Senate Select Committee on Superannuation and Financial Services

Main Inquiry
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THE TREASURY

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Ms Sue Morton
Secretary
Senate Select Committee on
Superannuation and Financial Services
Parliament House
CANBERRA ACT 2600

Dear Ms Morton

SENATE COMMITTEE INQUIRY INTO THE OPPORTUNITIES AND CONSTRAINTS FOR THE PROVISION OF GLOBAL FINANCIAL SERVICES.

Thank you for your letter of 8 August 2000 to the Secretary of the Department of the Treasury listing questions on notice resulting from the Department's appearance before the Senate Select Committee on Superannuation and Financial Services on 14 July 2000. The Secretary has asked that I reply on his behalf. The reply also includes answers to issues raised in a number of e-mails to Financial Institutions Division staff over the last month.

1. 14-day Cooling-off Period

The draft *Financial Services Reform Bill* (FSR Bill) provides for cooling-off periods for a range of products including investment life insurance, superannuation and managed investments.

The draft FSR Bill makes provision for cooling-off periods as a way of ensuring that consumers can participate with greater confidence in the financial services sector. This is because cooling-off periods give consumers time to reflect on decisions made in the heat of the sales pitch and to reverse those decisions if the consumer, within a short time after the sale, reconsiders their initial decision.

Cooling-off periods have applied to products regulated under the existing life insurance and superannuation regimes for a number of years. The application of cooling-off periods to managed investments will provide a harmonised consumer protection regime in relation to functionally similar products – investment life products, managed investments and superannuation. Providing the same regulatory treatment for functionally similar products is a prime objective of the FSR Bill.

Under the draft FSR Bill, cooling-off provisions are the means for providing significant flexibility for industry participants in relation to the timing of the giving of various disclosure documents. For example, the Bill contains a general rule that a written Statement of Advice must be given to a client prior to providing financial services arising from that Statement of Advice. There is an exception to that rule in the case of financial products that are subject to a cooling-off period. Thus, where there is a cooling-off period, the service provider may provide the product before giving the client the Statement of Advice. This exception to the general rule is possible because the cooling-off period ensures the consumer is still adequately protected — although they receive the Statement of Advice after acquiring the product, they have the benefit of the 14-day cooling-off period to reflect on the Statement of Advice when they receive it, and if necessary change their mind about the product they purchased. Similarly, the giving of a Product Disclosure Statement may also be delayed where the relevant product has a cooling-off period (proposed section 982E).

These measures have been designed to balance both consumer protection interests and industry's need for flexibility in the way that it deals with clients, and have largely been welcomed by industry groups. The removal of cooling-off periods in relation to a particular financial product would trigger a more prescriptive and inflexible obligation on industry as to the timing of giving of disclosure documents.

Calculation of the money to be repaid to the retail client

One concern expressed by industry members has been the potential for consumers to use the cooling-off period as a way to protect themselves against market movements. For example, some industry participants express concern that, if a consumer invested in a managed investment or investment life insurance product and the market moved against them in the 14-day cooling-off period, the consumer would be able to withdraw their money and suffer no loss.

This was never the intention. The Commentary to the draft FSR Bill provides that where the market moves against the consumer in the cooling-off period, the amount returned to the consumer will be reduced by the amount of the market movement. (Refer paragraph 8.160.)

In addition, the Commentary also includes discussion of the treatment of tax paid in relation to certain products.

Various industry participants indicated in submissions on the draft FSR Bill that a number of additional adjustments should be included to ensure the cooling-off provisions more effectively balanced the interests of consumers and industry in respect of managed investments. These submissions have been analysed and the Bill and proposed regulations that will address what a consumer gets back, will take account of these concerns.

While a number of industry participants have expressed concern at the application of cooling-off periods to managed investments, the Investment & Financial Services Association Ltd (IFSA), a significant industry body, has in its submission on the FSR Bill said that 'IFSA supports general application of cooling off in the interests of harmonised consumer protection in relation to all functionally similar products'.

