SUBMISSION

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry — Round 5 Superannuation Policy Issues

21 September 2018

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Mr Simon Daley

Solicitor Assisting the Royal Commission

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21 September 2018

Dear Mr Daley

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry ("the Commission") – Round 5 Superannuation submission

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the Commission's invitation to make written submissions on policy issues in relation to the superannuation industry raised in Round 5.

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system, so all Australians can enjoy a comfortable and dignified retirement. We focus on the issues that affect the entire Australian superannuation system and its $2.7 trillion in retirement savings. Our membership is across all parts of the industry, including corporate, public sector, industry and retail superannuation funds, and associated service providers, representing over 90 per cent of the 14.8 million Australians with superannuation.

If you have any queries or comments in relation to the content of our submission, please contact Julian Cabarrus, Director of External Affairs and Strategy on (02) 8079 0815 or by email at jcabarrus@superannuation.asn.au

Yours sincerely

Dr Martin Fahy

Chief Executive Officer

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1. Introduction

ASFA's purpose is to help achieve the best retirement outcomes for fund members. Our advocacy work is guided by policy principles, including that the relevant policy will increase sustainability and members' confidence in the superannuation system.[1]

ASFA considers that meeting community standards and expectations is at the heart of engendering confidence in the system. Given the fiduciary nature of superannuation it is reasonable to expect that, at a minimum, savings are managed with a high degree of prudence and integrity by trusted institutions.

The proceedings of the Commission and questions posed by Counsel Assisting are about areas of industry conduct and regulation where improvements are possible. This submission will discuss how stronger regulatory frameworks can be developed and conflicts management can be improved to address the issues identified by the Commission.

ASFA considers it is important to acknowledge that the superannuation system is already delivering significant improvement in retirement living standards for all Australians.

This is the case even for those earning well under average weekly earnings. For instance, for a person aged 30 on $40,000 a year (below even median employment earnings), with a current balance of $20,000, the compulsory superannuation system will deliver an estimated $263,500 at retirement. This will increase retirement income from $23,662 a year provided by the Age Pension to $34,078 a year. For those on higher incomes the increase in retirement incomes will be even greater.

The increase in retirement savings has already contributed to a decrease in the proportion of those aged over 65 receiving the Age Pension from 80 per cent to 70 per cent and this is projected to fall further. Despite the ageing of the Australian population, expenditure on the Age Pension is projected to stay well below 3 per cent of GDP, a very low level by world standards.

Superannuation makes a substantial difference to the adequacy of retirement income and the ongoing affordability of the Age Pension. The community deserves to be financially confident in retirement and the superannuation system is delivering in this regard. This national beneficial outcome is the backdrop when changes to the regulation of superannuation are being considered.

[1] Appendix 1 – ASFA Policy Principles

2. Summary of ASFA's key positions

The below table denotes ASFA's key positions in response to the questions raised by the Royal Commission.

Ref:	Royal Commission question	ASFA response
Conflicts of Interest – Structures		
825.18	If certain structures do raise inherent problems, is structural change of entities, mandated by legislation or otherwise, something that is desirable?	There is no overwhelming evidence to support a prohibition on particular structures within superannuation. ASFA's strong preference is not legislative intervention to mandate structures, as in most instances conflicts that arise are manageable. The focus should be on strengthening conflicts management and regulatory frameworks to facilitate improved conduct and outcomes for consumers.
825.17	Are there structures that raise inherent problems for a superannuation trustee being able to comply with its fiduciary duties?	**Dual-regulated entities** ASFA considers that a requirement to have a significant proportion of separate directors for the RSE licensee and responsible entity, including separate chairpersons, could help address actual or perceived conflicts of interest in dual regulated entities. **Related party service providers** ASFA considers that a requirement to more rigorously validate the selection of related party service providers could strengthen industry practice and improve conflicts management. Mechanisms to achieve this could include: • enhanced assurance processes to provide comfort that arrangements are in the best interests of fund members • rigorous benchmarking that demonstrably supports the trustee's decision **Prudential codification of best interests and a trustee 'safe harbour'** APRA prudential guidance would assist trustees to more effectively implement their best interests' obligations. The guidance should focus on the trustee's decision-making process and governance. ASFA also recommends the introduction of a safe harbour for trustees who meet the requirements.

