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18 October 2006

Mr David Sullivan
Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
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Parliament House
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Dear Mr Sullivan,

Please find attached the Australian Bankers' Association (ABA) submission to the Parliamentary Joint Committee (PJC) on Corporations and Financial Services inquiry into the structure and operation of the superannuation industry.

The ABA welcomes the opportunity to provide some general observations about Australia's current superannuation and retirement income system as well as specific comments on some of the terms of reference examining the structure and operation of the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

If you have any queries regarding the issues raised in this submission, please contact me or the ABA's Director, Corporate & Consumer Policy, Diane Tate on (02) 8298 0410: dtate@bankers.asn.au.

Yours sincerely

A handwritten signature in black ink that reads "David Bell". The signature is written in a cursive, slightly slanted style.

David Bell



Submission to the Inquiry into the Structure and Operation of the Superannuation Industry

18 October 2006

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Inquiry into the Structure and Operation of the Superannuation Industry

1. Introduction

The Australian Bankers' Association (ABA) welcomes the opportunity to provide comments to the Parliamentary Joint Committee (PJC) on Corporations and Financial Services inquiry into the structure and operation of the superannuation industry.

The ABA has recently provided comments on the Federal Government's 2006 Budget announcement to reform the superannuation system. We commend the Government on its vision and welcome the proposals as a package of reforms designed to reduce complexity and increase flexibility of the superannuation system as well as encourage greater superannuation and private savings for Australians. We would be pleased to provide to the Committee with a copy of our formal submission to Treasury.

The ABA strongly supports the policy principles guiding the changes to the superannuation system – that is, *simplicity, flexibility, adequacy* and *literacy*. The ABA has been advocating these policy principles for sometime. The changes should also foster competition and avoid economic distortions for savings and investment products. It will be important to ensure that the required technical changes to superannuation, taxation and social security legislation effectively deliver the objectives of the proposals and maximise the opportunity to reduce administration burdens and compliance costs.

Overall, we believe that Australia's superannuation and retirement income system should maintain the 'three pillars policy'; endorse the policy principles of *simplicity, flexibility, adequacy* and *literacy*; provide incentives for Australians to save and plan early for their retirement; and encourage private savings.

2. Background

The Superannuation Guarantee (SG) legislation was introduced in 1992, with the completion of the phased introduction in 2002 with minimum employer superannuation contributions of 9%. The compulsory superannuation system provides a balance between employees relinquishing current consumption and expenditure for increasing living standards in retirement.

The Government's *Intergenerational Report* (May 2002) noted that demographic changes over the next decades will lead to significant fiscal strain due to increased government expenditure. Modelling has demonstrated that the age pension and the health and aged care system are essential components of retirement incomes for retiring Australians. Without a reliable age pension 'safety net', many Australians will face inadequate standards of living.

In 2002, the Senate Select Committee on Superannuation considered the issue of superannuation adequacy. The ABA's submission to the inquiry indicated that a significant gap exists between the expectations of Australians for their standard of living in retirement, and what the present system will actually deliver. The ABA suggested that a national goal should be established for significantly increased retirement provision through a combination of increasing superannuation contributions from individuals; extending Government co-contributions; reducing taxation; and generally improving the incentives for voluntary contributions.

Furthermore, the ABA considered that simplification of superannuation is feasible, and would improve not only simplicity and transparency but also equity and incentive. Simplification should be integrated with reform of the tax structure applying to superannuation, including removal of Reasonable Benefit Limits (RBLs) and age-based limits and removal of restrictions on who may contribute and differences of treatment among different recipients of benefits.

The key findings of the Senate Select Committee's report *Superannuation and Standards of Living in Retirement* (December 2002) include:

- The available evidence demonstrates that the current arrangements for superannuation may not provide an adequate income in retirement for most people and that strategies need to be identified to address the shortfall;
- The current taxation treatment of superannuation produces some inequities which need to be addressed;
- The relationship between superannuation and the age pension and other social security measures could be better integrated;
- The superannuation system in Australia is very complex, not easily understood and requires simplification.

In 2003, the Senate Select Committee on Superannuation considered the issue of superannuation and planning for retirement. The ABA's submission to the inquiry indicated that reform of the superannuation and welfare system should seek to, where possible, fully integrate based upon the development of an effective 'safety net', which would provide all Australians with an adequate income when they are unable to provide for themselves at any stage of their lives. The ABA highlighted a number of key issues regarding planning for retirement, such as encouraging older employees to remain in the workforce longer, improving the structure of tax and social security benefits, making access to financial planning advice easier and retraining of mature aged workers.

In 2004, the Treasurer announced the Government's *Transition to retirement* policy. These changes allow people, once they have reached their preservation age, to access some or all of their existing preserved superannuation benefits in the form of a non-commutable income stream. These changes shifted retirement planning, as once Australians reach their preservation age they no longer have to formally retire to gain access to their superannuation. Also in 2004, *Choice of Fund* legislation was passed giving certain employees a choice of superannuation fund. 'Super Choice' required a substantial consumer education effort from the Government and financial services industry.

In 2005, the House of Representatives Standing Committee on Economics, Finance and Public Administration considered how we could improve the superannuation savings for people under age 40. The ABA's submission to the inquiry identified a number of barriers or disincentives with the superannuation system that if addressed, and coupled with increasing incentives and improving awareness of the importance of saving early for retirement, would lift superannuation and private savings for Australians.

In 2006, the Treasurer announced the Government's *A Plan to Simplify and Streamline Superannuation*. These changes represent the most significant changes to superannuation and retirement incomes policy since the introduction of compulsory superannuation. The ABA's submission on the proposed changes broadly supported the reforms as enhancing Australians' ability save for the future and determine what savings and investment choices best suit their needs pre and post retirement. In particular, removing tax on superannuation benefits for people over age 60, removing RBLs and age-based limits and replacing these with annual contribution limits, reducing the impact of the assets test, removing compulsory cashing requirements and simplifying retirement income rules, should improve consumer sovereignty and promote competition across the superannuation industry.