2. Proposed Licensing Arrangements

The Commentary to the draft FSR Bill contains an outline of the proposed transitional licensing provisions for financial service providers.

In general, submissions on the draft FSR Bill did not comment to any great extent on the proposed transitional provisions. However, a number of concerns were raised at the necessity for industry participants who were currently operating under the various service provider licensing and registration schemes applying in respect of general insurance, life insurance, securities and futures to obtain a new licence under the FSR regime. In addition, concerns have been expressed at the ability of the regulator to licence the anticipated number of applicants within the proposed two year transitional period.

Given that the FSR regime imposes new or differing licensing criteria as compared with the various existing regimes, the Government has been concerned that to merely grandfather existing licensees/registrants across would be to undermine the integrity of the FSR regime and to hinder the regulator's ability to ensure that all Australian Financial Service Licensees had met, and were meeting, comparable standards.

At the same time, however, the Government has been keen to ensure that the transitional provisions result in minimum disruption to industry and that the regulator will be able to effectively and efficiently administer the transition to the new regime. Accordingly, to reflect the input that the Government received from industry and the regulator (the Australian Securities and Investments Commission), the transitional proposals initially contained in the Commentary have been modified. The Government now proposes to provide for a streamlined or fasttrack mechanism for registrants or licensees under existing insurance, deposit taking, securities and futures regimes. This streamlined approach will allow existing licensees to apply for a new licence for the conduct of their existing financial service business on the basis of self-declarations about compliance with the relevant licensing criteria. This approach will minimise disruption to business while preserving the integrity of the licensing regime.

3. Collective Investment Vehicles (CIVs)

CIVs were excluded from the Ralph Review of Business Taxation recommendation to tax trusts like companies ('entity tax regime'). To prevent parties circumventing the entity tax regime Ralph recommended CIV status be restricted. Restrictions included a CIV being an Australian resident unit trust.

Industry argues that denying flow-through tax treatment to foreign funds renders the Foreign Investment Fund exemption ineffective. Issues raised in consultations on business tax reforms are under active consideration, including those on entity taxation and CIVs. Further consultations are anticipated.

4. Offshore Banking Unit (OBU) Regime

The Government is committed to developing Australia as a global financial centre and the OBU regime is a component of that strategy.

Australia is not alone in having a regime listed as 'potentially' harmful and there are no immediate implications. Most other Organisation for Economic Co-operation and Development (OECD) member countries, including the United States of America, Canada, France and Korea, have one or more regimes listed.

The Australian OBU regime is highly comparable to similar offshore finance regimes. The Asian Currency Unit (Singapore's offshore finance centre) is the broadest regime in general terms and it includes corporate treasury operations and offers a number of incentives such as tax holidays (not offered by Australia). As a non-OECD member, the Singapore regime has not, however, been assessed against the harmful tax practice criteria.

Consistent with the OECD timetable, Australia will work with the OECD over the next three years to develop guidelines to determine 'actual' harm and further evaluate regimes that have been listed as 'potentially' harmful.

In agreeing to the OECD work on harmful tax practices in 1998, Australia made it clear to the OECD that taxation should not inhibit Australia from being attractive to financial centre activities.

Further evaluation of Australia's OBU regime by the OECD will need to take that policy position into account.

5. London Function (Senator Conroy's question)

Senator Conroy inquired about the menu for the Tuesday evening dinner as part of Australia Week in London in July 2000. It comprised a salad of sea scallops and crispy duck; oven roasted lamb with accompaniments; ice cream and fruit; cheeses and wine.

The dinner was seen as a significant marketing opportunity to showcase the advantages of Australia as a centre for global financial services. In total there were 55 attendees at the function, a significant number of whom included European representatives at the highest levels from some of the world's largest financial services providers.