		Increasing trustee understanding and capability ASFA considers that - prior to commencing their role - trustees should be required to complete a certificate IV level course in the responsibilities and obligations of being a director of a corporate trustee of a superannuation fund provided by a Registered Training Organisation. Extending these requirements to executives and senior managers within superannuation funds is also worth consideration.
Best Interests Duty		
825.19	Would it be preferable to extend the obligation to act in the best interests of members of a superannuation fund so that: (i) contravention of the obligation attracts a civil penalty; and (ii) the obligation (and the civil penalty for breach) extends to shareholders of trustees and any related bodies corporate	**Contravention attracting a civil penalty** ASFA considers that APRA should be able to impose a sanction for a failure to act in the best interests of members – either through a civil penalty being imposed by a court or through the imposition of a condition on a licence or the revocation of an authorisation or licence. If there is to be an extension of civil penalties it should include protections for honest mistakes and actions undertaken in good faith. **Extension of obligations and civil penalties to shareholders of trustees** ASFA does not consider it appropriate to extend the obligation (and the civil penalty for breach) to shareholders of trustees and related bodies corporate, as it is the role of the trustee to act independently as a fiduciary with respect to beneficiaries of the trust.
Conflicts of Interest – Specific Matters		
825.15	Are legislative interventions to remove grandfathered commissions and ongoing service fees from superannuation accounts appropriate?	ASFA supports ending grandfathered trailing commissions with a one year transition period from the date of legislation that supports an orderly transfer to modern arrangements. To achieve the best outcomes for members there are a number of transitional issues that must be addressed so that successor fund transfers to more modern products can occur without impediment.
825.16	Are there possible detrimental effects on the provision of high quality financial advice by such changes?	ASFA is of the view that access to the different types of financial advice is vital to superannuation fund members as they consider financial decisions in the accumulation phase and in retirement. To maximise access for superannuation fund members to financial planning advice, ASFA supports: • Trustee discretion with regard to the charging of intra-fund advice fees from the general administration fee

		• Maintaining the existing right of members to pay for full personal financial advice from their superannuation account balance if they elect to do so, and where the fee disclosure statement and opt-in requirements are being met
825.7 **and** **825.8**	Is it appropriate that superannuation be sold through bank branches? Are there statutory reforms that are required to address this problem (if it is a problem) or are the existing laws with respect to personal financial advice and general financial advice sufficient?	ASFA considers the starting principle should be that the right advice or information is made available to all Australians, whether that is through a bank branch or another channel. We do not consider that the best way to address issues arising from conflicts is a unilateral ban on particular types of entities from providing services or prescription of industry structures. Issues arise due to a lack of clarity around what constitutes general, intra-fund and personal financial advice. A holistic review of these categories should be undertaken to clarify what constitutes the different types of advice and what education and training requirements are appropriate for each.
825.3	Is it appropriate, as a response to conduct of superannuation trustees that seeks to induce employers to select funds, or affect their decisions as to default funds, to make alterations to section 68A of the SIS Act to widen the prohibition?	ASFA considers that the current section 68A provision is sufficient and that any issues relate more to its enforcement rather than its content. Industry would benefit from greater clarity from the regulators in relation to the specific conduct that contravenes section 68A.
Regulators		
825.25	What can be done to encourage the regulators to act promptly on misconduct or potential misconduct?	**Encouragement toward prompt action on (potential) misconduct** ASFA is of the view that the regulators have significant powers and should demonstrate effective use of these prior to consideration of additional powers being provided. ASFA considers that a detailed review of the regulatory mandates of APRA and ASIC to identify and address any specific gaps or overlaps is warranted. **Resourcing and capability** ASFA considers it appropriate that at the conclusion of this Royal Commission, a further capability review of ASIC is conducted, and a capability review is performed for APRA, to ensure both regulators are well placed to implement the Commission's recommendations.