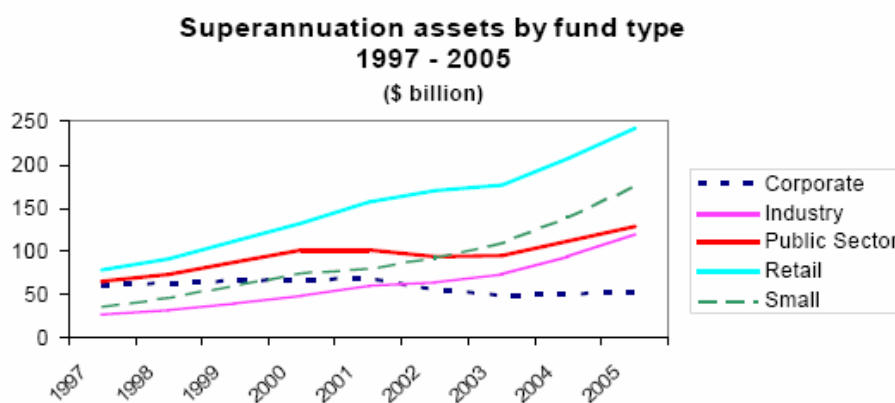
There have been substantial (almost constant) changes to superannuation, taxation and social security policy over the last five years. Some additional changes seeking to encourage greater superannuation and private savings include extending superannuation co-contributions, adjusting personal income tax rates, removing the work test for superannuation contributions for those under 65, introducing spouse contributions and splitting of contributions with spouses and abolishing the superannuation surcharge, as well as pending changes to simplify and streamline superannuation.

Changes in the superannuation industry have been driven by both reforms to public policy and to regulation. In addition to implementing new public policy, the superannuation industry has transformed through new regulations relating to licensing, conduct and disclosure obligations, due to amendments to the *Corporations Act 2001* by the *Financial Services Reform Act 2001* (FSR Act) and amendments to the *Superannuation Industry (Supervision) Act 1993* (SIS Act) by the *Superannuation Safety Amendment Act 2004*.

Given the scale of the changes and how recent they are, and with further changes envisaged to take effect from 1 July 2007, it is difficult to assess whether it all amounts to greater efficiencies for financial services providers and improved protections for consumers. However, overall, the ABA strongly supports encouraging greater superannuation and other private savings, thereby promoting higher retirement incomes and improved living standards in retirement.

3. Overview of the superannuation industry

Total superannuation assets increased by 18.5% during the year to 30 June 2005 to \$761.9 billion. Of this total, \$464.3 billion is from APRA-regulated superannuation entities and \$172.0 billion is regulated by the Australian Taxation Office (ATO). The remaining \$125.7 billion comprises exempt public sector superannuation schemes (\$82.5 billion) and the balance of life office funds (\$43.2 billion). The number of superannuation entities increased by 6.9% during the year to 311,000. The increase was largely due to the growth of ATO-regulated Self-Managed Superannuation Funds (SMSFs) which grew by 7.5% (21,186 funds) during the year. The number of entities with more than four members decreased by 25.8% (461 entities). The member accounts grew by 4.3% during the year to June 2005¹.



¹ APRA (2006). *Statistics: Annual Superannuation Bulletin*. June 2005 (issued 20 April 2006).
<http://www.apra.gov.au/Statistics/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=10762>

4. ABA's position on superannuation

4.1 Sustaining the 'three pillars policy'

The three basic pillars of Australia's retirement income system are:

- Age pension funded by Government revenue;
- Compulsory superannuation contributions (9% of earnings); and
- Incentives to encourage private saving for retirement.

In order to lift superannuation and private savings, it is important for Australians to have confidence in the stability and sustainability of the superannuation system, including the continuance of the age pension as part of the overall retirement income system. The World Bank continues to affirm multi pillar retirement incomes systems as sound policy.

The ABA supports Australia's stable and sustainable three pillars retirement income system.

4.2 Simplifying retirement incomes

Consumers must have confidence that their superannuation savings are safe over the long-term. Australia's superannuation system is significantly cumbersome. Currently, retiree investment and income decisions are strongly directed by tax and social security incentives. The strength of incentives and penalties could amount to over-regulation, and indeed in some respects distortion of the retirement income system.

Complexity of Australia's retirement income system reduces understanding for consumers as well as placing heavy administrative burdens and compliance costs on providers, and thereby costs on every consumer. Reducing complexity and minimising administrative burdens and compliance costs should be a continuing goal for any changes to the superannuation system.

The removal of tax on superannuation benefits for people over age 60 will simplify the system. The system can then be characterised as TTE (Taxed contributions, Taxed earnings, Exempt benefits), and the simple message that superannuation is "tax-free in retirement" should encourage retirement saving. Given that Australia was the only country to tax superannuation, or equivalent, at three stages, this change will better align Australia with international practice and experience.

The ABA suggests that the retirement income phase should be simple and clear, such as:

- Strategies, tools and products should help retirees spread their available income across retirement – subject to their needs and preferences.
- Strategies, tools and products should be able to be tailored to individual circumstances.
- Strategies, tools and products should be flexible to adapt to the inevitable changes retirees will face.

The ABA believes that measures should seek to reduce the complexity of the superannuation and retirement incomes system so that consumers have greater confidence in, and understanding of, methods of private savings and performance of superannuation savings. Furthermore, better integration of superannuation, social security and taxation systems will promote enhanced superannuation and private savings.

4.3 Increasing flexibility of superannuation

Retirement can extend over 30 years and retirees' circumstances are certain to change over that time. Currently, superannuation rules tend to constrain both income and capital flexibility, especially in complying income streams.

However, the new contribution rules, removal of tax from superannuation benefits for people over age 60, and income stream changes will improve flexibility of superannuation in the contribution phase, in preparing for retirement and in retirement.

- In the contribution phase: The replacement of the current lower maximum deductible contribution limits (age-based limits) for people aged under 50 with a single limit of \$50,000 will remove a barrier to higher early contributions. People will have the flexibility to make higher contributions according to their earning and saving capacity.
- In preparing for retirement: The nature of tax and age pension incentives tended to throw up a limited range of retirement income options, often a single strategy, regardless of the individual/couple's circumstances and desires. People will now have fewer constraints on their retirement income choices due to complex rules.
- In retirement: The simplified tax and superannuation rules will boost retiree flexibility in terms of their options for use of their income and capital as well as transition into and out of retirement, if they so wish.

The removal of tax on superannuation benefits, coupled with the removal of the age-based limits and RBLs and replacement of these limits with the annual contribution limit, in effect establishes a lifetime cumulative limit that balances concessionality and accessibility. Furthermore, the changes will allow retirees far wider scope to tailor retirement income choices to their needs, and to adjust their arrangements to suit changing circumstances.

However, superannuation will still be subject to preservation rules. The requirement under the SIS Act that superannuation benefits be kept in the superannuation system until the member reaches preservation age, contributes to the inflexibility of superannuation as a savings vehicle. Preservation means that a person is generally unable to cash-in their superannuation benefit (or a part thereof) from a superannuation fund until they have retired after preservation age. The inflexibility of superannuation can result in lack of confidence with superannuation. Therefore, it is vital that consumers have incentives to make additional voluntary contributions as well as confidence in the stability and sustainability of the superannuation system.

The ABA supports the preservation of superannuation as improving the standard of living for Australians in retirement, but also in addressing the fiscal pressures of an ageing population. However, to offset the inflexibility of preservation, superannuation should be accompanied by:

1. Incentives to promote the attractiveness of superannuation (e.g. expanding the co-contribution scheme to align better with income tax rates),
2. Flexibility to enable retirees to tailor their retirement incomes and financial investments to their needs, circumstances and preferences, and
3. Key messages on the value of long-term savings.

