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Dr Bachelard
The Secretary
Senate Economics Legislation Committee
Room SG.64
Parliament House
CANBERRA ACT 2600

Dear Dr Bachelard

Superannuation Safety Amendment Bill 2003

IFSA welcomes the opportunity to respond to the invitation by the Senate Economics Legislation Committee on 11 December 2003 to contribute to the Committee's inquiry and make a submission on the Superannuation Safety Amendment Bill 2003 ('**Bill**').

IFSA strongly supports the purpose of the proposed legislation and acknowledges the need to ensure that superannuation savings have the benefit of a strong regulatory regime that seeks to ensure superannuation trustees are aware of their responsibilities to members, their obligations under the law, are appropriately qualified and are fit and proper persons. The proposed trustee licensing and superannuation fund registration regimes are, we believe, essential structural elements for a strong regulatory regime.

IFSA has previously provided comments in consultation with Government officials on exposure drafts of the Bill. Those comments have resulted in a number of changes and refinements to provisions of the Bill. The following submission provides our general comments on the broad policy basis for Government regulatory reforms in the financial services industry, and specific issues/comments/recommendations on certain provisions in the Bill. The comments are of a technical and practical nature and should in no way be seen a fundamental criticism of the overall package.

General Comments

IFSA considers that the framework for the new trustee licensing and superannuation entity registration regimes to be sound. However, we maintain that unless there is good reason for differentiation, the proposed changes by the Bill should be consistent with similar requirements in the Corporations Act 2001 ('**Corporations Act**') that

were introduced by the Managed Investments Act ('**MIA**') and the Financial Services Reform Act ('**FSRA**').

Superannuation and non-superannuation managed investment laws have similar objectives. Consistency in regulatory requirements and administration will help to lower risk and reduce implementation costs for the industry. The potential for regulatory duplication and overlap be avoided. Government must ensure that the same standards for trustees are applied regardless of whether it is a superannuation investment or non-superannuation investment management activity. The proposed licensing and registration requirements will provide a foundation for investor confidence in the regulation and management of superannuation savings.

In considering the proposed amendments, any proposition that trustee duties under the superannuation and managed investment regimes are in some way different must be dismissed. As stated at paragraph 3.9 of the Explanatory Memorandum to the Bill, "Superannuation is essentially a managed investment with special characteristics including compulsion, preservation rules that restrict access until retirement, taxation advantages and limited choice and portability".

The Explanatory Memorandum to the Bill also acknowledges that the responsibility of APRA, as a prudential regulator, is to monitor superannuation savings to ensure they are prudently invested and managed (paragraph 3.11). IFSA is mindful of the need to guard against overlapping and duplicative legislative requirements resulting in confusion and additional costs to industry and members. Requirements of the Bill should seek to ensure that APRA and ASIC work in a complementary fashion given their different mandates. To do otherwise would undermine the significant structural legislative achievements resulting from the implementation of Wallis Inquiry recommendations.

It is of concern to IFSA where statements are made that would lead one to understand that accountability for trustees of superannuation entities is less than that of the responsible entity of a managed investments scheme. We note the statement at paragraph 3.37 of the Explanatory Memorandum to the Bill that "a trustee of an employer sponsored fund with significant functions outsourced will not be expected to demonstrate the same level of detail in its risk management strategy ('**RMS**') and risk management plan ('**RMP**') as the trustee of a public offer entity". The fact is that both public offer entities and employer-sponsored funds may outsource significant functions and, there should be no difference in the applicable standards.

It is also important to ensure that the proposed regime is flexible enough to encompass the risk management structures that currently exist across conglomerates, particularly conglomerates with a life office. Life Offices should be able to meet the risk management requirements that currently exist through the APRA PAIRS processes. That is, it should not be necessary to duplicate these requirements.

Issues/Comments/Recommendations

Commencement – Clauses 2 and 10

IFSA notes and supports the proposed 2 year licensing transitional period. However, given the importance of the regulations to the implementation of these measures, the date of commencement should be the later of the date fixed by Proclamation, the date of enactment of the Bill, and the passing of the regulations.