		ASFA considers that the regulators should provide greater transparency in relation to their use of resources on an annual basis. This should include specific reporting in relation to the resources assigned to enforcement activities and the outcomes from those activities. **Adequacy and appropriateness of breach reporting regimes** ASFA considers that the Government should, as soon as practicable following the conclusion of the Royal Commission, provide clarification as to any intended reform of the breach reporting obligations for AFS licensees. ASFA is of the view it would be beneficial to conduct a review of RSE licensees' breach reporting obligations — similar to that undertaken by the ASIC Enforcement Review Taskforce — to identify and address any impediments to the timely provision of information to APRA.
825.26	Is the present allocation of regulatory roles appropriate to achieve specific and general deterrence from misconduct?	ASFA considers the current allocation of regulatory responsibilities between APRA and ASIC to be broadly appropriate, but would support a detailed review of the regulatory mandates to ensure that any specific gaps or overlaps (actual or perceived) are identified and addressed. ASFA does not support the creation of a specific 'pensions regulator' at present.
Engagement by superannuation funds with Aboriginal and Torres Strait Islander people		
825.11	Should those superannuation funds who do not currently permit the early release of superannuation on the basis of severe financial hardship do so?	As a matter of public policy it has been determined that, where a member is experiencing severe financial hardship, it is appropriate to release an amount of their superannuation. Given this, there is an argument that it should be available to all members (other than perhaps defined benefit members), irrespective of the fund of which they are a member.
825.12	Should the lower life expectancy of Aboriginal and Torres Strait Islander people be taken into account when considering how to administer or release the funds of Aboriginal and Torres Strait Islander people?	The public policy focus should be on improving life expectancy for Aboriginal and Torres Strait Islander people. ASFA would support the government reviewing superannuation settings such as temporarily lowering the preservation age, to provide better access to superannuation benefits for Aboriginal or Torres Strait Islander people. Improving poor life expectancy outcomes must however remain the longer term policy priority.

Other Policy Issues and System Changes		
825.23	Is it appropriate to introduce some form of "stapling" so that a person's account for receipt of default contributions is linked to the person and travels with the person when she or he changes job?	ASFA is supportive of continuing to reduce unintended duplicate accounts. However, there are pros and cons to 'stapling' consumers to a single superannuation account. Consolidating accounts into a new, appropriate default each time a member changes jobs is another option worth considering so that individuals are consistently defaulted into arrangements suitable for their most recent circumstance.
825.14	Is it appropriate for shareholders of RSE Licensees to retain a broad discretion to appoint and remove directors?	It is appropriate that shareholders of RSE licensees retain a broad discretion to appoint and remove directors. Ultimately it is up to the trustee directors to ensure the fund is operated in the best interests of members.
825.21	Is one way of addressing and discouraging misconduct on the part of superannuation trustees to seek to encourage improvements to outcomes for members whose contributions are made to MySuper products or is the link too tenuous to justify recommending any system changes to the default system?	ASFA does not consider that there is a link between amending the MySuper settings and discouraging or addressing misconduct. Regardless of this, we consider that strengthening the MySuper regime would be beneficial for consumers. ASFA supports elevating the threshold for MySuper authorisation to raise the standard for all MySuper products. The settings should support the sustainable delivery of high quality MySuper products to the market, on an ongoing basis.

3. Conflicts of Interest – Structures

3.1. Mandating structural change

825.18 If certain structures do raise inherent problems, is structural change of entities, mandated by legislation or otherwise, something that is desirable?

3.1.1. Market dynamics, competition and innovation

ASFA considers that there is nothing inherent in the concept of for-profit provision of services that will necessarily lead to poor outcomes for fund members.

The profit-seeking business entity is fundamental to a market based economy, where entities are incentivised to generate a (required) rate of return on invested capital, for the owners of that capital.

Modern market-based economies rely on competition in product and service markets to allocate scarce economic resources in the private sector. All superannuation funds regulated by the Australian Prudential Regulation Authority (APRA) use for-profit service providers as part of the superannuation value chain and readily invest in for-profit companies to generate returns for their members and deliver on their retirement savings objectives.

For-profit and mutual or co-operative ownership co-exist satisfactorily across many areas of the economy such as health insurance, deposit taking and lending by banks and by credit unions, and primary produce marketing.

A competitive market environment promotes efficiency, innovation and productivity gains and, over the long term, higher living standards. Competition and price signals have a well-established role in generating these outcomes.

With respect to superannuation (and financial services more broadly), this can include innovations to products that better meet members' needs. It can also include services for members that use improved technologies to inform, educate and engage with members. Competition motivates these forms of innovation and over time improves the quality of products and services offered.

There are some unique features of superannuation that inhibit price signals such as:

- Low levels of engagement and a large number of default members
- The role of intermediaries such as advisers in facilitating choice
- A high intensity regulatory climate and significant barriers to entry
- Difficulties with price comparability due to complexity of pricing structures and variability of disclosures

Notwithstanding this, the system produces very good outcomes for the vast majority of Australians.

