person who may be the perpetrator dealing with the situation. A meeting of members may not solve all of that. It may or it may not, but there might be other mechanisms.

**Senator HOGG**—You are really looking for someone to slip up, in many instances, to detect the fraud, aren't you? Taking it through to the logical conclusion, which is the concept of the meeting, most of those people would not be armed with either the facts or the ability, in some instances, to be able to pursue the issue from the floor. You really need someone to slip up.

Once you get that break, then you can generally break open the complete case. Is that a reasonable assessment of how these things unfold?

**Dr Graycar**—Yes.

**Dr Grabosky**—It is important to distinguish between the situation before the horse bolts and focusing on the barn door. One of the virtues of transparency as a safeguard is that, at least in theory, it provides an opportunity for scrutiny, that makes an offence harder to commit. Transparency is more of a proactive countermeasure than a reactive countermeasure. It is less likely that you will find something wrong at an annual meeting than simply holding the trustees or the principals to account in subjecting them to a degree of scrutiny and surveillance. Having said that, there may well be indicia that emerge at a meeting that may lead one to pursue a lead and uncover malpractice. Simply having the opportunities to subject the principals to scrutiny on a regular basis is good in principle.

**Senator HOGG**—Generally, you uncover fraud before someone becomes too greedy—is that a reasonable basis from which to operate? Because they become too greedy then the whole operation becomes suspect. Once it becomes suspect then people look. Is that a reasonable way to characterise it?

**Dr Grabosky**—By and large, Senator.

**Senator SHERRY**—I will refer to the last point you made in response to Senator Hogg and partly in response to Senator Watson. Companies have annual general meetings. I cannot recall a case where theft and fraud within a company has been uncovered at an annual general meeting of the shareholders. It may have happened, but I do not think that is the way in which theft and fraud would generally be uncovered within a company or organisation. I accept your point in terms of prevention, accountability and transparency, but trying to get together 100,000 or 200,000 members of some of these larger superannuation funds, given the practical consideration of trying to get even a representative group together, would be very hard.

**Dr Grabosky**—I would not challenge that at all. Indeed, one of the considerations that is really important is balancing the virtues of whatever countermeasure it is you seek to apply to the situation against the cost that this imposes on the funds. One could imagine some fairly elaborate preventive instruments which would be prohibitively expensive. It would be chilling to the entire industry, and obviously one wants to avoid that. The challenge is to find the optimal level of intervention which will minimise the risks and the cost at the same time—that is the holy grail, as it were.

**CHAIR**—Would you like to comment on the concept of reporting annually a summary of the complaints register which superannuation trustees are required to keep.

**Dr Grabosky**—Mr Chairman, are you suggesting that as a regulatory idea?

**CHAIR**—Yes, I am throwing the concept to you to get your feedback.

**Dr Grabosky**—That is an interesting concept. I have not devoted a lot of attention to it. It just calls to mind the very recent case of the Japanese company which had been concealing its complaint letters for years.

**Senator SHERRY**—One final point: I mentioned this debate about choice—I call it deregulation—where individual members of a fund will, effectively, be required to make a choice about the fund they are going to be in. It seems to me that a person who is currently a member of a fund, who is not heavily involved in the decision making in any way, shape or form, is being expected to take upon themselves the role that a trustee performs at the present time; they are expected to make a whole series of judgments that the trustees make for them at the present time. I just link that to my earlier question about any potential problems in terms of theft and fraud in that devolution of responsibility out of the trustees' hands—and they are fairly small in number—into the hands of millions of members of funds and the problems that will lead to, in the area you specialise in.

**Dr Graycar**—This is balanced against the strengthening of the professional requirements for trustees. There are two issues. While people make choice, they make choice about the fund that they are going to put their money into—and we know that in many areas, consumers are not always sufficiently well educated to make those sorts of choices and there are all sorts of factors then that influence the outcome. People have bought cars that are not the best cars, because the advertising had told them that they are the best, even though they are not. You can find that argument in many other product areas as well. I think it is a very big ask for an individual member to take on the whole responsibility of making sure the fund is not only performing well in terms of financial return and stability, but also in terms of acting honestly. That has to be something that trustees and management have to ensure.

