Association of
Financial Advisers

# Response:

## PJC – Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012

Submission: Association of Financial Advisers Ltd

**5 October, 2012**

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Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Email: corporations.joint@aph.gov.au

Dear Ms O'Neill,

**Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012**

The Association Of Financial Advisers Limited ("AFA") has been serving the financial advising industry for over 65 years. Its aim is to provide members with a robust united voice, continually improve practices and focus firmly on the exciting, dynamic future of the financial advising industry. The AFA also holds the client to be at the centre of the advice relationship and thus support policies that are good for consumers and their wealth outcomes.

With over six and half decades of success behind it, the AFA's ongoing relevance is due to its philosophy of being an association of advisers run by advisers. This means advisers set the agenda, decide which issues to tackle and shape the organisation's strategic plan.

The AFA thanks the PJC for the opportunity to provide a submission on the Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 ("MySuper Tranche 3 Bill"). This submission has been prepared by the AFA on behalf of its members and in response to the MySuper Tranche 3 Bill.

The Australian Superannuation system, with approximately $1.3 trillion in assets, is now a large industry, and in fact is the fourth largest private pension market in the world. The compulsory nature of the Superannuation Guarantee, the legislated increase in the SGC and the tax advantaged options with respect to member contributions, make the Australian Superannuation system a strong and robust industry. Changes to the system, as proposed by the MySuper package of bills, have significant implications for the industry and the country, and therefore it is essential that these changes achieve the stated objectives.

Ensuring the right outcome for consumers is critical in this legislation. Superannuation is typically a person's second biggest asset behind their home. Achieving the right consumer outcomes will also be critical to the Australian economy, through achieving a reduction in the reliance on the government pension.

The AFA has the following key concerns with the MySuper Tranche 3 proposal:

# Intra-fund Advice

- The AFA is pleased that the Government's position on the payment of advice fees through a single uniform administration fee has been further modified. The exclusion of complex advice and ongoing personal advice is a positive change, however the classification of what is complex needs to be reviewed.
- The AFA's key concerns on this issue are that consumers get the best quality advice possible; to avoid members who do not use advice, unfairly subsidizing those who do; and that this arrangement does not serve to under-value financial advice. Where a service can be obtained in a manner where the cost is less than transparent, then it can create a misunderstanding of the true price/cost of the service and also a reduction in the perceived value of the service. In the context of the cost of providing personal financial advice, this situation is likely to be contrary to the longer term objective of having more Australians accessing financial advice.
- Our concern is the conflict between the suggestion that complex advice is excluded, but the specific reference to advice involving a related pension fund or insurance product. Whilst it might be possible to argue that some forms of insurance advice are non-complex, it is likely that in most cases where it is done properly, it will involve complex advice. Where advice is provided in relation to a pension fund, it is inevitable that this will involve complex advice.
- Advice with respect to a pension fund is retirement advice and in all cases retirement advice is complex. This is a point in a client's life where their source of income fundamentally changes and they need to take stock of their existing debts and assets, their expected expenses in retirement, their access to Centrelink benefits and their timeframe for funding their lifestyle. This is very comprehensive in terms of the information that needs to be collected and the factors that need to be considered.
- We note one key point in the recent ASIC Shadow Shopping exercise where retirement advice failed to consider a client's existing debt. This advice was considered poor advice. The same consideration is relevant in the case of intra-fund advice about a pension fund, where it is not possible to exclude the consideration of a very broad range of relevant factors.
- The legislation and guidance needs to be clearer with respect to what is complex advice and what should not be included as part of intra-fund advice. The legislation also needs to be clearer in terms of the meaning of on-going personal advice. Does this mean that the advice can only be provided in one interaction (meeting or phone call)? This limitation is discussed in terms of what the member would reasonable expect. A member seeking advice on the most suitable investment option may expect this to be reviewed over time as the members relevant personal circumstances change. The other issue here, is that Trustees might design their services in a manner where they can be selected in discrete units, but with an expectation that the member will return for further advice. This approach to eliminating ongoing personal advice, requires clarification.
- We would further like to raise a concern with the reference to a cash management facility. We cannot see how this would be directly related to the fund and how advice on a cash management facility, paid through an administration fee, would possibly pass the sole purpose test.