There is a need for strong regulatory frameworks to manage behaviours, but there is no overwhelming evidence to support a prohibition on particular structures within superannuation.

The market for superannuation can be categorised as follows:

- Choice products, which individuals choose on the basis of their own investigations or are more usually assisted by another, such as licensed financial adviser
- Default products, which are chosen by an employer where an employee does not nominate a fund.

Different considerations apply to these two categories. For choice products, effective disclosure and competition, together with measures to deal with any conflicts of interest on the part of advisers, including

in regard to conflicted remuneration, are the means to get good outcomes for consumers. Legislative prescription of the characteristics of choice products is neither necessary nor desirable.

In regard to default superannuation funds there is a stronger case for further prescription of product characteristics as members are less engaged and the forces of competition may be less. This is the basic rationale for the introduction of MySuper products, which are simple and relatively low cost superannuation offerings.

As a general principle, the level of regulatory intensity should reflect the strength of the promise made to participants in the system. In a compulsory, defined contribution system where the consumer bears the market risk (and reward) associated with their investments, the core promise is that trustees will provide effective stewardship of their savings and place their collective interests first. While there can be no guarantees in relation to fund performance, good governance should be a hallmark of the system.

The Commission has raised some concerns in relation to aspects of superannuation fund governance and, through particular case studies, demonstrated that there are opportunities for improvement. The shortcomings identified point to errors of process that can be remedied.

There is no overwhelming evidence to support a prohibition on particular structures within superannuation. ASFA's strong preference is not legislative intervention to mandate structures, as in most instances conflicts that arise are manageable.

The focus should be on strengthening conflicts management and regulatory frameworks to facilitate improved conduct and outcomes for consumers.

3.1.2. Insourcing and outsourcing

The retirement funding value chain requires the provision of key services and activities including:

- Fund administration
- Benefit payments
- Investment management/asset consulting
- Insurance
- Custodial services
- Advice

These services are either performed by the superannuation fund itself, or provided by a third-party entity which may be related to the trustee.

For some stages of the value chain, third-party provision is dominated by providers that specialise in providing particular products and services to superannuation funds. This includes administration services, where significant economies of scale have facilitated a small number of large entities to achieve scale.

For other stages of the value chain, third-party provision is dominated by providers that specialise in particular products and services, but where superannuation funds are just one group of clients. This includes life insurance, where specialist providers offer life insurance (ultimately to retail customers) through a range of channels – including through superannuation funds.

Vertically-integrated financial services institutions (such as the large retail banks) may have some, or all, of the required functions within the corporate group structure. Funds within a particular group may outsource to another area of the organisation, or to an unrelated entity. By the same token, the group may offer products and services to funds outside of the group. The prime example is investment management

services. Funds within vertically-integrated financial services institutions typically outsource investment management to specialist providers both inside and outside of the corporate group.

More recently, funds (such as industry and public sector funds) that have traditionally outsourced services including investment management, advice and insurance, have sought to integrate a higher proportion of these activities within the superannuation fund, either through acquisition or organic growth. In particular, large superannuation funds with significant scale seek to generate service or performance benefits to members through such integration.

This underscores the competitive and dynamic nature of the industry. Superannuation funds and service providers look to gain a presence in, or expand their existing share of, particular stages of the supply chain.

Funds' decisions on insourcing and outsourcing also reflect risk mitigation strategies. The increasingly complex regulatory environment for superannuation funds has substantially increased the administrative and compliance burden on superannuation funds, which favours outsourcing. On the other hand, insourcing may give funds greater control.

In the following section we discuss how conflicts might be better managed to ensure that fiduciary obligations are met when related party service providers are used by fund trustees.

3.2. Managing structural conflicts of interest

825.17 Are there structures that raise inherent problems for a superannuation trustee being able to comply with its fiduciary duties? For example, where a trustee is a dual-regulated entity that would seem to raise an inherent conflict of interest, or the potential of a conflict of interest. Are there other structures such as investment of funds in insurance policies issued by related party insurers or the integration of a superannuation trustee into an advice business that also raise inherent problems? Is it possible to say that these conflicts are ever manageable?

3.2.1. The conflicts management framework

A major challenge for a superannuation trustee in complying with its fiduciary duties is dealing with conflicts of interest.