A very general important principle in protecting any organisation against fraud is the quality of the leadership of the CEO: the messages that are sent in terms of accountability, transparency, the way in which any minor infractions are not tolerated. You are dealing with other people's money, so it is about the highest standards of ethical behaviour and quality management, and leadership getting that across. That is what we would hope is best practice in any organisation. The consumer would hope that his or her organisation would run well along those lines. But to transfer the control, the sort of fraud prevention, to the consumer is just an impossible ask.

**Senator SHERRY**—I understand the context in which you made the used car analogy but, in terms of superannuation moneys, one of the critical differences is that it is one of the few products that is compulsory for employees. There is also the ethical issue of it being for retirement: you will need the moneys in retirement, there is no second chance. You might get a second chance with a used automobile, but it is not compulsory to buy it. There is a whole series of other issues that make super stand out as almost something unique in the marketplace.

**Dr Graycar**—But then that is where the intervening regulatory activity is still very important. A similar argument might well be made with health insurance funds. It is not compulsory, but government has a policy view saying that it wants to raise the level of health insurance fund membership. There are many funds, they compete, but we would like to think that anybody who becomes a member of a health insurance fund knows that they are going to get a certain level of coverage for certain things. There will be differences—some might give you so much for this procedure and so much for that procedure—but at least there is a level of

coverage, and consumers make a choice. But there is a regulator in between that at least makes sure that there is something they cannot fall below. Similar things should apply in the super area.

**CHAIR**—The use of derivatives in superannuation is governed by two pretty fundamental principles. Firstly, the use of derivatives is allowed for purposes of hedging but not for speculation. Of course, the dividing line between the two is pretty fine. Secondly, underneath, there is a cash backing. Given the leverage opportunities of the use of derivatives, have you any messages for the industry?

**Dr Graycar**—I do not know the answer to that.

**Dr Grabosky**—This, again, brings us to the question of prudent management. There are all kinds of instruments and products that one can use; there is a range of competence within the industry, as well, presumably. But I would not claim to have sufficient expertise to be able to say that a certain type of activity should be prohibited.

**CHAIR**—I think that this is the first time that the institute has appeared before the committee. Is that right? I might stand corrected. Thank you very much. We found your presentation very interesting, very informative, and we look forward to you coming back sometime and to working with you again.

**Dr Graycar**—It was our great pleasure.

[3.12 p.m.]

**MUNNS, Mr Neville Oliver, Secretary, WA Shearing Contractors Association**

**CHAIR**—Mr Munns, I should indicate that, although you are appearing before the committee by teleconference, as a witness to the committee, you are protected by parliamentary privilege with respect to the evidence given before the committee. That means that you are given a broad protection from action arising from what you might say in this teleconference and that the Senate does have power to protect you from any action which disadvantages you on account of evidence given before the committee. While the committee prefers to conduct its hearings in public, and there will be a *Hansard* transcript of what is said, if there are any matters which you wish to discuss with the committee in private, please tell us and we will consider your request.

Thank you very much for appearing before the committee today. I would like to introduce my colleagues. I am Senator John Watson, from Tasmania. The deputy chair is also from Tasmania, Labor Senator Nick Sherry. Also present are Labor Senator John Hogg, from Queensland, and Democrat Senator Lyn Allison, from Victoria. I now invite you to make an opening statement.

**Mr Munns**—The submission we have made is fairly concise. As the committee will realise, we represent shearing contractors in Western Australia. The shearing industry is a very labour intensive industry, so we have been fairly involved in problems arising out of occupational superannuation. I do not think that, at this stage, I need to add any more to my submission. Perhaps I could elaborate on any points that are not clear to the committee.

**CHAIR**—Would you like to speak of your experience in terms of some of your members incurring what might be regarded as excessive fines and the lack of flexibility in terms of the regulator or the tax office being able to exercise discretion.