4.4 Improving adequacy of superannuation

Generally, Australians are still not planning early enough, or saving enough, for their retirement. It is vital that sustainable public policies provide incentives as well as address disincentives for superannuation and other private savings, to ensure optimum living standards in retirement.

The removal of age-based limits will give Australians the ability to make higher contributions early in working life, and thereby will significantly boost retirement savings through compounding investment returns. It will now be possible for young adults to make a head start on superannuation, and also perhaps allow them to ease contributions when individual or family disposable income is low, such as when paying off a HECS or HELP debt, saving for a mortgage or when children are young.

However, the ABA considers that it is important for consumers to have a financial goal for enhancing their financial independence. The Senate Select Committee's finding that the goal for an adequate level of retirement income should be around 65% of pre-retirement income provides a reasonable target for retirement income. Efforts should continue to focus on closing the retirement savings gap by encouraging a savings culture, with Australians establishing financial goals and planning early for retirement.

The ABA believes that initiatives to promote financial independence should focus on lifting voluntary superannuation contributions, increasing private savings and enhancing long-term wealth accumulation.

4.5 Building literacy in savings strategies

Currently, it is difficult, if not impossible, for many Australians to understand the technical details and implications of the superannuation system. The ABA and its member banks have demonstrated a long-term commitment to promoting consumer understanding and financial literacy. However, even as recently as at the ABA's Financial Literacy Symposium "Broadening Financial Understanding" held in June 2006, commentators pointed out that superannuation had become so complex that even basic messages are difficult to get across to consumers.

Low financial competence and understanding make it more difficult for consumers to plan and save effectively for their retirement. While the changes to simplify the superannuation system will enable consumers to better understand their retirement income choices and make better retirement savings and income decisions, the changes will need to be accompanied by basic consumer information, so that Australians gain the capabilities to better manage their savings.

According to ANZ *Survey of Adult Financial Literacy in Australia 2005*²:

- 74% of people with low levels of financial literacy and 78% of people on low incomes were unlikely to understand that employees can make additional voluntary contributions to their superannuation fund.
- 65% of people said they had not identified a figure for how much per year they would need to live on when they retire.
- 34% of people expect to live "about as comfortably" in retirement as they were now (down from 37% in 2002) and 40% of people expect to be "less comfortable than they were now, but getting by OK" (up from 37% in 2002).

² <http://www.anz.com.au/aus/aboutanz/Community/Programs/FinSurvey2005.asp>

- 55% of people under 65, employed and with superannuation correctly identified the "super choice/portability" reforms as changes to the law that (at the time of the survey) would come into effect 1 July 2005.

These survey results are telling, particularly in an environment of further superannuation reform. It will be imperative that consumers are given useful information on the new superannuation system.

The ABA considers that information should be developed around 'information seeking opportunities'. Much of this material already exists and there is an opportunity to produce simpler information people can understand more easily, including:

- General superannuation and contributions queries – how much can I save; what is the co-contribution and how will it help me; how much do I need for retirement, etc. (Many of these questions are, or will, be addressed by the Financial Literacy Foundation, and the simplified rules provide a great opportunity to capitalise on individual interest when it arises.)
- Starting to think about retirement – what are my options; how do I work out what is enough; how long will my money last; how can I accelerate my savings; should I put my savings in one place, etc.
- Considering retirement – what do I have to do; what is an income stream (now a much simpler question); when and how do I want income in retirement; where do I find more detailed information, etc.
- In retirement – how do I match my income with my needs; how do I make my savings last; what do I need to do for tax/age pension, etc. assisting retirees in planning and taking control of their retirement income choices.

As part of the ABA's financial literacy program, we are producing a suite of financial literacy booklets aimed at assisting consumers better understand financial services and take control of their finance. In 2005 the ABA, IFSA and FPA released a financial literacy booklet: *Smarter Super: Make the most of Your Retirement* to coincide with the implementation of 'Super Choice'. This publication seeks to explain some of the technical aspects of superannuation as well as provide some useful tips and suggestions so that individuals feel more confident about their superannuation savings.

The ABA strongly believes that knowledge of superannuation and other private savings options, coupled with the capacity and incentive to save, will better promote a wider savings culture in Australia. Financial literacy is the key to getting the most out of the superannuation system. Therefore, encouraging access to professional financial advice is particularly important not just for ensuring that individuals have access to information necessary for them to make a decision about savings and investments, but also for promoting financial literacy within the community.

A good level of financial literacy is essential for enabling individuals to be both aware of the decisions they need to make about retirement and to take sound decisions about matters such as when they will retire, how much they need (or want) for retirement, and so on.

The ABA is committed to broadening the financial understanding of Australians, especially through financial literacy programs implemented in partnership with government and community sectors. The ABA and member banks will produce materials to assist consumers understand the new superannuation system. However, the ABA suggests that the Government undertake a national campaign to raise awareness of the changes to come into effect in 2007 and promote consumer understanding of superannuation. We envisage that the Government's Financial Literacy Foundation will be instrumental in delivering key messages and coordinating information dissemination. Key messages should highlight the importance of discretionary saving, both additional employer contributions from salary sacrificing and voluntary employee contributions.

4.6 Promoting incentives to save and plan

Importantly, the ABA believes that Australians should have incentives to save and plan for their future. Reducing complexity and increasing flexibility with superannuation will go a long way to removing barriers to early saving and retirement planning.

As we said in our submission to the House of Representatives Standing Committee on Economics, Finance and Public Administration on its inquiry into improving the superannuation savings for people under age 40:

“Understanding the factors that influence younger peoples’ decisions about superannuation, savings and investment will be important for determining how best to target savings messages, encourage greater superannuation contributions and promote greater voluntary and private savings. Ultimately, improving superannuation savings by encouraging voluntary superannuation and other private savings will assist in closing the retirement savings gap...”

Reducing complexity and increasing flexibility will lead to greater confidence in superannuation, which in turn will lead to greater interest and commitment in saving and planning early for retirement and benefits for private and national savings.

The ABA believes that Australia’s retirement income system should be promoted through targeted messages that seek to encourage greater superannuation contributions and private savings.

4.7 Encouraging private saving

Superannuation is a vital part of retirement incomes; however, other private savings are also important. Self-provision in retirement should be the aim of strategies for enhancing financial independence and retirement income adequacy. The ABA considers that as part of improving retirement income adequacy, incentives for superannuation and private savings should promote long-term savings and address current inequities between particular financial products and investments.