It is of critical importance that superannuation funds have appropriate frameworks in place to manage conflicts of interest. These frameworks can include:

- Policies in relation to conflicts management, outsourcing and related party transactions
- Maintenance of conflicts registers
- Public disclosure of conflicts where required and appropriate
- Risk management processes, controls and testing in relation to material conflicts
- Trustee decision-making processes that clearly demonstrate related party arrangements are being entered into on an arms-length basis
- The establishment of conflicts management committees to manage inherent conflicts of interest
- Organisational culture

There are regulatory requirements for managing conflicts of interest set out in legislation and prudential standards.

The *Superannuation Industry (Supervision) Act 1993 (SIS Act)* prescribes trustee covenants that are included in the governing rules of a registrable superannuation entity. The particular covenants relating to conflicts of interest require the following of trustee directors:

Where there is a conflict between the duties of the trustee to the beneficiaries, or the interests of the beneficiaries, and the duties of the trustee to any other person or the interests of the trustee or an associate of the trustee:

- to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons; and
- to ensure that the duties to the beneficiaries are met despite the conflict; and
- to ensure that the interests of the beneficiaries are not adversely affected by the conflict; and
- to comply with the prudential standards in relation to conflicts.[2]

APRA *Prudential Standard SPS 510 Governance* requires that the governance framework of a registrable superannuation entity (RSE) licensee must, at a minimum, include the RSE licensee's policies and processes relating to the management of conflicts.

APRA *Prudential Standard SPS 521 Conflicts of Interest "*establishes requirements for the identification, avoidance and management of conflicts of duty and interest by an RSE licensee. These requirements are essential to ensure that an RSE licensee and its responsible persons meet legislative obligations in Part 6 of the *Superannuation Industry (Supervision) Act 1993*".[3]

Most recently, on 29 May 2018, APRA wrote to all RSE licensees to inform them of the outcomes of a thematic review specifically examining the RSE licensees' management and governance of related party arrangements. APRA note that "the thematic review was prompted by APRA's observations of weaknesses in how some RSE licensees govern and manage aspects of their outsourced arrangements with related party service providers."

In their review, "APRA found that for the sampled RSE licensees there have been improvements in the governance and management of related party arrangements since the conflicts of interest thematic review, with a number demonstrating effective approaches to managing related party service provider arrangements."

This is encouraging, notwithstanding some of the evidence before the Commission. Overall, this suggests that the trend has been towards improvements in related party conflicts management across the industry. APRA also identified a number of areas for further improvement that should be considered by all RSE licensees and additional issues have arisen as part of the Commission process.[4]

3.2.2. Dual regulated entities

A dual regulated entity structure is where a RSE licensee is also the Responsible Entity of a managed investment scheme.

Dual regulated entities can provide benefits to consumers through the generation of economies of scale and scope. This can lead to operational efficiencies, lower fees and better outcomes for fund members, provided that any actual or potential conflicts of interest are appropriately dealt with.

ASFA considers that the current division of regulatory responsibility — with APRA responsible for supervision of the RSE and its licensee, but the Australian Securities and Investments Commission (ASIC) responsible for supervision of the managed investment scheme and its responsible entity — is appropriate.

We note that on 30 January 2015, APRA and ASIC wrote to all RSE licensees that are superannuation dual regulated entities, to inform them of measures that would be taken to strengthen regulation of these

[2] *Superannuation Industry (Supervision) Act 1993*, Part 6 Section 52(2)(d)
[3] APRA, Prudential Standard SPS 521, Conflicts of Interest
[4] APRA, letter to RSE licensees, *Related party arrangements thematic review*, 29 May 2018

entities.[5] In summary, the measures resulted in previous regulatory exemptions being lifted so that each entity had to ensure it met the resource and risk management requirements of their respective regulator.

The trustee of a dual regulated RSE licensee is required to prioritise the interests of superannuation fund members over and above the interests of the shareholders or any other related body, however the Commission has raised concerns as to whether this conflict is being managed appropriately.

There is merit in making explicit the right of the trustee to obtain independent advice on potential and actual conflicts.

Another practical reform is to require there to be a significant proportion of separate directors for the responsible entity and RSE licensee, including a separate chair. It needs to be acknowledged that this is likely to increase costs associated with additional directors and an alternative approach could involve strengthening the conflicts management framework, such as the use of conflicts management committees.

The trustee board's relationship to other boards (responsible entity or other) in the conglomerate entity should be clearly documented in relevant group and trustee policies. The role of the trustee boards as an unencumbered steward of trust property should be explicit in all cases.

