

Chapter Three

Disclosure and Education

Introduction

3.1 During the inquiry, various parties argued that employees need to have access to adequate financial information, and have adequate financial education, if they are to make an informed choice of fund under the provisions of the Choice Bill.

3.2 This chapter considers:

- current financial disclosure standards;
- financial education and literacy standards in Australia; and
- other consumer protection issues.

Financial disclosure standards

3.3 In order to make an informed choice about where to invest SG monies, individuals need funds to disclose adequate and comparable information about such matters as fees, charges, commissions, and rates of return. Product disclosure statements, including reports of fund returns, are important aspects of an effective disclosure regime which evidence to the inquiry suggests is an essential precondition for the implementation of choice.

Product disclosure statements

3.4 The *Financial Services Reform Act 2001*, and associated regulations, has been designed to provide a framework for adequate disclosure. However, some parties submitted that the current disclosure provisions of the *Financial Services Reform Act* are inadequate and do not permit comparisons between funds. Within this framework, product disclosure statements provide details of fund returns, fees and charges associated with the fund, investment profiles, and other such information.

3.5 To regulate reporting in product disclosure statements, the Government introduced regulation 7.9.10 and 7.9.11(1), (1)(a), (1)(b) and (2) under the *Financial Services Reform Act 2001*, which came into effect on 11 March 2002. The regulations required superannuation funds to disclose an 'ongoing management charge' (OMC) in their product disclosure statements.

3.6 However, on 16 September 2002, the Senate disallowed these regulations, following a notice of motion moved by Senator Conroy on 18 June 2002. In the

absence of the OMC regulations, underlying disclosure regulations and obligations are now provided by the *Corporations Act 2001*.¹

3.7 During debate on the motion to disallow the regulations, Senator Conroy expressed his opinion that the OMC did not assist consumers, on the basis that it excluded entry and exit fees from its calculation.²

3.8 The Committee notes that a broad number of parties also expressed this position during the Committee's inquiry into the Choice Bill, at which time the OMC was still operative. They included Quadrant Superannuation,³ Cbus,⁴ the Industry Funds Forum,⁵ the AIG,⁶ the ACA,⁷ Quadrant Superannuation, ASFA and the MTAA Superannuation Fund. For example, ASFA noted in its written submission that the OMC did not provide a means for consumers to compare costs between funds:

ASFA fully supports the objective of providing prospective fund members a means to compare costs between funds. However, the current OMC requirements do not achieve this end. They are misleading and will be incomprehensible to most people.⁸

3.9 Similarly, the MTAA Superannuation Fund argued that the provisions of the *Financial Services Reform Act 2001* fell short of full disclosure of all fees and charges:

It is simply not good enough, in our view, for separate parts of the industry, essentially divided along the not-for-profit and for profit retail or wholesale product lines, through a "self regulation" approach, to establish different interpretations of what is in or left out of an OMC, particularly when these could relate to matters as important as entry and exit fees.⁹

3.10 The Committee also notes that the Parliamentary Joint Committee on Corporations and Financial Services tabled a report into regulations made under the *Financial Services Reform Act 2001* in October 2002. In that report, the Committee

1 *Committee Hansard*, 19 September 2002, p. 323.

2 Senate Hansard, 16 September 2002, p. 4132.

3 *Submission 14*, Quadrant Superannuation, p. 2.

4 *Submission 16*, Cbus, p. 11.

5 *Submission 30*, Industry Funds Forum, p. 3.

6 *Submission 9*, AIG, p. 2.

7 *Committee Hansard*, 2 September 2002, p. 21.

8 *Submission 17*, ASFA, p. 3.

9 *Submission 11*, MTAA Super Fund, p. 11.

noted that a number of witnesses to its inquiry also raised concerns about the former OMC.¹⁰

3.11 Given concern regarding the provisions of the former OMC, Superpartners argued in its written submission that Government regulations should require full financial disclosure of fees and charges on accounts, contributions, rollovers and benefits/exits (which were not measured by the OMC). Superpartners argued that it is fees and charges that largely determine members' final benefits rather than the OMC. This point was reiterated by Ms Galbraith from Superpartners in evidence:

What is much more critical with fees and charges are those that are actually levied on members' accounts and the effect that that has on their account balance. To a certain extent, it is almost irrelevant what a fund's ongoing management charges are. A fund may have significantly higher ongoing management charges, but if it is managing by doing that—to yield higher returns, it might be actively investing as opposed to passively investing or it might be doing a multitude of things—if, at the end of the day, it is producing higher returns and they are not reflected in higher fees and charges on members' accounts, then that is really what counts.¹¹

3.12 Superpartners further argued in its written submission that the only way to meaningfully compare two or more alternative fee structures is to determine their impact on the final value of the benefit. To achieve comparability and consistency in doing this requires 'a set of standardised, realistic assumptions' which can be utilised to assist fund managers to project the final benefit to illustrate the effect of fees and charges.¹²

3.13 The Committee also notes that in evidence on 3 September 2002, Dr Anderson from ASFA indicated that the Association is currently conducting its own research into disclosure of fees and charges. ASFA anticipates having the results of that research available by November 2002.¹³

3.14 The Committee subsequently raised this matter with Treasury officials, who are participating in the steering group for the study. Mr Thomas from the Treasury indicated that the study is being conducted with a group of 20 individuals, and is looking at a template product disclosure statement and that ASFA is also looking at an

10 For example the ACA, ASFA and Freehills and Rainmaker Information Pty Ltd. See Parliamentary Joint Committee on Corporations and Financial Services, *Report on the Regulations and ASIC Policy Statement made under the Financial Services Reform Act 2001*, pp. 39-44.

11 *Committee Hansard*, 2 September 2002, p. 2.

12 *Submission 26*, Superpartners, p. 2.

13 *Committee Hansard*, 3 September 2002, p. 144.

alternative to the OMC.¹⁴ Mr Rosser from Treasury stated that the early results from the testing indicated that ‘people had difficulty understanding the OMC’.¹⁵

3.15 The Committee notes that the ACA is also currently engaged in the process of consumer comprehension testing of different models of fee disclosure, and that the Association has urged the Government to re-engage in this process.¹⁶

3.16 Under the FSR regime, ASIC, as the regulator, has a key role. The Committee notes that on 26 September 2002, ASIC released a report entitled ‘Disclosure of Fees and Charges in Managed Investments: Review of Current Australian Requirements and Options for Reform.’ The report was prepared for ASIC by Professor Ramsay from the University of Melbourne. The report made a number of recommendations including:

- a) Standardised description and definition of fees;
- b) Separate disclosure of administration and investment fees;
- c) Improved disclosure of entry/contribution fees and exit/withdrawal fees including the use of common terminology across all products;
- d) The effect of fees on returns should be shown over various periods via a table; and
- e) There should be disclosure of fees paid to advisers.¹⁷

Reporting of fund returns

3.17 In its written submission, the MTAA Superannuation Fund suggested that in the absence of adequate disclosure regulations, funds would be tempted to highlight only positive aspects of their particular products, and ignore less desirable aspects. As a result, it will be very difficult to compare products and make an informed choice:

In an ‘open slather’ market place, funds will only be as good as their latest crediting rates - even their last monthly interim return will be scrutinised, tabulated, benchmarked and on-sold by researchers to third party advisers and gate-keepers. Inevitably, this will lead to trustees adopting investment policies that address this shorter term investment outlook, to the detriment of Australia’s retirement income investment pool.¹⁸

14 *Committee Hansard*, 19 September 2002, pp. 310-311.

15 *Committee Hansard*, 19 September 2002, p. 311.

16 *Submission 53*, ACA, p.2.

17 Prof Ramsay, *Disclosure of Fees and Charges in Managed Investments: Review of Current Australian Requirements and Options for Reform*, Report to ASIC, 25 September 2002.

18 *Submission 11*, MTAA Super Fund, p. 12.

3.18 The Committee notes the concern of various parties that the introduction of choice without sufficient disclosure standards may lead individuals to take short-term investment decisions based on returns over a short time period. Ms Kelleher from CPA Australia cited the example of moving from a fund that achieved an eight per cent return in the last year to another that achieved an 8½ per cent return, only to move their funds again the following year.¹⁹

3.19 The Committee also notes that the issues associated with advertising fund returns is currently being addressed by ASIC in its recently released discussion paper and guide on the use of past performance in investment advertising.²⁰ The Committee shares ASIC's concerns in relation to a range of misleading, or potentially misleading, advertising practices. The Committee also shares the concerns expressed by ASIC's Executive Director of Consumer Protection, Mr Peter Kell, that 'an undue emphasis on past returns can lead to consumers having unrealistic expectations and making poor investment decisions'.²¹ The Committee notes that ASIC is seeking comment on the draft guide by 15 November 2002.²²