The cost of the function was 11,869.85 pounds. This cost covered catering, AV/sound/lighting, dinner material (menus, place cards etc), and flowers. Additional costs were incurred by Axiss associated with pre-function organisation, costs related to staff travel and accommodation and additional London-based support.

6. Axiss Australia

Mr Hosking's opening statement of 16 May 2000 to the Committee outlined key areas of focus for Axiss Australia and described, in general terms, the strategy being adopted. An overview of Axiss Australia is at Attachment A.

7. Facts and Figures on Axiss

The Australian Centre for Global Finance was established in August 1999 and was rebadged as Axiss Australia in June 2000. Les Hosking commenced as Chief Executive Officer on 24 January 2000. In addition to the CEO, Axiss currently has seven full time staff, one part time member of staff and two consultants working on education and promotion initiatives. Government funding is budgeted until the end of June 2001.

8. Data Collection and Benchmarking of Australia's Performance

The issue of assessing performance/demonstrating achievements in this area has already been addressed in Mr Hosking's evidence before the Committee on 16 May 2000 and in the letter to the Committee Secretary dated 14 July 2000.

9. Education, Research and Training

Mr Hosking's letter of 14 July 2000 addressed this issue and Axis Australia has subsequently provided further information to Ms Robyn Hardy (of the Committee's Secretariat). You may wish to note that Minister Hockey on 16 August 2000 announced a joint venture in business and finance education involving Stanford Business School, the Australian Graduate School of Management and the Melbourne Business School. Axiss Australia helped facilitate discussions between the three institutions and Axiss envisages a continued role during the development stage as well as providing support with promotional activities. The initiative is aimed at positioning Australia as a centre for excellence in education and training for the financial services sector in this region and, thereby, provide a solid foundation for the establishment of Australia as a financial services centre. Press release No. FSR/044 by the Minister for Financial Services and Regulation provides further details.

10. Promotion

It is our understanding that correspondence covering promotion has been exchanged between Axiss Australia and Ms Robyn Hardy, of the Committee's Secretariat, on 14 August 2000 and subsequent to this date. There is no additional information.

11. Financial Sector Advisory Council Taskforce

The Financial Sector Advisory Council (FSAC) Taskforce last met on 30 November 1999. Consideration is being given to the future of the FSAC Taskforce in light of the establishment of Axiss Australia.

The current members of the FSAC Taskforce are:

Chair: Mr Les Hosking, Chief Executive Officer, Axiss Australia

Members: Mr Derek Young, Managing Partner, Asia Pacific Financial Services, Andersen Consulting;

Mr John Fraser, Managing Director and Regional Head, UBS Asset Management Asia Pacific; and Chairman of UBS Asset Management (Australia) Ltd;

Mr Kenton Farrow, Chief Executive, Australian Financial Markets Association;

Mr Richard Humphry AO, Managing Director and Chief Executive Officer, Australian Stock Exchange Limited; and

Mr Robert Webster, Executive Director, International Banks and Securities Association of Australia.

12. Regulatory Advisory Committee

The maintenance of the strength and integrity of Australia's system of financial sector regulation is fundamental to the aim of promoting Australia as a global financial services centre. To this end, the Regulatory Advisory Committee (RAC) was established on 29 June 1999.

A total of five RAC meetings have been held since this date. The purpose of RAC is to coordinate the resolution of regulatory issues identified by member agencies, including Axiss Australia, and to support the development of Australia as a centre for global financial services by assisting in promoting the quality of Australia's regulatory regimes.

I trust this information will be of assistance to you.

Yours sincerely

Steve French
General Manager
Financial Institutions Division

Attachment A

Overview of Axiss Australia

Australia has considerable scope to develop as a global financial centre. Strong management of the economy and recent government initiatives designed to make the economy globally tax competitive and the regulatory framework "world best practice", together with the quality of our people skills, technology infrastructure and the quality of life on offer, can all work to our advantage. However, these strengths are generally not appreciated or well known in the global financial services industry.