ASFA considers that a requirement to have a significant proportion of separate directors for the RSE licensee and responsible entity, including separate chairpersons, could help address actual or perceived conflicts of interest in dual regulated entities.

The trustee board's relationship to other boards (responsible entity or other) in the conglomerate entity should be clearly documented in relevant trustee and group policies, clearly designating that the trustee will perform its role unencumbered.

3.2.3. Related party service providers

An issue that has come up during the course of the Commission is whether the purchase of services from a related party is in the interest of the members of the fund, such as circumstances where there is common ownership with the issuer of a life insurance policy held by the trustee.

APRA Prudential Standards and Guidance prescribe a number of requirements for trustees to meet when outsourcing to related bodies corporate.[6] In particular, the guidance requires that the trustee consider "the impact of group/related party expectations and how the other interests are managed when an RSE licensee is considering the best interests of beneficiaries". Also, "where the conflicts management policy does not cover specific conflicts issues related to outsourcing, APRA expects that the outsourcing policy would do so."[7]

Properly managed, there can be efficiency, cost and risk management benefits associated with providing superannuation products through an integrated financial services organisation. Trustees have typically used a variety of mechanisms, such as due diligence and market surveillance, to test the competitiveness of arrangements that are in place.

However the Royal Commission has raised concerns that controls in place are not always effective, with a particular issue of whether the pricing of such services is competitive.

A requirement to more rigorously validate the selection of related party service providers could strengthen industry practice and improve conflicts management. One possible mechanism might be to require

[5] ASIC and APRA letter to RSE licensees re: legislative reform of superannuation dual regulated entities, 30 January 2015
[6] Standard and Guide 231
[7] PPG 231 paras 10 & 11

enhanced assurance processes that provide additional comfort around the trustee's decision. This could include review of the determination by relevant committees, internal auditors, or an appropriately qualified independent third party. Another would be to require rigorous benchmarking be undertaken that demonstrably supports the trustee's decision.

ASFA considers that a requirement to more rigorously validate the selection of related party service providers could strengthen industry practice and improve conflicts management. Mechanisms to achieve this could include:

- enhanced assurance processes to provide comfort that arrangements are in the best interests of fund members
- rigorous benchmarking that demonstrably supports the trustee's decision

3.2.4. Prudential codification of best interests and a trustee 'safe harbour'

One of the challenges of operating a superannuation fund is that best interest duties require trustees to determine what is best for the members as a whole, rather than what is best for any particular individual. It might be in the best interests of an individual fund member to pay no fees and receive a large distribution of investment earnings but the interests of all fund members need to be considered along with the overall financial viability of the fund.

Prudential guidance from APRA on best interests would assist trustees to effectively meet their obligations. One option might be for APRA to provide details of what is required in the form of a prudential standard or prudential practice guide. A prudential practice guide could, for example, codify the processes APRA expects trustees to follow in considering the best interests obligation and outline how the trustee ought to act in particular circumstances.

Importantly, prudential guidance should make clear that fulfilment of the duty relates to the trustee's decision-making and governance processes. It is not the outcome of particular decisions that should be scrutinised but rather the process followed by the trustee, in good faith, to determine a course of action at a particular point in time. ASFA recommends the introduction of a safe harbor from prosecution for trustees who meet these requirements, similar to that operating for financial advisers in relation to their prescribed best interests duty contained in the Corporations Act.

Such codification and the development of a 'safe harbour' would more clearly define APRA's expectations as to the discharge of specific trustee duties contained in the SIS Act. It is also likely to generate shared interpretation and more consistent levels of conduct across the industry. This could also occur through legislation as discussed in the section below.

APRA prudential guidance would assist trustees to more effectively implement their best interests' obligations. The guidance should focus on the trustee's decision-making process and governance.

ASFA also recommends the introduction of a safe harbor for trustees who meet the requirements.

3.2.5. Increasing trustee understanding and capability

ASFA considers that - prior to commencing their role - trustees should be required to complete a certificate IV level course in the responsibilities and obligations in being a director of a corporate trustee of a superannuation fund provided by a Registered Training Organisation. This will ensure that trustee directors are aware of, and understand, the scope and nature of their responsibilities, including acting in the best interests of members and managing conflicts of interest and duty.

In comparison, people who are appointed as directors of corporations often complete an Australian Institute of Company Directors (AICD) course, or similar, with respect to their responsibilities and obligations as a company directors. Given the additional requirements to be met by the trustee of a superannuation fund, such as exercising trustee and fiduciary duties, it is important that a director of a superannuation trustee receive additional training with respect to these obligations.