Classes of Licence –section 29B

IFSA notes that APRA will have an ability to issue different classes of licence and provides for two broad classes i.e. public offer entities and non public offer entities. IFSA supports the ability of a trustee under the proposed law to hold a single licence that enables it to operate a number of classes of registrable superannuation entity ('**RSE**') – section 29B(5).

Period for deciding applications from existing trustees – section 29CB

IFSA notes that in many cases, the trustee of a public offer superannuation entity will also be the responsible entity of a registered managed investment scheme and will hold an Australian Financial Services Licence ('**AFSL**') authorising it to operate the scheme. To avoid duplication in relation to applications for a RSE licence, the Bill should provide for the streamlining of licences for approved trustees where an entity is currently the trustee of a RSE and holds an AFSL.

A entity making a streamlined application to APRA should be required to either:

- provide to APRA a copy of their AFSL licence and their application to ASIC for their AFSL; or

- confirm their approved trustee status. Approved trustees are currently subject to regular oversight and review through mechanisms such as provision of Prudential Management Certificates, supervisory visits by APRA, and regular prudential reviews by APRA.

While the Bill differentiates between existing trustees and new trustees for application purposes it does not provide for streamlining of applications. IFSA members consider this to be a failing in the transitional arrangements.

Grant of RSE Licences – s29D

Section 29D(1)(a) should be amended to impose a positive test requiring APRA to 'have reason to believe' that an applicant 'will comply' instead of the current provision which requires that APRA have 'no reason to believe' and that 'they will fail to comply'. IFSA considers that a positive test provides APRA with greater flexibility in its consideration of applications.

Capital Requirements – section 29DA

IFSA notes that capital requirements are to apply only to corporate trustees. Given that capital requirements are intended to apply to ensure that an entity has the financial capacity to ensure that operational functions are performed, IFSA questions the limitation of capital requirements only to corporate trustees.

IFSA notes that capital requirements imposed on the responsible entities of managed investment schemes under the Corporations Act may be satisfied in a number of ways, including the outsourcing of the custodial function to an entity that satisfies the capital requirements.

Trustee Licence Numbers – section 29DB

In order to minimize the costs to trustees we suggest that the ABN number, where available, should be able to be used as the trustee licence number in the same way that it is able to be used with the Australian Registered Scheme Number (Corporations Regulation 5C.1.03).

IFSA is also concerned with how the new trustee licence number will work with the SFN currently held by all funds, and the Superannuation Product Identification Number (SPIN) held for all products. IFSA questions whether all these numbers are needed.

Industry is concerned about the proliferation of numbers that may be confusing to consumers and, urge cooperation between regulators for a simplified, and where possible, a single numbering system.

Documents required to bear licence/registration numbers – sections 29DC, 29MB

We are concerned with sections 29DC and 29MB of the Bill that require trustees to cite RSE licence and the RSE registration numbers on all documents that relate to the entity. Due to difficulties identified by IFSA, ASIC provided relief during the transition period from the requirement to cite AFSL numbers in disclosure documents that were prepared before the licensee received its AFSL. While we note that it is proposed to provide APRA with a power to exclude a particular document from compliance with this requirement, IFSA considers that in relation to disclosure documents that a specific exemption should be included in the Bill for existing disclosure documents at the commencement of the approval period. Administrative responsibility for such documents is, of course with ASIC, not APRA.

Additionally, there needs to be a consistent approach by regulators in relation to the citation of numbers on prescribed documents, and the prescribed documents need to be similar. While section 912F of the Corporations Act provides for the prescription of documents by regulation, section 29DC(2) of the Bill leaves the prescription up to APRA.