The changes to the superannuation system will go some way to encouraging diversified pre-retirement savings and post-retirement incomes and will supplement superannuation savings by enabling greater choice, financial independence and a higher standard of living in retirement. Improving the private savings environment will also reduce future fiscal pressure of Australia’s ageing population.

Australia has a low level of deposits compared to other countries. Some evidence as to why deposits might be low in Australia was given when the report on *International Comparison of Australia’s Taxes* (“Hendy/Warburton report”) was released in April 2006. It showed that Australia has the highest top marginal tax rate on interest income amongst OECD countries³.

One of the simplest means to protect against unforeseen circumstances (such as the loss of a job or the loss of a family member providing supporting income) is to encourage people to have a savings buffer and/or protect themselves against such unforeseen circumstances. For example, the Government could consider addressing current anomalies in tax treatment and introducing rebates for people who invest in life insurance or other risk products. It is important that disincentives are replaced with incentives for savings and investments.

³ http://comparativetaxation.treasury.gov.au/content/report/downloads/CTR_full.pdf (p xxv)

The ABA recommends that Government could consider strategies for improving incentives for private savings and supporting development of risk products for increasing national savings, sustaining retirement incomes and managing age-related expenditure.

5. Regulation of superannuation

The Australian Prudential Regulation Authority (APRA), Australian Securities and Investments Commission (ASIC) and the Australian Taxation Office (ATO) all regulate aspects of the superannuation system.

5.1 Regulators

5.1.1 APRA

APRA supervises complying superannuation funds other than self-managed superannuation funds (SMSFs). All trustees must hold a Responsible Superannuation Entity (RSE) licence and only an RSE licensee can register a superannuation entity with APRA. The two year transitional licensing period for trustees of prudentially regulated superannuation entities ended on 30 June 2006.

Trustees must manage superannuation funds prudently. There is no prudential standard making power in respect of regulated superannuation entities. However, APRA does have the power under section 332 of the SIS Act to issue modification declarations.

Superannuation funds and trustees must meet certain requirements before they are able to obtain, and retain, an RSE licence. For example, trustees must demonstrate fitness and probity, maintain adequate resources (including financial, technological and human resources) and develop a risk management plan for each fund under their control.

APRA provides guidance on the manner in which it interprets and assesses compliance with the operating standards contained in the law. APRA issues circulars and guidance notes on its interpretation of the SIS Act, SIS Regulations and related matters. APRA's guidance on superannuation is non-binding. However, APRA uses its guidance as part of reviewing trustees' compliance with superannuation regulation.

In addition to APRA requirements, the Government is able to apply standards to superannuation funds and retirement savings accounts which relate to maintaining prudential supervision or furthering retirement income policy objectives, such as restrictions on access to benefits. The ABA considers it is unnecessary for compliance with circulars to be mandatory or for APRA to have the power to make standards relating to superannuation.

5.1.2 ASIC

ASIC administers the Corporations Act, the *Australian Securities and Investments Commission Act 2001* (ASIC Act), and parts of the SIS Act as they apply to superannuation trustees and other financial service providers in the superannuation industry. Superannuation funds and trustees must comply with the relevant responsible entity and managed investment scheme provisions of the Corporations Act. Those that hold an Australian Financial Services Licence (AFSL) have to comply with various conduct obligations, disclosure requirements and meet standards for advice provided to retail investors.

ASIC issues policy statements, guides, FAQs, and class order and other relief instruments. ASIC uses its suite of FSR documents as part of its compliance surveillances to ensure that financial services providers meet their licensee obligations.

5.1.3 ATO

The ATO ensures SMSFs comply with the SIS Act and regulations.

5.2 ABA comments on regulation of superannuation and financial services

Superannuation trustees may be subject to both prudential regulation and market conduct regulation, and therefore require a licence from both APRA and ASIC.

5.2.1 Prudential regulation

In March 2002, the Superannuation Working Group recommended that the SIS Act be amended to require that trustees of superannuation entities (excluding SMSFs) be licensed by APRA and that all superannuation funds be registered by APRA prior to commencement of operations. Subsequently, the SIS Act was amended and the transition period for licensing and registration expired on 30 June 2006.

Importantly, the requirement for an APRA licence would be in addition to the FSR requirements to have an AFSL to advise or to deal in interests of the fund. However, a trustee should not be required to gain an ASIC licence to operate the fund.

While we understand that the Government has made a policy decision that superannuation should be prudentially regulated, amongst other reasons due to the compulsory nature of superannuation savings, prudential controls should not unduly restrict superannuation funds. For example, the ABA believes that prudential oversight of superannuation funds should not prescribe investment rules, as this would lead to more conservative investment strategies and ultimately reduced retirement benefits.

Consistent with the ABA's submission to the *Options for Improving the Safety of Superannuation Issues Paper*, we consider that the separation of prudential and retirement income provisions of the SIS Act should be a longer-term objective. However, the ABA acknowledges that this would be a very large undertaking and should only be pursued where a new framework reduces complexity, increases clarity and reduces compliance costs. Some commentators say that the combination of prudential and retirement income provisions would not have occurred if introduced after the implementation of Wallis.

5.2.2 Financial services regulation

In April 2006, the Parliamentary Secretary to the Treasurer released the *Corporate and Financial Services Regulation Review Consultation Paper*. The consultation paper is the latest release to refine aspects of FSR. The ABA has been liaising closely with the Treasury and ASIC on many of the proposals. We believe that the proposals should strike a better balance between the costs of compliance and the benefits for the Government, industry and consumers of regulation.

The ABA believes that FSR should facilitate market efficiency and integrity, product innovation, market confidence and informed consumers. Therefore, it is important that Government and industry continue to work together to reduce unnecessary compliance burden without compromising the intent of the law. The ABA looks forward to working with the Government on implementing changes through the *Simpler Regulatory System Bill*.

5.2.3 Business regulation

In October 2005, the Prime Minister and the Treasurer announced the inquiry into reducing the regulatory burden on business ('Regulation Taskforce'). The inquiry sought to identify practical options for alleviating the compliance burden on business from Government regulation. The ABA made a number of submissions to the inquiry. The Finance Industry Council of Australia (FICA) also commissioned an extensive review of regulation in the financial services sector by CRA International (FICA Report).

Broadly, the ABA highlighted a number of themes of regulation:

- Incrementalism and “reform fatigue”;
- Increased prescription versus principles-based guidance;
- Inadequate consultation and transparency when implementing regulation;
- Need for cooperation between regulators to reduce duplication and inconsistency;
- Lack of national uniformity; and
- Creation of a “compliance culture”.

It is pleasing that the Government has responded to a number of industry's concerns through the release of the *Corporate and Financial Services Regulation Review Consultation Paper* and *A Plan to Simplify and Streamline Superannuation*, but also through the commitment to work with the Productivity Commission, and bodies like the Council of Australian Governments (COAG), to improve regulatory decision making, performance benchmarking and harmonisation of regulation across jurisdictions.