There would need to be a suitable transition period for existing trustee directors to complete such a course. Consideration could also be given to the need for trustee directors to complete a refresher course after a specified period in the role, perhaps every three years.

Extending these training requirements to executives and senior management would assist them to better understand these trustee obligations and operate in accordance with them.

ASFA considers that - prior to commencing their role - trustees should be required to complete a certificate IV level course in the responsibilities and obligations of being a director of a corporate trustee of a superannuation fund provided by a Registered Training Organisation. Extending these requirements to executives and senior managers within superannuation funds is also worth consideration.

4. Best Interests Duty

825.19 Would it be preferable to extend the obligation to act in the best interests of members of a superannuation fund so that:

(i) contravention of the obligation attracts a civil penalty; and

(ii) the obligation (and the civil penalty for breach) extends to shareholders of trustees and any related bodies corporate (within the meaning of the Corporations Act) of the trustee in respect of any conduct that will affect the interests of the members of the superannuation fund?

4.1. Civil penalties

4.1.1. Contravention attracting a civil penalty

It may be worth considering extending the obligation to act in the best interests of members of a superannuation fund so that a wilful or reckless contravention of the obligation attracts a civil penalty to the fund.

Currently, as a covenant which is statutorily deemed to be incorporated into the fund's governing rules, a failure to act in the best interests of members represents a breach of trust. A breach of trust can only be enforced by a beneficiary in the equitable jurisdiction of a State or Territory Supreme Court, and there is a limited range of remedies available.

If there is to be an extension of civil penalties, at a minimum it should include protections similar to those contained in the common law and the *Corporations Act 2001*, for example for honest mistakes and actions undertaken in good faith.

ASFA considers that APRA should be able to impose a sanction for a failure to act in the best interests of members – either through a civil penalty being imposed by a court or through the imposition of a condition on a licence or the revocation of an authorisation or licence.

If there is to be an extension of civil penalties it should include protections for honest mistakes and actions undertaken in good faith.

4.1.2. Extension of obligations and civil penalties to shareholders of trustees

Notwithstanding the above points, we query the extension of the best interests obligation (and the civil penalty for breach) to shareholders of the trustee, and any related bodies corporate (within the meaning of the Corporations Act) of the trustee, as - notwithstanding any potential and real conflicts of interest and duty – the shareholders do not control the action of the trustee.

Extending the obligation runs the risk of unintended consequences. For example, imposing an obligation to act in the best interests of members of a superannuation fund on shareholders of the trustee and any related bodies corporate would effectively amount to imposing a fiduciary obligation on them.

It ought to be – and is – the unfettered role of the trustee to act as a fiduciary with respect to the beneficiaries of the trust, but not the shareholders or related bodies corporate. The trustee has a fiduciary obligation to manage any conflicts of interest and conflicts of duty that arise between the interests of the members of the fund and those of the trustee's shareholders and related bodies corporate.

ASFA does not consider it appropriate to extend the obligation (and the civil penalty for breach) to shareholders of trustees and related bodies corporate, as it is the role of the trustee to act independently as a fiduciary with respect to beneficiaries of the trust.

4.1.3. Consequences of amending the penalty regime

825.20 Are there unforeseen consequences of such a legislative intervention that would make it undesirable to strengthen the SIS Act in this way?

There would be benefits to extending the SIS Act in such a way. The key benefit is that this would enable a regulator to take direct action, as opposed to one or more members having to take action for a breach of trust in the Supreme Court of a State/Territory. Furthermore, it would serve to clarify/confirm the obligation in a Commonwealth Act and render it subject to the jurisdiction of Federal/Commonwealth courts, thereby ensuring consistency for all members.