APRA to give notice of refusal of applications – section 29DE

Section 29DE currently provides that where APRA refuses an application for a RSE licence it must take all reasonable steps to ensure that the trustee is notified of APRA's refusal and reasons for that refusal as soon as practicable after refusing the application. IFSA considers that, consistent with the rights of an applicant for an AFSL under section 913B(5) of the Corporations Act 2001, APRA should be able to refuse an application to grant a licence only after giving the applicant an opportunity:

(a) to appear, or be represented, at a hearing before APRA that takes place in private; and
(b) to make submissions to APRA in relation to the matter.

IFSA considers that there should be no difference in the rights of a person in relation to the refusal of an RSE licence to those of an applicant for an AFSL.

Conditions imposed on all licences and on groups of licences – sections 29E, 29EA(2)

A further Note should be added at the end of section 29E(1) and section 29EA(2) drawing the attention of groups of individual trustees to sections 13A and 338A of the Bill and, the possibility of strict liability and civil penalties applying to a group of individual trustees unless reasonable enquiries were made and existed for the individual trustees to believe that they complied with their obligations as an RSE licensee. An example a strict liability offence is that imposed under section 29HC where the RSE licensee fails to provide APRA with a copy of its modified risk management strategy within 14 days of the modification.

The responsibility on individual trustees should be underlined rather than, as is currently the case in the Notes to each section, implying that the only consequence is a direction from APRA to comply or cancellation of the licence.

Variation of RSE Licences - section s29F

Section 29F currently limits APRA's ability to vary licence conditions. IFSA considers that APRA should have the ability to vary licence conditions imposed under section 29E – **Conditions imposed on all licences and on groups of licences** - as well as conditions imposed under section 29EA being **Additional conditions imposed on individual licences by APRA**.

Consultation on licence conditions – sections 29EA(5), 29FC(3), 29FD, 29GA

IFSA considers that a failure by APRA to consult with ASIC about the imposition, variation, or revocation of an RSE licence condition that will affect the ability of the licensee to provide non superannuation financial services provided under the licensee's AFSL, should not apply to those non superannuation financial services subject to regulation by ASIC.

IFSA considers that it is important to clearly define and limit the role and regulatory responsibility of APRA to prudential supervision of superannuation. To do otherwise potentially impacts on the integrity of regulation. It is for ASIC to regulate the

activities of the holder of an AFSL and any action to change licence conditions are a matter for it to consider and enforce. This provision in its current form has the potential to significantly impact the financial services businesses of a trustee offering both superannuation and non-superannuation financial services.

Contents of risk management strategies – section 29H

IFSA questions the need for a separate RMS (sections 29E(1)(c) and 29H) and RMP (sections 29L(2)(e) and 29P). While the RMS relates to the licence and the RMP relates to RSE, they are duplicative and directly concern the operation of the RSE. IFSA recommends that a single document be used for setting out procedures and measures in place for the operation of the RSE and for risk minimization, as is the case with the compliance plan requirement in Part 5C.4 of the Corporations Act. This document should be limited to the prudential management activities. IFSA notes and supports the annual auditing requirement.

IFSA submits that section 29H(2)(a)(iii) is too onerous in requiring the RMS to set out procedures for identifying, monitoring and managing risks to it arising from expected changes in the law. Until a proposed change to the law is enacted it is not a matter that a trustee needs to factor into its operations. Given the complexity of the law and administrative systems in place to comply with the law, changes will generally have reasonable transitional period to enable implementation. Trustees should not be required to incur expenditure in relation to matters that may not eventuate.

Modifications to risk management strategies – section 29HB

It is a condition precedent to the grant of an RSE licence that APRA is satisfied that the RMS for the body corporate or group of individual trustees meets the requirements of section 29H (section 29D(1)(e)). Section 29HB empowers APRA to direct the RSE licensee to modify its RMS. A failure to comply with the APRA direction may constitute an offence under section 29JC.

IFSA considers that it is more appropriate that APRA be empowered to notify an RSE licensee that APRA considers that the RMS of the trustee no longer complies with section 29H and, if the RMS is not remedied within the period specified in the notice the RSE licence will be cancelled. Being a trustee of RSE while unlicensed is an offence (section 29J).