The ABA recommends that the Government conduct a review of the regulatory framework for superannuation. A review should include specific examination of the role of APRA, ASIC and ATO with a view to removing unnecessary duplication of regulation of the superannuation industry.

6. Financial advice and superannuation

Some commentators have suggested that the pending changes to the superannuation system will mean the end of financial planning or estate planning. The ABA disagrees with this view. While financial planning will be less orientated towards the taxation and regulation surrounding superannuation, it will remain a vital part of the financial services system, as consumers will need to receive information and advice about savings and investment opportunities that best suit their needs, circumstances and preferences.

It will be important for the superannuation and retirement incomes framework to enable retirees to take advantage of greater superannuation flexibility to build responsible retirement income strategies that best suit their needs, circumstances and preferences. It will therefore also be important for consumers to receive useful information about superannuation and other retirement income products.

6.1 Regulation of financial advice

In most cases, under the current law trustees of superannuation funds with net assets of at least \$10 million may be treated as ‘wholesale clients’ where financial product advice is provided to them. This means that most clients who receive advice about superannuation products are required to be treated as a ‘retail client’ (members of superannuation funds, employers and trustees of superannuation funds with net assets of less than \$10 million are treated as retail clients when they obtain advice about superannuation).

In addition, the boundaries between ‘factual information’, ‘general advice’ and ‘personal advice’ are unclear. While the recent FSR refinements have attempted to overcome some concerns from industry and consumers with the advice regime (such as refinement to Reg 7.1.33H allowing product issuers to discuss the features of their product without triggering the need for an AFSL goes some way to alleviating the concerns), there is still a need to give further consideration to the distinctions between factual information, general advice and personal advice. Despite some amendments having been made to ASIC Policy

Statement 175: *Licensing: Financial product advisers – Conduct and disclosure* [PS 175], there continues to be concern with some of the interpretations contained in the policy statement.

In practice, trustees are still often unable to provide education about superannuation without triggering the 'advice threshold' (Statement of Advice (SOA) requirements). Consequently, many trustees hold an AFSL. Greater clarity will promote a better understanding of the features of superannuation as well as deliver improved client relationships.

6.2 ABA comments on financial advice

It is the ABA's view that the advice regime should not apply to simple products or the provision of information on products that are well understood, even though some basic personal information may have been provided by the consumer to the financial services provider. The advice regime has unnecessarily restricted the provision of information and education on some financial products, where inadvertently the consumer may provide some basic personal information, and therefore any information provided to the consumer may be considered advice.

Section 766B of the Corporations Act defines 'financial product advice' as a recommendation or a statement of opinion, or a report of either of those things, that is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or could reasonably be regarded as being intended to have such an influence.

Subsection 766B(3) defines 'personal advice' as financial product advice that is given or directed to a person (including by electronic means) in circumstances where the provider of the advice has considered one or more of the person's objectives, financial situation and needs; or a reasonable person might expect the provider to have considered one or more of those matters. Subsection 766B(4) defines 'general advice' as any advice that is not 'personal advice'. Currently, the definition of financial product advice captures a number of communications between superannuation fund trustees and members.

The ABA considers that the scope of 'general advice' is too broad – there needs to be some proportionality for advice and greater recognition of the value of the provision of information on some financial products as improving the financial understanding of Australians. If the definitions of advice and/or applicable disclosure requirements were adjusted for some financial products, this would deliver better outcomes for both customers and industry. However, care should be taken to ensure that any exceptions are not cast too wide and unintentionally compromise the intent of the law in terms of consumer protection.

The ABA considers that where a client sits down and goes through a detailed financial plan with an adviser, taking into consideration the long-term investment needs and circumstances of the client, then clearly the advice regime should apply. However, we believe that the law should better accommodate the provision of information on some financial products, even where a consumer may provide some basic personal information. For example, while superannuation may not be considered a simple product, like a basic deposit product, some useful information is generic, even though it reflects a particular circumstance of an investor, or a group of investors, like preservation rules, salary sacrifice, investment options, insurance, and taxation issues. In this instance, the type of information can facilitate a greater understanding of superannuation, and not necessarily be product specific or investment strategy/fund manager specific.

Often members want information on the range of options they may have available within a fund. But as soon as the member provides a piece of information about their personal circumstances and the trustee responds by discussing various superannuation rules or investment options, the SOA requirements are triggered, even when the member is only seeking basic information, not a recommendation. While an increasing number of trustees are licensed to provide financial advice, a number of trustees are not licensed. This is an unfortunate consequence of the FSR regime, because advice on superannuation products is less available or less conveniently available for customers. Alternatively, those that have adopted an advice model must bear the additional compliance costs or pass these onto customers, placing upward pressure on the cost of superannuation, and more broadly the cost of financial advice.

The ABA's submission to the *Corporate and Financial Services Regulation Review Consultation Paper* contains a number of possible solutions, including:

- Adjusting the definition of personal advice in section 766(3);
- Introducing different rules for advice given in relation to "simple" and "complex" financial products, and consequently different SOA requirements;
- Making additional exceptions for forums and one-on-one discussions where tailored examples of product benefits or forecasts are provided to a retail investor; or product specific web calculators or risk profilers are made available to retail investors, which should not constitute advice.

To the extent that it is not clear within the current law, the ABA believes that an explicit amendment be made to the law to address the proportionality of advice. This will simplify the provision of financial advice and promote better outcomes for consumers and industry, including an effectively scalable spectrum of basic through to more complex "advice" about products and investment scenarios that is reflected more appropriately in the cost and availability of advice.

It is encouraging that the Government is acknowledging that there are high levels of confusion and inflexibility in the way licensees deal with legal interpretations regarding the advice regime. However, these matters are very difficult to resolve – and we believe that further consideration should be given through a working group with Treasury, ASIC, industry and consumer representatives to workshop a suitable solution.

The FSR refinement proposals, if implemented, will alter the regulatory requirements for advice, including the classification of who is a retail client for superannuation advice and potentially the manner in which the advice regime applies to superannuation products.

The ABA recommends that the law be amended to address proportionality of advice. Further consideration on how to better accommodate the provision of information on some financial products should be done through a working group.

The working group should give consideration to options, including:

- Amending the definition of financial advice to better accommodate the provision of information about the features of the superannuation fund; such as preservation rules, salary sacrifice investment options, insurance, and taxation issues; by superannuation trustees seeking to educate members.
- Refining the SOA requirements to allow limited advice on the range of options available within the fund. The ABA would not support a dilution of the SOA requirements in the circumstance where a product recommendation is made.
- Enabling the provision of product specific web calculators or risk profilers and other tools to assist educate consumers about superannuation.