Moreover, technological advances, market liberalisation and globalisation have changed the way in which financial services business is undertaken and thereby created new opportunities. There is considerable scope for eliminating the disadvantage of distance that has long separated Australia from other parts of the world. Indeed, Australia's geographic location could well assist in positioning Australia as an integral part of a "continuous" or 24-hour trading day spanning the close of the US and European trading days – if we are able to capitalise on this advantage.

The benefits from transacting a larger share of world financial services business and positioning Australia as a global financial centre lie in the gains to economic growth and employment. These benefits accrue not only to the financial services sector but will impact on related sectors, and indirectly, permeate through to all sectors of the economy.

Axiss Australia's objective is to position Australia as a global financial centre, with particular emphasis to its potential importance in the Asia-Pacific timezone.

Achieving this objective will require a benchmarking of existing competitive advantages and an effective promotion strategy aimed at increasing awareness of Australia's strengths as a global financial centre.

It will also require Axiss Australia to examine the factors affecting the evolution of financial markets and identify the key characteristics likely to attract global financial service providers to the Australian market in the future. Axiss Australia will need to ensure that the conditions necessary to continued development as a global financial centre are in place, and recognised as being so by key decision makers in the financial services sector.

Axiss Objectives

The key objective of Axiss Australia is to make Australia a global financial centre and gain a greater share of world financial services business.

In achieving this objective, Axiss Australia will seek to:

- Improve its understanding of the existing competitive advantages Australia has to offer through improved data collection, benchmarking and analysis;
- Develop and implement an effective promotion strategy designed to increase awareness of Australia's credentials as a global financial centre;
- Gain a better understanding of Australian and global capital markets and the factors that drive their evolution;

- Identify areas where Australia will need to be proactive in engineering Australia's continued future development as a global financial centre;
- Improve its information and data on these key development areas;
- Provide policy advice to the Government and develop initiatives designed to facilitate Australia's development as a global financial centre;
- Promote an awareness of initiatives in these key areas and their benefits for Australia's continued development as a global financial centre;
- Provide a vehicle for high-level strategic dialogue between the government and finance sectors; and
- Ensure that policy and promotion efforts are coordinated with other agencies so that Axiss Australia's efforts supplement and/or complement rather than duplicate the efforts of other agencies pursuing similar objectives.

These can be considered key elements of a general strategy directed at the overarching objective of making Australia a global financial centre.

Promotion

Perceptions of Australia and its operating environment are often incorrect or outdated.

Central to Axiss Australia's work is the task of overcoming the outdated impressions of Australia and its business and finance sectors. To that end, there is a need to:

- ➢ improve data and information so as to better understand quantitatively our advantages in these areas and benchmark our comparative performance; and
- ➢ implement a promotion strategy aimed at increasing awareness by key decision makers in the financial services sector of Australia's strengths as a global financial centre.

The promotion of existing advantages is likely to prove effective in increasing the number of players and the size of their operations in the Australian financial services sector today, but with financial services increasingly mobile, emphasis must also be given to ensuring the permanence or sustainability of such "successes".

Looking Forward

Axiss Australia will need to be forward looking and adopt strategies aimed at ensuring that Australia remains competitively positioned as a global financial centre well into the future.

Axiss Australia has identified the following three areas as essential elements necessary to ensuring that Australia best positions itself as one of the key global players in financial:

- ➢ Stable and deep capital markets with world class innovative product development and operating within a "cutting edge", world best practice regulatory framework responsive to a changing business environment;

- Technology, encompassing both a world class telecommunications and information technology (IT&T) infrastructure available at competitive cost; and

- An education, training and research framework delivering a highly skilled, innovative, cost competitive and responsive workforce.

These three areas are highly integrated. Global financial centres will emerge where there exists the IT&T infrastructure, the skilled labour and the regulatory framework conducive to undertaking financial services business.

Against this background, Axiss has identified capital markets, education and training and IT&T as issues for attention if Australia is to remain positioned as a global financial centre into the future.