



AUSTRALIAN BANKERS' ASSOCIATION INC.

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Senator Grant Chapman
Chair, Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
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Dear Senator Chapman,

On 7 March 2007, the Australian Bankers' Association (ABA) was due to appear before the Parliamentary Joint Committee on Corporations and Financial Services to give testimony to the inquiry into the structure and operation of the superannuation industry. Unfortunately we were unable to attend. Please find following supplementary comments that we hope are useful for deliberation by the Committee.

1. Opening remarks

The ABA strongly supports the superannuation and retirement incomes policy principles of *simplicity, flexibility, adequacy* and *literacy*. The ABA has advocated these policy principles for some time.

The Federal Government's 'Simpler Super Package' addresses these principles and is the most significant change to superannuation and retirement incomes policy since the introduction of compulsory superannuation. The changes should streamline and simplify the superannuation system for the benefit of all.

However, it is important that the changes also foster competition and avoid economic distortions for savings and investment products. The changes to superannuation, taxation and social security legislation must effectively deliver the objectives of the proposals and maximise the opportunity to reduce administration burdens and compliance costs for industry. To this end, the transitional arrangements will need to acknowledge the massive impact of the changes on systems, policies, procedures and processes, particularly as we creep closer to the implementation date.

There have been substantial (almost constant) changes in the superannuation industry over the last five years. These changes have been driven not just by reforms to public policy, but also to regulation. The superannuation industry has transformed through new regulations relating to licensing, conduct and disclosure obligations, due to FSR reforms and amendments to the SIS Act.

The ABA's position on superannuation and retirement incomes policy is as follows:

- (1) *Sustaining the 'three pillars policy'*: The ABA supports Australia's stable and sustainable three pillars retirement income system – age pension, compulsory superannuation contributions and private savings.
- (2) *Simplifying retirement incomes*: The ABA believes that strategies, tools and products must suit the circumstances and needs of individuals and be flexible to change as retirees' needs and circumstances change.
- (3) *Increasing flexibility of superannuation*: 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. The superannuation system needs to balance concessionality and accessibility and provide incentives to promote the attractiveness of superannuation and private savings.
- (4) *Improving adequacy of superannuation*: Generally, Australians are still not planning early enough, or saving enough, for their retirement. It is vital that we send strong messages about the long-term value of savings, increasing private savings and lifting voluntary contributions.
- (5) *Building literacy in savings strategies*: Low financial competence and understanding make it more difficult for consumers to plan and save effectively for their retirement. The ABA believes that the Government and industry need to work together, such as through the Financial Literacy Foundation, to assist Australians gain the financial capabilities to better manage their finances.
- (6) *Promoting incentives to save and plan*: The ABA believes reducing complexity and increasing flexibility with the superannuation system go a long way to removing barriers to early saving and retirement planning, but targeted messages need to encourage greater private savings and voluntary contributions by getting people to think about the value of long-term wealth accumulation.
- (7) *Encouraging private savings*: Changes to the superannuation system will go some way to encouraging diversified pre-retirement savings and post-retirement incomes. The ABA suggests that the Government could also consider assisting Australians deal with unforeseen circumstances by addressing current differences in tax treatment across savings products and introducing rebates for people who invest in life insurance or other risk products.

The ABA has recently made a submission to the Government's *Streamlining Prudential Regulation: Response to 'Rethinking Regulation' Proposals Paper*, which contains a number of proposals that seek to streamline prudential regulation without reducing confidence in the regulatory system. While it is pleasing that the Government has given considered thought to some of the concerns raised by industry with the Regulation Taskforce, many of these proposals represent a significant shift more broadly in prudential policy and regulation. We are anxious to work closely with the Government as it consults further with industry about the ramifications of some of these proposals.

The ABA is also currently working with the Government on implementing refinements to financial services regulation (FSR). We made substantive comments to the Government's *Corporate and Financial Services Regulation Review Proposals Paper*, which contains proposals that address concerns with unintended and unnecessarily complex consequences arising from FSR and other amendments to the Corporations Act. It is important that regulation promotes efficient and effective industry operations and provides adequate investor protections.

A number of the proposals in these papers would have a substantial impact on the structure and operation of the superannuation industry. It is timely that the Committee is looking at superannuation, but we also acknowledge that there well could be more changes in the pipeline. The ABA would be happy to provide the Committee with copies of our submissions to these reviews upon request.

2. Specific comments

In our initial submission to the Committee, the ABA has made a number of specific comments about the structure and operation of the superannuation industry, including regulation of superannuation and financial services, regulation of financial advice, cost of compliance and emergence of self-managed superannuation funds. Following are additional comments on the definition of financial advice; financial literacy, education and advice; and regulation of superannuation.