Furthermore, the ABA's submission to the *Corporate and Financial Services Regulation Review Consultation Paper* supports extending the wholesale client definition to employers operating large businesses. 'Sophisticated employers' conducting a business, other than a small business as defined in section 761G, should be treated as 'wholesale'. In general these employers put out their superannuation to a tender process and the tenders contain far more information than that required in a SOA. This change should not disadvantage employees, as they will still receive disclosure documents commensurate with acquiring a financial product.

The ABA believes that market forces should dictate the fee structure for financial advice and not regulation. Furthermore, the ABA notes the emergence of fee-for-service models of advice. Whether a consumer chooses to pay commissions or fee-for-service should be at the discretion of the consumer, depending on what model suits their needs and financial situation. Therefore, it would be useful for there to be greater transparency around fee structures so that consumers can better understand fees and commissions and identify triggers that they may need to consider with respect to a particular investment.

6.2.1 Promoting forecasts

There are some advantages for consumers in providing benefit projections. However, this could create an expectation from consumers that the projection will be realised. Consumers tend not to understand the underlying assumptions and parameters used in projections and the impact that a small variation in an assumption can have on overall performance. Furthermore, assumptions may not be borne out in practice for an individual member, so disclaimers required would confuse and thereby limit the value of the projection. While the ABA considers that the current restrictions on forecasts are probably excessive, any form of standardisation is likely to cause difficulties.

Therefore, we suggest that the Government and industry work together on improving financial literacy and providing accessible tools (for example, product specific web calculators or risk profilers) to help people understand the drivers impacting their eventual retirement income and options available to them to improve their retirement income. In addition, the Government should also give further consideration to possible reforms that would permit superannuation funds to provide benefit projections to individual members on a standardised basis (for example, fee and performance neutral) as part of their annual reporting.

6.2.2 Encouraging consumers to seek advice

While consumer guides are useful in enhancing knowledge across the community, gaining access to professional financial advice is also important for consumers⁴. The financial services industry is constantly changing with the emergence of new products and services. Public policy on superannuation, social security and taxation as well as the legislative and regulatory regime is not well known or understood. It is important for Australians to be able to access information and advice that will help them better understand how to manage their superannuation and other private savings and better comprehend what may impact on their retirement incomes.

Currently there are anomalies in the system that do not encourage individuals to seek professional financial advice to assist them get the best out of their superannuation savings. For example, current taxation arrangements inhibit incentives for financial advice relating to superannuation, such as individuals being unable to obtain a tax rebate or deduction for advice on superannuation, while a deduction is available on non-superannuation investment advice.

⁴ [http://www.fido.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Super_Choices.pdf/\\$file/Super_Choices.pdf](http://www.fido.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Super_Choices.pdf/$file/Super_Choices.pdf)

Taxation arrangements also inhibit fee-for-service financial advice and the ability for employers to provide retirement income planning for their employees; for example, FBT is levied on the cost of an employer paying for advisory services.

The ABA recommends that disincentives for accessing financial advice should be removed through providing a tax rebate or deduction for those who seek professional financial advice in relation to superannuation and retirement income products. This approach would acknowledge through public policy the enduring importance of the service of financial advice.

7. Member investment choice

The legislative requirements relating to advice and market conduct and disclosure is administered by ASIC. All trustees are required to only act on a member's investment choices after having disclosed the information reasonably necessary for the fund member to understand the effect and risk of the strategy.

Some superannuation funds allow members to instruct the trustee to follow an investment strategy. Under the SIS Act, trustees that offer investment choice to members must balance the objective of providing choice while ensuring they invest fund assets in a prudent and responsible manner. Neither the legislation nor APRA prescribes any investment limits.

In March 2006, APRA issued Superannuation Circular II.D.1 in relation to advice about choice of investment within an APRA-regulated superannuation fund. It is APRA's view that the SIS Act requires that the trustee must properly develop each investment strategy offered and provide the necessary information about each, in accordance with the SIS Act and Regulations, and cannot abrogate responsibility in relation to investment strategies by requiring members to seek their own financial advice⁵.

It is the ABA's view that, despite APRA's efforts to revise the draft circular following industry consultation, there remains ambiguity in the interpretation regarding trustee obligations and members' responsibilities. This ambiguity is largely due to uncertainty with the law, which gives rise to a difference in interpretation between APRA and industry as to the operation of sections 52(4) and 52(2)(f) of the SIS Act. We believe that APRA's interpretation would effectively extend trustee responsibility to individual member investment choice and ignore the availability of financial advice in member investment choice.

The ABA believes that the regulatory arrangements for investment choice, in both superannuation and non-superannuation products, are essentially disclosure based. We are concerned that the interpretation of the law as contained in the circular would in effect extend trustees' obligations to individual members' investment choice. The formulation of the investment strategy(ies) for the superannuation fund is the responsibility of the trustee; however, under a member investment choice regime the selection of investments within a strategy is the responsibility of the member. Superannuation is a personal investment and therefore investment choice is the member's responsibility. Advice and disclosure requirements should be consistent with the provisions of the Corporations Act and the trustee obligations and authorisations under their AFSL (if any).

⁵ APRA's submission to the Parliamentary Joint Committee on Corporations and Financial Services' Inquiry into the structure and operation of the superannuation industry. September 2006. Page 7.

The ABA notes that the Investment and Financial Services Association (IFSA) has provided feedback on particular concerns from the financial services industry and we endorse IFSA's comments. The ABA supports IFSA's recommendation that the Government should amend the law to clarify the operation of these provisions of the law.

The ABA recommends that section 52(4), 58 and Reg 4.02 of the SIS Act should be amended to clarify the duties of trustees of superannuation funds offering member investment choice. Duties are to: formulate and document investment strategy(s); manage those investment strategy(s) in a prudent manner; and acquire, redeem and report on investments. Responsibility for investment selection within the strategies offered by the trustee is that of the member.

8. Self managed superannuation funds

The growth in Self Managed Superannuation Funds (SMSFs) over the past decade has been significant, albeit less significant over more recent years. Reasons for the increase in SMSFs are generally because individuals want more control and flexibility with their superannuation, self-employed/business owners wanted to include the real property of their business as assets in their fund, investors want to take advantage of tax and social security strategies available to SMSFs (now no longer available), and it is perceived that there are lower fees and better returns with SMSFs.

The ABA does not believe that requiring all trustees of superannuation funds to be listed public companies is necessary. This would in effect do away with the SMSF sector, as most SMSFs would need to be wound up. However, the ABA believes that there should be tighter regulation of the SMSF sector, to remove regulatory arbitrage and improve consumer protections.

Currently, there are differences between how managed investments, superannuation and SMSFs are licensed and regulated. Unlike managed investments where licensed financial advisers provide advice to consumers, unlicensed practitioners, such as accountants, often promote SMSFs.