**Mr Munns**—Yes. There was one serious case in which we were involved in helping a member. I point out that the taxation department were trying to help this member but unfortunately they had no latitude and they had to follow the letter of the law. This meant that, even though the employer had paid the required contributions, because he had been late for several years in a row, he was forced to pay those contributions again and pay a 10 per cent interest charge from the time when the worker earned the contribution plus further charges. As I have said in the submission, this resulted in the employer being sent into bankruptcy. His marriage broke up and he had to go back to being a shearer. He lost all of the business capital he had built up over a considerable time.

We feel that the penalties for late payment should be reasonable. People are more aware of this need to pay by the end of July but I am sure that there will be an occasion when someone misses the post and is only a day or two late, but they are still late and it becomes a shortfall and the commissioner has no discretion. He has to apply the draconian measure of saying, 'Pay me the contributions,' and then it goes through a warped system of getting the money to the shearer. And the employer must cover contributions he has already paid to the insurance company. I think that is rather harsh, because their intention was to pay and they have just been late. In fact,

as I said in the submission, you are better off not paying at all—then you only have to pay once if you do get caught.

**CHAIR**—Mr Munns, would it be possible for you to speak into the receiver?

**Mr Munns**—Yes. I will take it off speakerphone.

**CHAIR**—I think it will be a little bit clearer for our members here. Thank you very much.

**Mr Munns**—Yes. I am now speaking on the telephone.

**CHAIR**—That is a lot clearer. Thank you very much.

**Mr Munns**—I think I have covered that aspect of the fine situation. As I say, people are more aware of it. I give publicity to our members in June to make sure that they get their payments in by July but, as I say, the postal pixies do a good job but there could be a case where a member does not get his contribution to the office in time. But I think there is a bit of a safeguard now. The insurance companies have indicated that they will not accept late contributions, so that might be a safeguard. You could get a situation where they inadvertently put them in the bank.

**CHAIR**—Senator Allison, have you got a question?

**Senator ALLISON**—I would imagine that you have strong views about the frequency of SG payments. It would suit your members for monthly or quarterly contributions? Could you perhaps tell the committee what your views are there.

**Mr Munns**—As we said in the submission, we would favour going to a quarterly contribution. Many of our members do pay monthly. They have been paying up to now when they have done their monthly remittance of the pay as you earn group tax. I think now with the GST they might get onto a different cycle but at least it would be quarterly.

Our concern is more for the worker in as much as some contractors hold that money until late July and we believe it should be going into the worker's account and earning interest right from the start, rather than going in after, it could be, 12 months. There is also the problem—and it is not just contractors—that if an employer gets into financial difficulty and does not have the money, then you cannot get blood out of a stone and contributions are not paid.

**Senator ALLISON**—Have your members experienced any difficulty with payments not being made and therefore losing disability and even death insurance cover?

**Mr Munns**—Our members are actually employers. They employ the shearers and the shed hands, so our members do not experience that. The fund we deal with in the main is Australian Primary Superannuation Trust and they have a ruling that if premiums fall in arrears 60 days, then the policy will lapse. However, they have agreed that if the employer is holding the premium and he pays them after the death or disability on which the worker wants to claim, when those premiums are paid, they will retrospectively establish the contract of insurance.

**Senator ALLISON**—Roughly, on how many occasions has that situation occurred?

**Mr Munns**—I do not have any evidence that would enable me to answer that question.

**Senator ALLISON**—Is it very infrequent or rare—can you say that?

**Mr Munns**—I would say it is very infrequent.

**Senator SHERRY**—About how many employees would your employer members be employing on average throughout a year?

**Mr Munns**—The problem is we have seasonal activity. There is a peak in autumn, it drops off in winter and then it peaks in spring, when 60 per cent of the work is carried out in this state. I did calculate that in the peak spring period, we would have, say, 2,500 shearers working, and there would be one shed worker—a wool presser, a rouseabout or a wool classer—to each shearer, so there could be 5,000 in that spring peak. But in the winter and the latter part of the season, it would probably drop down to a thousand shearers and a thousand other workers.