Financial education standards

3.20 In addition to perceptions that the current Commonwealth financial disclosure standards are inadequate, various parties also submitted during the inquiry that individual employees in Australia lack the financial education necessary to make informed choice of fund decisions. As stated by Superpartners in its written submission:

While meaningful disclosure in superannuation fund documentation is a vital first step, as people are often greatly influenced by what is said to them, it is vital that they possess the requisite skills to be discerning and discriminating. Given that financial products and services are abstract and intangible, and that people are frequently intimidated by matters financial, it is even more important that people are armed with the necessary tools to evaluate different choices.²³

3.21 During the inquiry, Senator Hogg cited figures from an Australian Bureau of Statistics survey which, using the latest data available, showed that 19.7 per cent of the Australian population aged 15-74, or approximately 2.6 million people, have very

19 *Committee Hansard*, 2 September 2002, p. 83.

20 ASIC, *Discussion Paper, The use of past performance in investment advertising*, 30 September 2002 and accompanying draft guide on the use of past performance in promotional material.

21 ASIC, Media and Information Release, *ASIC issues discussion paper on the use of past performance information in investment ads*, 30 September 2002.

22 This material is available at the ASIC website at www.asic.gov.au.

23 *Submission 26*, Superpartners, p. 2.

poor prose literacy skills.²⁴ The survey also showed that up to six million Australians could have some difficulty in adequately reading and understanding printed material they could be expected to encounter in daily life. Currently, approximately 8.8 million Australians have superannuation funds.

3.22 Members of the Committee also cited during hearings the product disclosure statements issued by superannuation funds which describe their product, the fees and charges attached, the returns achieved by the funds and so forth. Some sample statements provided to the Committee ran to in excess of 60 pages. Senators on the Committee suggested that often these statements were overly complex and detailed and would be unintelligible to many Australians.²⁵

3.23 Similar concerns were expressed to the Committee in written submissions and in evidence. For example, the MTAA Superannuation Fund argued in its written submission that the workforce is ill-prepared to make an informed choice of fund, due to a lack of understanding of superannuation legislation, investment fundamentals and the income retirement system generally. The MTAA Superannuation Fund continued, 'These are not paternal platitudes – this is fact'.²⁶ Similarly, Ms Kelleher from CPA stated in evidence to the Committee on 2 September 2002:

I think in practice a lot of people will do whatever the next-door neighbour is doing or will go with whatever they think looks good without understanding everything behind it or what it means to them in entry and exit fees and ongoing management fees for the time that they are in there. Yes, they get the statements that say, 'These are the charges that you are bearing,' but I question whether they understand what it is that they are bearing. I would hate to see choice implemented without there being a thorough education program.²⁷

3.24 In response to these concerns, however, Ms Harris from the NFF argued in the hearing on 11 September 2002 that individual employees are becoming better educated on financial issues, and that most have a greater ability than they had ten years ago to make superannuation decisions.²⁸

The 2002-2003 Budget education allocation

3.25 Given concerns regarding current financial literacy standards in Australia, various parties argued during the inquiry that the commitment to education accompanying the Choice Bill is insufficient. As discussed previously, in the 2002-

24 ABS, *Aspects of Literacy Survey: Assessed Skill Levels Australia 1996* (ABS Cat. No. 4228.0); *Committee Hansard*, 2 September 2002, p. 8 and *Committee Hansard*, 3 September 2002, p. 175.

25 See for example *Committee Hansard*, 11 September 2002, p. 207.

26 *Submission 11*, MTAA Super Fund, p. 9.

27 *Committee Hansard*, 2 September 2002, p. 82.

28 *Committee Hansard*, 11 September 2002, p. 198.

2003 Budget, the Government allocated \$28.7 million over four years (from the ATO's existing budget) to an education and implementation campaign, to be administered by the ATO, to inform employees and employers of their rights and obligations in relation to choice.