While accountants have a limited exemption from the licensing provisions of the Corporations Act for their actions regarding establishing a SMSF, this exemption does not extend to the provision of financial advice. The exemption stipulates that advice given by a registered tax agent is not financial product advice if the advice is given in the ordinary course of activities and is reasonably regarded as a necessary part of those activities. However, in most instances, where an accountant suggests that a client consolidate other superannuation balances into a SMSF, then the exemption would not apply.

While SMSFs provide an alternative superannuation vehicle for some people (such as individuals that have the time and skill to manage their own superannuation savings and meet the trustee obligations contained in the SIS Act), those people that seek 'advice' on SMSFs may not have the same consumer protections awarded to those people that seek 'advice' on other managed investments or superannuation vehicles (e.g. training and competence standards set out in PS 146 may not be met).

Essentially, SMSFs are a product designed to hold financial assets for retirement, therefore regulation should be product neutral. (This does not necessarily imply that regulation of SMSFs should transfer from the ATO to APRA.) This approach will ensure that the prudential and conduct of business framework (including sound investment strategy and quality of financial advice) is maintained and SMSFs, as an alternative superannuation vehicle, can continue to grow as a viable savings vehicle for retirement. Given the rapid growth of these superannuation vehicles over recent years, the ABA suggests that the Government conduct a review of the regulatory treatment for SMSFs to ensure funds are prudentially and safely invested.

Furthermore, the pending changes to the superannuation system will highlight the importance of compliance in making sure that SMSFs do not abuse the concessions afforded superannuation; for example, currently a significant level of voluntary superannuation contributions are made to SMSFs. The pending changes also provide an opportunity to reduce unnecessary compliance burdens; for example, redesign ATO lodgement forms. It is important for trustees of SMSFs to be aware of their responsibilities and make sure that they comply with their legal obligations.

Nevertheless, the ABA wonders whether the growth in SMSFs will be sustained under the new tax treatment for superannuation, given that the SMSF sector has been to a certain extent driven by tax and social security strategies, which are now no longer available.

The ABA recommends that the Government should conduct a review of the SMSF sector to ensure the ongoing efficient, effective and safe regulatory structure for the management of SMSFs. A review should focus on administration and regulation of SMSFs, consumer protection for investors in SMSFs, and especially the level of compliance by SMSFs with superannuation law and tax agents and accountants with financial services law.

9. Cost of compliance

It is the ABA's view that regulation of banking and other financial services including superannuation, should seek to minimise the compliance burden placed on entities. Regulators should be committed to supervising the superannuation industry as efficiently and effectively as possible.

Trustees and funds have considerable compliance costs placed on them due to both the SIS Act and Corporations Act.

The ABA has made a number of representations to Government and regulators on the cost of compliance with financial services regulation. The ABA has some data on direct compliance cost estimates of ASIC licensing and FSR implementation, we would be pleased to provide data to the Committee upon request. However, at this stage, we do not have data on direct compliance cost estimates for APRA licensing and superannuation reforms.

The main ways to reduce cost of compliance is to eliminate unnecessary regulation, remove legislative complexity and reduce regulatory inconsistency and/or duplication through assessment of regulation.

In the ABA's submission to the Regulation Taskforce we highlighted the need for more comprehensive and consistent assessment of business regulation and regular monitoring of regulatory costs. The costs of Australian regulation should be benchmarked against international best practice.

As such, we strongly endorse a number of the recommendations of the Regulation Taskforce, including:

- Regulators should develop a wider range of performance indicators for annual reporting (Rec 7.16)
- There should be provision for merit review of any administrative decisions that can significantly affect the interests of individuals or enterprises (Rec 7.18)

- Unless there are exceptional circumstances, a regulatory proposal with material business impacts should not proceed to Cabinet or other decision-maker unless it has complied with the Government's Regulatory Impact Statement (RIS) requirements (Rec 7.9)⁶
- Rigorous cost-benefit analysis be employed in regulation making, such as analysis should be used to compare different regulatory options, and should incorporate adequate risk analysis (Rec 7.2)

In the ABA's submission to the *Corporate and Financial Services Regulation Review Consultation Paper* we also provide comments on harmonising regulation; for example, the breach reporting requirements of ASIC and APRA. We support the concept of consistency in breach reporting arrangements, i.e. what must be reported and when it must be reported. However, there should be recognition of the different regulatory objectives and supervisory methods of the two regulators. Therefore, we suggest that a section 912D-type regime be extended to APRA regulated superannuation entity licensing, where requirements align based on significance and materiality. It would be useful for ASIC and APRA to provide procedural guidelines or a checklist.

In addition, we suggest the following amendments:

- Introduce a materiality test for breaches that must be notified to APRA. The materiality test should be broadly consistent with the ASIC administered definition of 'significant', but with a prudential emphasis e.g. amend the section 912D criteria as follows:
 - i. the number or frequency of similar previous breaches;
 - ii. the impact of the breach or likely breach on the licensee's ability to meet its obligations to depositors/policyholders/members etc;
 - iii. the extent to which the breach or likely breach indicates that the licensee's arrangements to ensure compliance with those obligations is inadequate;
 - iv. the actual or potential financial loss to depositors/policyholders/members etc of the licensee, or the licensee itself, arising from the breach or likely breach;
 - v. any other matters prescribed by regulations made for the purposes of this paragraph.
- Amend the timeframe for reporting to 10 business days.

Breaches relating to minimum solvency or capital adequacy should continue to require 'immediate', i.e. as soon as practical, notification to APRA to assist in maintaining financial system stability.

In addition, we are of the view that documents produced for the purposes of complying with these requirements should be made confidential and subject to privilege to assist the free flow of information between industry and the regulators.

The ABA is pleased that the Government has indicated that it will address inconsistencies between ASIC and APRA breach reporting.

⁶ Grounds for a RIS to be deemed 'inadequate' should include: failure to document relevant existing regulations at all levels of government and explain why they do not suffice; inadequate cost-benefit analysis of regulatory options; failure to quantify compliance costs of options; inadequate risk analysis and assessment; and failure to document directly relevant international standards and, where a proposed regulation differs from them, to identify the implications and fully justify this variation. (Rec 7.8)

Also in the ABA's submission to the *Corporate and Financial Services Regulation Review Consultation Paper* we provide comments on product rationalisation. We strongly support the introduction of a simplified mechanism to allow financial product issuers (including superannuation, managed investments and life insurance products) to be able to restructure and rationalise outdated products. It is important that the law enables the financial services industry to more easily update the technology underpinning financial products and to introduce a simplified and sustainable process to enable customers to be shifted from legacy products to more suitable modern products, without financial detriment to the customer. The maintenance of legacy products is expensive and inefficient.

The benefits of product rationalisation include enhanced competitiveness; improved disclosure; improved safety; reduced operational risk; access to innovative investment opportunities; and reduced costs.