2.1 Definition of financial advice

The ABA has made a submission to the *Corporate and Financial Services Regulation Review Proposals Paper* outlining our concerns with the way the law currently defines financial product advice and the consequences of this definition for the associated compliance costs borne by industry and consumers. 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 financial advice regime, including ASIC guidance.

The ABA has concerns with the distinction between 'factual information', 'general advice' and 'personal advice'. The breadth of these definitions has had a perverse impact on industry and consumers due to the problematic manner in which these definitions capture certain activities. We believe that greater clarity will improve client relationships, reduce unnecessary process and documentation and will go towards improving accessibility and reducing the cost of financial advice.

Section 766B(3)(a) of the Corporations Act states that personal advice is triggered when a financial service provider knows a client's objectives, financial situation or needs and considers that information in recommending or selling a financial product. Section 766B(4) defines general advice as financial product advice that is not personal advice.

The advice obligations under the law are time consuming and expensive¹. While such obligations may be suited to regulate the activity of financial planning, where a client receives considered advice on a long-term investment strategy, FSR applies more broadly to even simple products and simple advisory scenarios. This has resulted in some financial service providers adopting a 'no advice' model, which means that helpful information from, for example, bank staff, is not as accessible for customers, because depending on how it is worded and the situation in which it is provided, it could constitute advice.

Similarly, some superannuation trustees do not provide information to their members, because they hold personal information about the member and so basic information provided could constitute advice.

¹ The obligations associated with the trigger of financial advice include documentation (e.g. Statements of Advice (SOAs) or Records of Advice (ROAs), Financial Services Guides (FSG) and Product Disclosure Statements (PDSs) where applicable, or alternative disclosures), training and other compliance factors.

In these instances, the consumer misses out on valuable information. The advice regime has unnecessarily restricted the provision of information and education on some financial products. In situations where the consumer provides some basic personal information (inadvertently or otherwise), under the current regime, any information subsequently provided to the consumer may be considered 'advice' and therefore triggers a range of disclosure and other compliance obligations. We are also aware that consumers have expressed dissatisfaction with the advice regime. Some have indicated frustration with limitations in receiving useful information on simple products; whereas others have been annoyed by the process and substantial documentation associated with the provision of simple advice.

It is the ABA's view that the scope of 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. We consider that if the definitions of financial advice and applicable disclosure requirements were adjusted, this would deliver better outcomes for both customers and industry.

Summary of ABA's position on the definition of financial advice

1. The financial advice regime should not apply to 'simple products'. These products are generally widely understood and less risky than other financial products, for example, basic deposit products, general insurance products, non-cash payment facilities and cash management trusts.

Simple products should have basic and consistent disclosures – we note that FSR refinements have acknowledged that the advice regime has imposed stringent and preventative obligations on these products and therefore have attempted to alleviate such obligations, but these refinements have also resulted in different disclosures and other requirements for these products.

Financial service providers dealing in these products would still be captured by the law and subject to the general licence obligations, but they would not be captured by the advice regime. In addition, the Code of Banking Practice provides assurances that banks would "promote better informed decisions" (clause 2.1).

2. The definition of financial advice should be amended and refinements made to the SOA requirements. Currently the law is deficient in acknowledging the circumstances in which simple advice may be provided which does not require lengthy disclosures. Information can facilitate a greater understanding of financial products, such as superannuation, and not necessarily be product specific or investment strategy/fund manager specific.

Recommendation: The ABA recommends that Treasury establish a working group with industry and consumer representatives to 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.

The ABA is pleased that Treasury has established a working group to give closer consideration to refining the scope of the advice regime. The ABA is working with Treasury and ASIC on how we can further refine the law and regulation to better balance the needs of consumers and the costs for industry.

2.2 Financial literacy, education and advice

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. For example, the financial services industry is constantly changing with the emergence of new products and services. Superannuation, social security and tax rules have undergone massive changes over recent years. Consumers need to better understand their superannuation, retirement income and pre-retirement investment options – especially given some of the challenges Australia will face over the next 40 years as set out in the Intergenerational Report.

The ABA's *Broadening Financial Understanding* Financial Literacy Program has developed hardcopy and electronic materials to assist consumers better understand superannuation and more broadly how to manage their finances and savings. We have partnered with other industry associations and with government/regulators, but also importantly with community and consumer groups to develop, deliver and distribute financial literacy materials.

The ABA is also a partner with the Federal Government's Financial Literacy Foundation. It is our view that efforts are more successful when government, industry and consumer groups work together to target information to those who need it and make it available when they need it. The superannuation system is not well understood and it is our view that the new superannuation rules will require a coordinated effort to educate Australians about the changes and how they can get the best out of their superannuation and private savings.

Recommendation: The Federal Government and industry, through the Financial Literacy Foundation, should work in partnership to ensure that all Australians have access to information on the new superannuation rule changes, effective after 1 July 2007.