# Defined Benefit Members

- The AFA does not believe that the exclusion of defined benefit schemes from the MySuper framework is appropriate. If MySuper is good for superannuation members then it should be good for defined benefit members. Defined benefit funds are excluded from a large number of the MySuper provisions including the insurance requirements. It is unclear why the requirements with respect to insurance, that should apply to all superannuation members, have been excluded from defined benefit members. The opt-out option is not required for defined benefit funds and there is an exemption for defined benefit funds with the prohibition of self insurance.
- We also question the reason why defined benefit funds are automatically added to modern awards. There should be a process to assess suitability of defined benefit funds, as there are for other funds. This proposal appears to be inconsistent with the considerations of the Productivity Commission in their review of default superannuation funds in modern awards.
- It seems that this positioning is based upon the simplistic assumption that defined benefit arrangements are always better than accumulation schemes. This is not always the case.
- In many cases, members of defined benefit schemes may also have accumulation accounts. It seems inconsistent that there will not be the same MySuper provisions applied to these accumulation accounts.
- It seems that defined benefit schemes have been excluded from the MySuper regime as a matter of simplicity. It is difficult to see why the complexity in this area was avoided when the Government was willing to take on such complex and risky proposals such as the mandatory transition of accrued default amounts.

# Transition to MySuper

- The AFA Strongly opposes the mandatory transfer of “accrued default amounts” to MySuper products. The Government has failed to put forward an adequate case as to why this will be in the best interests of members. It is also a direct attack on the revenue streams of financial advisers and particularly corporate superannuation advisers.
- There is a clear alternative to this mandatory transfer, being the option to make a voluntary transfer to the new MySuper option. The Government could undertake an advertising program or national mail-out, as they have with other pieces of legislation, to notify people of the availability of new MySuper funds.
- The legislation will impact both members who have made no election as to where their superannuation contributions should be invested and also members who have specifically chosen to invest their superannuation contributions in an option that also happens to be the default option. The definition of “accrued default amounts”, which includes all members who have chosen an option that is where their contribution would have been invested, if they had made no decision, is fundamentally wrong. It is not the role of the Australian Government to assert that a member’s decision was invalid and the money will be moved against their will.
- Often the default option was selected by the employer. Thus in the one master-trust there could be many investment options that are being used as the default option for one employer or another.
- A member could end up in a default option as a result of a specific decision on their part to invest entirely in that option, to invest in a range of options including the default option or to follow the advice of a financial adviser to invest in the default option as this may best suit their risk profile. This legislation is taking the option that has the broadest impact and the greatest likelihood of negatively impacting people who are happy with their current arrangements. It is recognized that it is difficult to be absolutely certain who has not made a conscious decision to select their investment option. The legislation, if it was to proceed, should be based only on those people for whom there is absolute certainty that they have not selected an investment option.

# Transition to MySuper (cont)

- In practice, it will be relatively straight forward for some funds to determine who the "accrued default amount" members are. For other funds that have been operating for a long time and who have many aligned employers who have different default options, some of which may have changed over the years, this is an extremely complex matter. Does the Government expect trustees to recall all historical member files, to trace through, to see what decisions the member made and what the default options were at various points in time?
- The legislation appears to be based upon the incorrect assumption that the MySuper option will be identical or very similar to the default option(s). This is simply not possible as there may be multiple default options within the one fund. The legislation is also based upon the potentially incorrect assumption that the MySuper option will be a better option than the default option(s). There are a number of reasons why the MySuper options may generate lower returns.
- We are also very concerned that the definition of "accrued default amounts" might mean that this legislation has implications for retail superannuation products where a client has received financial advice and is in an investment option that happens to be the default option selected by the trustee. With retail funds, this proposal will detrimentally impact a large number of members who have deliberately chosen their investment options. Within retail funds, the proportion of clients who are in the default option, without having made that decision, would be very low. If the Transition to MySuper part of this legislation is to proceed, then it should be limited to corporate superannuation arrangements where the utilisation of default options by disengaged members is much more common.
- Moving members without their agreement and potentially knowledge may be particularly disadvantageous to some members. We have already considered the case of negative outcomes with respect to investments. The greater risk, however is with insurance. Whilst it is expected that a majority of these transfers will be from one product within the superannuation trust to another, there will certainly be a number where they are moved from one fund to another. This might be as a result of a product provider who runs a number of funds, only making the MySuper option available within one fund. It also might be because the existing fund has chosen not to proceed with a MySuper option and the members need to be moved to a new fund. Where there is a move from one fund to another and there is no guarantee of transferring the insurance on identical terms, the member is exposed to significant risk. In some cases it is likely that the new fund will be unable to offer the same insurance on the same terms. Underwriting may be required for insurance at a level of cover above the minimum level. If the member has experienced a health issue since the original cover was taken out (which could be many years), then it may simply not be available on reasonable terms.
- We note that trustees will be required to notify members and they will have up to 90 days to respond and potentially choose to stay in their current option. There is a particularly sizeable risk that people will simply not read this communication, or otherwise not get around to making a decision. In any matter this important, a single communication is clearly inadequate.
- There is no consumer protection in this measure. The member cannot take any action against the trustee for a detrimental outcome. It is striking that a Government would forcibly move a very large number of members, expose them to significant risk and then offer them no options for recourse if anything goes wrong. The legislation removing consumer protection in Section 29XB is as follows:

**"A trustee of a regulated superannuation fund is not subject to any liability to a member of the fund for an action taken to give effect to an election made in accordance with section 29SAA or 29SAB."**

- The legislation does not seem to take account of the fact that numerous unintentional errors and administrative issues will arise as a result of this mandatory transfer. It will either rest with the generosity of the trustees or aligned institution to remedy these errors or leave the consumer at a loss. Such losses could include having money out of the market during a period when asset values increase or being subject to a range of administrative errors that are possible when undertaking an exercise of this significance.
- The FoFA legislation recognized the existence of an adviser's property rights with respect to the commission payments on existing clients. This MySuper Tranche 3 legislation is specifically seeking, in an underhand manner to extinguish these property rights without recognizing them or compensating for them.

# Transition to MySuper (cont)

- The legislation requires the MySuper applicant to elect to transfer their existing default fund members to a MySuper fund by 1 July 2017. The trustees will then become legally obliged to proceed with this transfer and it will become a license condition. Even if the MySuper license is revoked, they will still be obliged to proceed with a transfer to a MySuper product. This is a tricky legislative mechanism to avoid Government responsibility for the forfeiture of property rights and to transfer the legal exposure to the trustees. The trustees are given protection from action by members, but not from actions by advisers.
- Where a trustee elects not to seek a MySuper license they will also be required to transfer the accrued default amounts to a MySuper fund. In this case the legislative mechanism to avoid exposure to the acquisition of property rights on unjust terms is less clear. It seems likely that this does constitute the acquisition of property rights on unjust terms, which means that trustees will be placed in a very difficult position.
- It is important to realize that this mandatory transfer of default fund members will involve substantial cost across the superannuation funds, the impacted advisers and the members. Many members are likely to seek financial advice as a result of this process, which will be good for them in the long run, but will involve short terms costs, driven by the actions of the Government.
- We have also reviewed the Draft Prudential Standard SPS 410 and it is clear that there will be a significant impact on Trustees to comply with this standard. The identification of impacted members, the quarterly reporting from March 2013 and the short timeframe to prepare a transition plan all point to significant costs for trustees. It appears that this draft standard is intended to encourage Trustees to arrange the transfers as soon as possible. The ongoing reporting obligation will place a disincentive on trustees to defer the transfer to the end of the period.
- The regulation impact statement prepared by Treasury in 2011, that specifically refers to this proposal, provides very little detail on the number of members involved or the costs to the industry. There is a reference to the rights of advisers and a suggestion that trustees may need to keep funds in reserve for any claims. There is certainly no numbers provided with respect to the impact of this initiative on the income of financial advisers. It is appears that this RIS has significantly underestimated the impact of this legislation on the industry.
- The AFA is deeply concerned with the way the legislation has been designed. Members who are the subject of a mandatory transfer will have no ability to take action against any party involved in the transfer. This is a seriously dangerous position from a consumer protection perspective. How can a Government force an outcome on consumers that might result in disadvantage and yet offer no level of consumer protection?
- In the AFA's view this part of the legislation is seriously flawed, and requires reconsideration to ensure that the right consumer outcomes are achieved and that the rights of financial advisers are properly addressed.

We seek the input of the PJC to consider the issues above and to incorporate appropriate suggestions in your report to Government.

Yours sincerely,

Richard Klipin

Chief Executive Officer
Association of Financial Advisers Ltd