**Senator SHERRY**—I notice at the end of your submission you say:

With the multitude of funds now available it is an onerous task for employers to draw a number of cheques in order to accommodate the requirement of their employees.

Are your employer members paying moneys into different funds for different employees?

**Mr Munns**—Yes. I think most reasonable employers try to accommodate their employees' wishes and, if the employee has perhaps come from another industry and has a fund already operating or has some reservations about the fund that is being utilised in general, they are accommodated.

**Senator SHERRY**—Don't you have a common fund that covers shearing employers and employees?

**Mr Munns**—There is a main fund, which actually is an amalgamation of three funds which were started, and—I have only received this information yesterday—of our 180 members, 130 of those members are making contributions to Australian Primary, but that does not mean to say they are not also making contributions to AMP or Prudential or any of the other thousands of funds that are available.

**Senator SHERRY**—Is Australian Primary a fund that is part of the industrial award provision in WA? Where does the fund come from?

**Mr Munns**—We work under a federal award and, at the moment, the clause on superannuation is not that specific. We are in the process of reviewing our award, and we have union agreement on the clause which says that the superannuation contribution will be paid into a mutually agreed fund. However, if there is no mutual agreement, it will be paid into Australian Primary.

**Senator SHERRY**—From an employer point of view, you would see it as a cost and a disadvantage for an employer to have to pay into hundreds or thousands of different funds, depending on the number of employees—a different fund for each employee?

**Mr Munns**—I think you have to weigh it up. It is extra work, sure, but you have to look at the other aspect of keeping the morale of your workers up, because they do work in a team situation. So you have to balance the two. But it does come up frequently from our members, and this is one of the arguments for paying annually. You would only have to draw one round of cheques, whereas, if you were doing it monthly, you would have to do it 12 times a year.

**Senator SHERRY**—So many of your employer members see a disadvantage if they have to send one cheque off to, say, the Commonwealth Bank, one cheque off to AMP and one cheque off to National Mutual. That becomes an administrative problem for them, does it?

**Mr Munns**—Yes. They are not inclined to be accountants by nature and bookkeeping is put on the backburner.

**Senator SHERRY**—I do not disagree with you—I understand and I sympathise. We have been looking at this issue. What about electronic transfer of moneys? We had a conference in Sydney—sometimes I get a bit Sydney-centric—and we were assured that electronic transfers of moneys will solve these problems for the sorts of people that you represent.

**Mr Munns**—I think it is a matter of timing and culture. We know those facilities are available but, when you are at Carnarvon, Meekatharra or some other remote area, you do not always have access to those facilities.

**Senator SHERRY**—Do you know how many of your employer members are paying superannuation contributions electronically at the moment?

**Mr Munns**—No, I do not know that. I know that 24 of our 180 members are on email and Internet.

**Senator SHERRY**—Is it a small minority? Do you have any idea?

**Mr Munns**—No, I have no idea really of what they are doing as far as their transactions are concerned.

**Senator SHERRY**—If you could take it on notice, you might just make some inquiries—I do not want to overburden you with work—and let us know what the situation is.

**Mr Munns**—I will certainly do that.

**Senator SHERRY**—Thank you for your submission.

**Senator HOGG**—My question goes to your comment in respect of those employees who work only two or three days with one employer and then move on. In your submission you referred to the fact that some of these people could earn between \$264 and \$378 and be below

that threshold of \$450 and, therefore, no superannuation contribution would be made. You then go on to say that, with the other days of work that they would pick up in that month, they would reach the threshold. Is this a major problem in the shearing industry? Is it something that can be addressed by having a portable industry fund such that, as they move from shed to shed, they do not lose the right to have this money paid into a central fund?