The ABA believes it is necessary for changes to be made so that FSR can more adequately deal with legacy products. We suggest amendments to the Corporations Act and other relevant financial services laws (e.g. SIS Act, Life Insurance Act and Insurance Contracts Act) to allow members of a legacy product to be transferred to a new product, provided the member does not suffer any detriment, or provided they are compensated appropriately. Capital gains tax rollover relief should be available to ensure tax neutrality.

It is also necessary for ASIC to provide interim relief for legacy products, as the costs associated with maintaining these products under the new FSR regime are significant. The financial products to which product rationalisation is primarily needed are managed investment schemes, superannuation funds and life insurance products.

The ABA supports the product rationalisation process outlined by the Investment and Financial Services Association (IFSA).

The ABA believes that the Government should develop performance benchmarks for measuring the performance of financial services regulation. Criteria should be developed by which the process of developing new regulations and reviewing existing regulations as well as the process of designing and implementing new regulation can be benchmarked. The identification of a framework and reporting indicators to assist government and regulators should be done in consultation with industry.

10. Financial advertising

Superannuation trustees must adhere to the 'sole purpose test' contained in section 62 of the SIS Act. Essentially, the object of the sole purpose test is to ensure that superannuation funds are maintained for the purpose of providing benefits to members upon reaching preservation age and retirement (or for a member's dependants if a member dies before retirement). While advertising is not prohibited under the sole purpose test, a trustee must be able to justify advertising or marketing. Trustees have duties to members of the fund and therefore a trustee must demonstrate a benefit of advertising and marketing for the fund and its existing members.

There are a number of provisions in the Corporations Act which regulate financial advertising, including section 1041E (misleading and false statements) and section 1041F (inducing persons to deal). Furthermore, pursuant to section 991A, a licensee must not engage in unconscionable conduct.

In particular, the law prohibits the making or publishing of a statement, promise or forecast if the person knows, or is reckless as to whether the statement is misleading, false or deceptive. Terms such as "not for profit" and "all profits go to members", are not defined in the Corporations Act. Where forecasts are made, a trustee must demonstrate the grounds for such a statement. Where other statements are made, such as relating to profitability, performance, fee structures, and so on, these statements must not be misleading.

Making sure that consumers understand superannuation should be managed through a combination of product disclosure, financial advice provided by licensed advisers, financial literacy materials, informing existing and potential members of the benefits through advertising, and, where warranted, consumer protection and enforcement action by the regulator.

It should be made clear that advertising a fund to attract new members or encourage existing members to increase their contributions is consistent with the sole purpose test. Obviously, existing rules about misleading, false or deceptive statements will apply to advertising, marketing and promotion of the superannuation fund. Therefore, superannuation funds should be aware of the statements made about the fund, such as the description of the nature of the fund and the allocation of profits, in the context of their legal obligations.

Some clarity as to terms used to describe different superannuation fund businesses within the industry may be useful in assisting consumers better understand the superannuation industry – this is particularly important in a 'Super Choice' environment.

The ABA believes that if a superannuation trustee breaches their legal obligations including misleading consumers (existing or potential members) through advertising and marketing, regulatory action should be taken.

11. Funding arrangements for prudential regulation

Currently banks and their wealth management businesses pay significant levies. While the ABA acknowledges that both ASIC and APRA need adequate funding to make sure they have adequate staff and resources to administer the law, we are concerned with the cost structures of the regulators.

The ABA believes that the Government should continue to give consideration to appropriate funding arrangements, including consideration of actual costs in supervising entities. Further consultation on levy structures will be required.

12. Capital requirements

Capital requirements under the SIS Act apply only to public offer superannuation funds. APRA states that capital requirements [net tangible assets requirements] provide some financial resources to act as a buffer against risk; evidence a commitment on the part of a trustee to its superannuation business; and act as an incentive to the trustee to manage the entity well⁷.

Superannuation fund members should have a level of protection afforded by capital. Capital requirements are part of ensuring the safety of superannuation, along with licensing, risk management, disclosure and recourse to funds and resources. It is important that consumers have confidence that their superannuation savings are being held in a prudent manner, just as their deposits are held by banks and other authorised deposit taking institutions.

⁷ Superannuation Guidance Note SGN 150.1. *Capital requirements – net tangible assets*. July 2004. p5. <http://www.apra.gov.au/Superannuation/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=7366>

However, uniform capital requirements for all trustees is inconsistent with domestic and international practice. The Basel II framework is a minimum standard for capital adequacy that seeks to align regulatory capital requirement more closely to the underlying risks that banks face. The framework encourages banks to identify risks and improve their ability to manage those risks, and therefore is intended to be flexible and better able to evolve with changes in markets and risk management practices.

Prudential regulation of superannuation should make sure that each fund and each entity has in place adequate operational functions to manage their risks and ready access to resources at times of stress. It should be noted that subsidiaries of banks that offer superannuation products are required to take account of operational risk when calculating regulatory capital. In practice, every fund and entity will have different levels of risk and the imposition of uniform capital requirements may be unduly burdensome.

Notwithstanding, we consider that it is reasonable for some funds, in addition to public offer superannuation funds, to maintain capital commensurate with their level of risk. Universal capital requirements will ensure that Australians have confidence in the safety of their superannuation savings and that the same rules applicable to public offer funds are translated to other superannuation funds.

The ABA believes that the law should be amended to ensure that complying APRA regulated superannuation funds take account of operational risk and maintain capital reflecting the level of risk of the fund and entity. However, uniform capital requirements may be unduly burdensome. Furthermore, as part of the product disclosure requirements contained in the Corporations Act, details of operational, institutional, governance, investment and other risks should be clearly disclosed to members, including operational functions such as outsourcing.

13. Concluding remarks

The ABA believes financial independence, financial security and a better lifestyle in retirement should be attainable for Australians. It will take a multi-dimensional approach from the Government, financial services industry and the community to ensure that all Australians take responsibility for their savings early so they are well prepared for retirement. Such a multi-dimensional approach should involve strategies to promote confidence in the superannuation and retirement incomes system by addressing the broad policy principles of *simplicity*, *flexibility*, *adequacy* and *literacy*, as well as deliver other social and economic benefits.

Currently there remain many challenges for all the participants in the regulatory process. The challenge for superannuation trustees in implementing good regulation is in understanding the myriad of obligations across various statutes and regulators. The challenge for legislators and governments in introducing good regulation is to balance the public interest with the realities of the compliance burden for financial services providers. The challenge for regulators in administering regulation is balancing the need to be consultative with industry (in order to develop sound policy) and the reality of their enforcement role.

Superannuation regulation should provide adequate consumer protections without imposing unnecessary compliance costs on providers as well as provide incentives to encourage Australians to save and plan for their future without imposing unnecessary restrictions on compulsory and voluntary contributions.