While 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. Financial planning will likely be less orientated towards the taxation and regulation surrounding superannuation, but 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.

Currently there are anomalies and inconsistencies in the system that do not encourage individuals to seek professional financial advice to assist them get the best out of their superannuation investments. Current taxation arrangements inhibit incentives for financial advice relating to superannuation; for example, individuals are unable to claim a tax deduction for investment advice obtained within superannuation, while a tax deduction is available for individuals that seek investment advice for DIY superannuation or non-superannuation products. Taxation arrangements also inhibit upfront fee-for-service financial advice relating to the initial establishment of investments, whereas ongoing financial advice on individual financial affairs is tax deductible. Taxation arrangements also

restrict employers providing retirement income planning for their employees, as FBT is levied on the cost of an employer paying for advisory services.

It is the ABA's view that how consumers want to pay for financial advice should evolve through market practices. Some consumers may want to pay commissions and defer the cost of advice, whereas others may want to pay an upfront fee-for-service. It is important that fee disclosures enable consumers to make informed decisions about fees and commissions, but regulation should not impose restrictions that may have adverse and unintended consequences for industry and consumers. In this respect, consumer choice should not be artificially influenced by taxation and other regulatory restrictions.

Recommendation: The ABA recommends that disincentives for accessing financial advice should be removed through providing a tax rebate or tax 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.

2.3 Regulation of superannuation

The Wallis inquiry established a regulatory system which some refer to as the 'twin peaks' model. The Government made a policy decision to establish ASIC as the conduct of business regulator and APRA as the prudential regulator.

Superannuation trustees and funds may be subject to provisions relating to responsible entities and managed investment schemes under the Corporations Act. In the last couple of years the SIS Act was amended to require superannuation trustees to be licensed and superannuation funds to be registered with APRA.

The Government made a policy decision that superannuation should be prudentially regulated, amongst other reasons, due to the compulsory nature of superannuation savings. (The ABA notes that other prudentially regulated entities, such as authorised deposit-taking institutions, have been subject to 'dual regulation' for some time.)

It is important that APRA and ASIC work in a co-operative, consistent and transparent manner to ensure that those entities that are regulated by both APRA and ASIC are not subject to unnecessary regulatory burden and compliance costs. For example, the ABA has made a number of comments on the breach reporting obligations in the Corporations Act and the prudential Acts and support harmonising breach reporting requirements as much as possible.

The ABA believes that it is important to make sure that the regulatory structure does not impose unnecessary costs or complexities. It is important to ensure that prudential controls do not unduly restrict superannuation funds. For example, prudential oversight of superannuation funds should not prescribe investment rules, as this would lead to more conservative investment strategies and ultimately reduced retirement benefits. APRA should not be able to exercise its directions power, unless of course the trustee has not met their legal obligations.

In addition to the regulatory framework administered by APRA and ASIC, self-managed superannuation funds (SMSFs) are regulated by the ATO. The emergence of SMSFs and their increasing popularity means that the ATO is increasingly responsible for regulating superannuation. The ABA is concerned with:

- ATO's ability to effectively administer the law with respect to the many SMSFs in the marketplace; and

- Accountants and the distinction between tax advice and the provision of financial advice relating to establishing and managing a SMSF.

Recommendation: The ABA recommends that the Government conduct a review of the regulatory framework for superannuation including examination of the:

- Role of APRA, ASIC and ATO with a view to removing unnecessary duplication and inconsistencies;
- Use, promotion and regulation of SMSFs with a view to ensuring compliance with the law by trustees of SMSFs and accountants giving advice on the structure of superannuation; the quality of financial advice with regards to SMSFs and adequacy of consumer protection; and regulatory neutrality of SMSFs; and
- Separation of prudential and retirement income provisions of the SIS Act.

3. Concluding comments

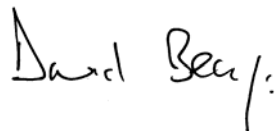
Some commentators say that the combination of prudential and retirement income provisions would not have occurred if introduced after Wallis. Some commentators also say that if we had it all to do again we might not end up with the regulatory structure we have today.

There are a number of challenges in the superannuation system:

- Superannuation trustees: there are challenges in implementing good regulation and understanding the myriad of obligations across various statutes and regulators.
- Legislators and governments: there are challenges in introducing good regulation and balancing the public interest with the realities of the regulatory burden and compliance costs for financial service providers.
- Regulators: there are challenges in administering regulation and balancing the need to be consultative with industry (in order to develop sound policy) and the reality of their enforcement role.

The ABA hopes that our comments are useful. If you would like to discuss any of the issues raised in our submission further, please contact me or Diane Tate, Director, Corporate & Consumer Policy on (02) 8298 0410: dtate@bankers.asn.au.

Yours sincerely



David Bell