3.26 During the Senate Economics Legislation Committee's consideration of Budget Estimates, the ATO advised that in 2002-03 and 2003-04, it will spend \$14 million on education and communication functions for the 8.8 million fund members and 650,000 employers impacted by choice. Over four years, the ATO will spend a total of \$14.5 million on changes to its own infrastructure and other administrative costs.²⁹

3.27 In its written submission, CPA Australia questioned whether the expenditure of \$28.7 million over four years, which is fully from the existing resources of the ATO, would be sufficient to create genuine understanding of choice of fund in Australia.³⁰ Similarly, in its written submission, the CSA stated:

We have concerns regarding the adequacy of the pool of funding set aside for the public education campaign to prepare employees for Choice. It is of paramount importance that choice should be exercised by individuals who are fully informed about the characteristics of superannuation as a long term investment. ... We believe that if individuals are to exercise choice, they must be better informed about investment as a whole and about the characteristics of long term investment pools and stock market cycles and fluctuations.³¹

3.28 The NFF also argued that the commitment to education accompanying the Choice Bill appears inadequate, suggesting that the allocated \$28.7 million over four years could be predominantly spent on administrative costs. The NFF continued:

It is critical that there is sufficient education at the workplace including additional resources including TV advertising or funding to employer and union groups to undertake seminars.³²

3.29 Similar concerns were expressed in hearings. Dr Pragnell from ASFA indicated in the hearing on 3 September 2002 his belief that the allocation of \$28.7 million would not 'go very far in a campaign that would catch most people' over four years.³³ Mr Hajaj, appearing on behalf of the Financial Services Consumer Policy

29 Senate Economics Legislation Committee, 2002-03 Consideration of Budget Estimates, 4 June 2002, answer to Question E187.

30 *Submission* 10, CPA, p. 2.

31 *Submission* 13, CSA, p. 7.

32 *Submission* 1, NFF, p. 11.

33 *Committee Hansard*, 3 September 2002, p. 149.

Centre at the UNSW, also argued that \$28.7 million over four years is inadequate.³⁴ Finally, Mr Silk from the Industry Funds Forum stated in evidence:

I think that, by any measure, \$28.7 million spent over four years is not going to achieve the sorts of objectives we would say are appropriate for an education campaign.³⁵

3.30 The Committee notes, however, that some parties indicated their belief that the funding level for education is adequate. For instance, the FPA suggested in its written submission that the allocation of \$28.7 million, with an 18-month lead-time, should provide the government and industry with ample opportunity to successfully implement choice.³⁶ Mr Breakspear from the FPA reiterated this position in the hearing on 11 September 2002. At the hearing the FPA indicated that a good model of an education campaign was the private health insurance lifetime cover campaign.³⁷

3.31 The Committee also explored with witnesses the possibility that the superannuation industry could potentially meet part of the cost of the education campaign. In response, however, Mr Hajaj, appearing on behalf of the Financial Services Consumer Policy Centre at the UNSW argued that the education campaign should be government funded, on the basis that it needs to target a broad range of parties including consumers, industry groups and government agencies.³⁸

3.32 While endorsing the principle that the education campaign should be Government funded, the ACA also submitted that the introduction of choice will require the kind of education campaign which accompanied the introduction of the GST.³⁹

3.33 In response to questions about the proposed education campaign, the NFF advised that the government education campaign should not be seen to supplement employer group education campaigns but vice versa. Further, that the form of the government education campaign should include direct mail to employers, TV, brochures, internet and through third parties such as employer groups. In addition to commencing at least six months prior to the introduction of choice, the NFF considers that education from the government would need to be ongoing beyond the introduction of choice, particularly to assist new employers and to ensure continuous compliance.⁴⁰

34 *Committee Hansard*, 2 September 2002, p. 23.

35 *Committee Hansard*, 11 September 2002, p. 269.

36 *Submission 37*, FPA, p. 2.

37 *Committee Hansard*, 11 September 2002, p. 213.

38 *Committee Hansard*, 2 September 2002, p. 23.

39 *Submission 53*, ACA, p. 2.

40 *Submission 46 and 47*, NFF.