**Mr Munns**—I think that it would be up to the members of parliament to amend the act. At the moment, it says that the employer shall pay on account of any worker they employ. So if they do not hit the \$450, there is no legal obligation to make the payment. Our members discussed this way back in the early days and said, ‘Right, we believe these workers deserve to have their contributions paid because they may come back to us next month. They are still an integral part of the work force for the shearing industry.’ I am not saying that every member follows that but that was, you could say, a moral decision we took, that three per cent—as it was in those days—should be paid to every worker even if they worked one day and earned \$110.

**Senator HOGG**—Most of these people would be people that you would see year in, year out, in the sheds, wouldn’t you?

**Mr Munns**—Not so much with the shed hands but for shearers, yes, they work for long times for the one contractor. Shed hands are more transient but many shed hands would work for the same contractor for four or five years.

**Senator HOGG**—The point that I am trying to make is that you are trying to build up a relationship with these people and, in good faith, you have clearly identified—and I applaud that—that these people are entitled to the benefit of that superannuation, even though they do not reach that \$450. How many employers would pay the superannuation component into a fund in spite of the fact that the employee might not be in receipt of the \$450 for the month from that particular employer?

**Mr Munns**—I honestly could not answer that question.

**Senator HOGG**—Could you take that on notice, please, and find out for us.

**Mr Munns**—Yes. I send a circular once a month to members; I will do a survey in the next circular.

**Senator HOGG**—I would appreciate that very much.

**CHAIR**—To help, Mr Munns, I can tell you that the Tasmanian experience is that there is an agreement between the union and the Tasmanian Farmers and Graziers Association which requires the payment of superannuation guarantee irrespective of the quantum of money paid. And while the act does provide this exemption, the practice—certainly in Tasmania—is that there is this understanding that employers will pay with the union, but I understand that is one matter that is going to be clarified when the new agreement is reached.

**Senator HOGG**—I understand that in the building industry, where there are situations not dissimilar to what you are describing in your industry, there are portable superannuation funds. Because an employee moves from one building site to another building site and is employed by

a different employer does not, in any way, strip them of the entitlement to superannuation, because they do not reach the \$450 in the month.

**Mr Munns**—Our fund would actually be portable. They would have a member number and, if they are employed by Mr Brown, he pays into that account number; then if they go down the road to work for Smith, he pays into the same account number. But it hinges on the fact that the superannuation legislation requires employers to make contributions only if the worker earns in excess of \$450 gross in a month.

**Senator HOGG**—I accept what you are saying, Mr Munns. Thank you.

**CHAIR**—Mr Munns, in your submission you indicate that the contribution adds 17c per sheep to the contractors rate for shearing sheep, and contracting is very competitive—a contract may be lost for the sake of 2c. To what extent is there avoidance within the industry? You indicate that shearers are reluctant to do business with employers. But would you say there is widespread avoidance of the obligation to pay the superannuation guarantee charge? It is not clear from your submission.

**Mr Munns**—I do not have any precise figures, and I do not think I could say it is widespread. If I had to put a figure on it, I could say probably 10 per cent to 15 per cent of employers are possibly not making the occupational superannuation contributions. We have been in discussion with the Perth office of the enforcement section of the superannuation division, and they are looking at a project which would have them making closer scrutiny of the wage declarations of employers and the amount they are claiming as having paid for occupational superannuation.

**CHAIR**—Thank you, Mr Munns. You have certainly brought another perspective—an important one—to the committee.

**Mr Munns**—I would add that, since we made that submission, rates of pay have gone up and occupational superannuation is now 24c a sheep; it will go up again on 7 September. Every time there is a wage increase, the proportion paid out to shear a sheep for occupational superannuation increases.

**CHAIR**—I wish to assure you that the issue of penalties is one matter that will certainly be addressed by the committee in our report, and you will get a copy of that report.

**Senator HOGG**—Thank you, Mr Munns.

**Mr Munns**—Thank you.

**CHAIR**—On behalf of the committee, I thank all witnesses who have given evidence for their participation.

**Committee adjourned at 3.34 p.m.**