APRA should be required to specify the reasons it now considers the RMS to be non-compliant and the RSE licensee should entitled to:

(a) to appear, or be represented, at a hearing before APRA that takes place in private; and
(b) to make submissions to APRA in relation to the matter.

Consequential amendments should be made to section 29JB and 29JC of the Bill.

Notification of breach of a licence condition – section 29JA

The Bill does not contain the concept of "materiality", which IFSA submits should be included, especially in light of the proposed strict liability of the SIS regime. Trustees should only be required to report a *material* breach of a licence condition to APRA. We note that section 912D(1)(b) of the Corporations Act requires notification of a breach to ASIC where the breach, or likely breach, is significant having regard to a number of factors.

The need for a materiality requirement is particularly evident in relation to the RMS under section 29E(1)(e) which, like the compliance plan under the managed investment provisions of the Corporations Act, is intended to detect, limit and rectify possible breaches of the law and the scheme's constitution. A contravention of the duties of a responsible entity under section 601FC of the Corporations Act is a civil penalty provision and not a strict liability offence. The nature and success of an RMS or a compliance plan is that breaches are detected and remedied without any penalty to fund members.

While IFSA agrees that criminal liability should apply in relation to deliberate or reckless breaches of licence conditions, a civil penalty is in the majority of circumstances more appropriate for a breach of the RMS.

It is important to stress that principles based legislation it is about encouraging ethical and accountable behavior. The requirements imposed on trustees in the operation of a superannuation fund and supervision of its activities must be such that they act to encourage the detection and reporting of failures rather than discourage quick action by imposing strict liability**.** It is important that the law foster a compliance culture rather than merely the imposition of penalties.

Self incrimination – section 29JE and 29QB

The defence against self-incrimination should apply other than in the case of fraud.

Applying for registration – section 29L

IFSA is concerned that the requirement under section 29L(2)(d) to provide an up-to-date copy of the governing rules of an RSE may, in some instances, require the production of a large number of documents and could result in an application including many hundreds if not thousands of pages. The existing definition of "governing rules" in section 10 of the Superannuation Industry (Supervision) Act 1993 provides that '"governing rules" in relation to a fund, scheme or trust, means:

(a) any rules contained in a trust instrument, other document or legislation, or combination of them;
(b) any unwritten rules;

governing the establishment or operation of the fund, scheme or trust.'

Greater specificity should be provided in the Bill as to documents forming a part of the governing rules for RSE registration purposes.

Additionally, if a separate RMS and RMP is to be required, the terms "risk management strategy" and the term "risk management plan" should each be defined to ensure that there is no confusion that they are different documents. The law should also using terms or acronyms that are used and accepted in the industry to describe other documents such as the 'Risk Management Statement' or "RMS' [See also comments on *Contents of risk management strategies – section 29H*].

Part 3 Operating Standards – clauses 30 and 32

IFSA is concerned by the potential for duplicative subordinate legislation to be introduced by way of standards. The making of standards should be limited to the prudential regulation of superannuation. The Part should provide "for a system of prescribed prudential standards".

It is assumed that the Standards will be subject to the requirements of the Legislative Instruments Act 2003.

Amalgamation of Funds – Part 18

APRA have stated that these provisions are only intended to be used if there is a situation where a trustee cannot obtain a licence and they cannot find a fund with a 'perfect match' (section 146 of the Bill). IFSA does not consider that these provisions will aid fund consolidation or product rationalisation. While there are valid reasons for these clauses, IFSA members would like to see further refinement of Superannuation Industry (Supervision) Act 1993 to allow for a more effective and transparent amalgamation, or rationalisation of funds.

We would be pleased to further assist the Committee in its consideration of the Bill. Please contact Richard Gilbert on (02) 8235 2515 or David O'Reilly on (02) 8235 2526 if assistance is required.

Yours sincerely

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