Targeting of education

3.34 During the inquiry, various parties also highlighted the targeting of the ATO's education campaign. They expressed concern that it may alert individuals that choice of fund is available, but without actually educating and equipping them to make an informed choice.⁴¹ For example, Mr Hajaj, appearing on behalf of the Financial Services Consumer Policy Centre at the UNSW, stated:

Maybe seven or eight years ago there was a massive education campaign for superannuation with the money tree campaign. That was done by the Australian Taxation Office. All feedback shows that that was not a particularly efficient education campaign, and we need to learn the lessons of that. The main lesson that came out of that was that we need far greater proactive engagement with all the stakeholders—and that was not done before.⁴²

3.35 Others expressed additional concerns that the resources available for the education campaign should not be diverted into a public relations exercise aimed at promoting the purported benefits of choice without aiding decision making. For example, ASFA, in its submission, cautioned against:

... either a 'feel good about reform' campaign (along the lines of the 'Unchain My Heart' campaign for tax reform) or a campaign chiefly focussed on employer compliance.⁴³

3.36 In response to this concern, the Society of Superannuants (SOS) advocated that the Choice Bill should prescribe how the education program would be delivered.⁴⁴

3.37 Various parties also argued that education of individuals on financial matters such as superannuation has to begin at school, so that school leavers have the ability to make informed choices.⁴⁵ Ms Wolthuizen from the ACA noted in the hearing on 2 September 2002 that the UK has begun an extensive financial education campaign in schools.⁴⁶

3.38 In this regard, the Committee notes that ASIC's *Consumer Education Strategy 2001-2004* includes a commitment to a financial literacy in schools project, to encourage the provision of financial education to children and teenagers through

41 *Committee Hansard*, 2 September 2002, p. 23.

42 *Committee Hansard*, 2 September 2002, p. 23.

43 *Submission 17*, ASFA, p. 4.

44 *Submission 4*, SOS, p. 1.

45 *Committee Hansard*, 2 September 2002, p. 14.

46 *Committee Hansard*, 2 September 2002, p. 23.

school education. ASIC intends to work with relevant agencies to review curricula in Australia.⁴⁷

3.39 The Committee also notes the written submission of the NFF, in which it argued that the education campaign should also target employers, so that they are fully informed of their obligations under a choice environment, and can provide employees with practical guides such as checklists and template standard choice forms.⁴⁸ Similarly, in evidence to the Committee on 3 September 2002, Dr Pragnell from ASFA noted his belief that employers will need assistance in determining both who should be offered choice, and what their default fund should be. He suggested that small employers in particular are likely to need assistance:

I think particularly when you start to get to smaller employers, who may have less formalised industrial relations arrangements, they are going to be in some pretty murky water in terms of coverage and in even murkier water in terms of what the default fund actually is. I think that when you start to deal with larger employers with more sophisticated industrial relations arrangements it is going to be more straightforward.⁴⁹

3.40 Finally, the Committee also notes the evidence of Ms Dyson from the AIST that funding should also be set aside for education of fund trustees under a choice regime. Fund trustees will need to make more information available to their members under a choice environment, but should be aware that they cannot offer financial advice unless they are licensed to do so by the APRA.⁵⁰

3.41 In response to these concerns, Mr Murtagh from the ATO indicated that the ATO is currently designing a choice education campaign, including costing of research, evaluation and monitoring elements, together with deliberate marketing and education activities using TV, radio, press advertising and the like. In addition, the ATO has set aside \$2 million in funding for a consumer information centre.⁵¹

Other consumer protection issues

3.42 A number of other issues relating to mechanisms to strengthen the consumer protection regime were also raised by the ACA in a supplementary submission to the inquiry. In its supplementary submission, the ACA emphasised that the success of the Choice Bill will 'ultimately depend on the quality of information and advice provided to consumers looking to make a choice'. To assist consumers to make a choice, the ACA recommended that the Government establish an independent advisory and information service, which should be located within ASIC.

47 ASIC, *Consumer Education Strategy 2001-2004*, October 2001, p. 22.

48 *Submission 1*, NFF, pp. 10-11.

49 *Committee Hansard*, 3 September 2002, p. 150.

50 *Committee Hansard*, 3 September 2002, p. 171.

51 *Committee Hansard*, 19 September 2002, p. 331.

3.43 In order to test the legality and quality of advice, the ACA also submitted that ASIC should increase the level of auditing of financial advice from once every three years to an ‘ongoing basis’.

3.44 The Committee notes that, while expressing its concerns about the lack of a swift compensation mechanism under the SIS Act, the ACA is also in the process of preparing a submission to Treasury on an appropriate compensation regime, in the event of fund failure.⁵²

52 *Submission 53, ACA, pp. 3-5.*