The major issues with respect to extending the obligation to act in the best interests of members of a superannuation fund, so that a contravention of the obligation attracts a civil penalty, include:

- defining what it is to (fail to) act in the best interest of members. The nature of the obligation to act in the best interests of members means that each case will very much turn on its facts. Accordingly, it will be important to define the obligation as a process which the trustee must go through to make a particular decision and, correspondingly, a contravention being a failure to follow that process, as opposed to the outcome not being in the best interests of members
- effectively codifying what is a common law obligation will mean that – to the extent that the language used to describe the obligation varies from that used in common law - it may serve to reduce the precedent value of those judgements
- determining who would have standing to bring an action. This could be given to one or more regulators, including APRA and/or ASIC, and presumably would need to be exercised in conjunction with the Director for Public Prosecutions
- determining the appropriate forum in which an action would be brought and the contravention/penalty determined. Given superannuation is a matter subject to Commonwealth regulation and legislation the Federal Court may be the appropriate jurisdiction.
- ensuring that there are sufficient resources available to ensure the regulators are resourced appropriately
- bringing an action before the courts can prove to be very resource intensive and expensive, both in term of time as well as money, including the diversion of resources and the opportunity costs this can represent. This can prove costly and ultimately, in some case, the cost/benefit analysis may prove not to be in the public interest. While court action should be used as a last resort, nevertheless the ability to impose a penalty for a contravention of a legislative obligation often represents the ultimate 'stick'. Having said that, often the making of an enforceable undertaking has both a general and a specific deterrent effect, as well as serving as an educative mechanism for the industry.

If the proposal to extend the obligation were to proceed it would be imperative that

- regulators performing their functions as required
- to the extent possible – there is an appropriate level of prescription and certainty about the nature and scope of the trustee's obligations. This will provide clarity to all stakeholders concerned and mitigate the risk of an action needing to be taken or of the action being unsuccessful.

5. Conflicts of Interest – Specific Matters

5.1. Financial advice

Access to good quality financial advice for superannuation fund members is vital and will be of increasing significance as the system matures and the range of retirement products becomes more diverse and complex.

As a Queensland University of Technology research paper reveals, not only does advice provide tangible benefits such as tailoring investment strategy to an individual's circumstances and navigating the social security and tax systems, it also contributes to well-being through greater understanding, security, and a sense of control, all of which support peace of mind.[8]

The way financial advice is delivered is also likely to continue to change with the growth of FinTech and/or what is commonly called robo-advice.

In this changing and evolving environment it is important in formulating policy to distinguish between the pre and post Future of Financial Advice (FOFA) periods as policy developed to address legacy issues may have unintended consequences for members receiving advice in the modern regime. It is also important to ensure that any reform does not constrain innovation in the way financial advice is provided. The settings of the post-FOFA regime are being further strengthened by the training, education and ethical standards sponsored by the Financial Adviser Standards and Ethics Authority (FASEA).

5.1.1. Grandfathered commissions

825.15 Are legislative interventions to remove grandfathered commissions and ongoing service fees from superannuation accounts appropriate? If so, why? If not, why not?

Trailing commissions were grandfathered as part of the FOFA reforms in recognition of the potential for disruption an outright and immediate ban on commission would cause to the provision of advice for certain members, and potential Constitutional issues associated with a complete ban. If this mechanism for remunerating a financial adviser is clearly disclosed and the member understands and accepts the arrangement there is nothing inherently objectionable in a trailing commission. ASFA notes that the Productivity Commission in its draft report[9] calls for clear and annual disclosure of the cost of trailing commissions to members and the public but does not recommend a ban on grandfathered commissions.

However ASFA accepts that trailing commissions can provide perverse incentives for businesses and financial planners. They are also commonly perceived as a more expensive and inferior arrangement to the modern approach of upfront fees and renewing ongoing fee agreements every two years. This can give rise to the perception of inconsistent treatment for different classes of members.

ASFA also considers it is appropriate that where a fee or commission is charged for the provision of advice, it should be incumbent on the recipient of that fee or commission to provide a relevant service for the benefit of the member that justifies receipt of the payment.

[8] Prof Cameron Newton, Prof Stephen Corones, Dr Kym Irving, & Drew Thomas (2015) *The Value of Financial Planning Advice: Process and Outcome Effects on Consumer Well-being,* Queensland University of Technology

[9] Productivity Commission, Draft Report, *Superannuation: Assessing Efficiency and Competitiveness*, draft recommendation 5, April 2018

For these reasons ASFA supports the introduction of a termination or 'sunset' date for grandfathered commissions with the length of the transition phase of one year. Appropriate transitional arrangements would permit an orderly transfer from trailing commissions to upfront fee for service and ongoing opt-in arrangements in relation to financial advice. Importantly, they will also facilitate superannuation businesses transferring members to more modern products, in their best interests.
There are a number of transitional issues to consider. The focus should be on getting members out of legacy products and into rationalised, streamlined products with scale and commercial benefits:

- Impediments to transitioning members to more modern products should be removed. For example there should be CGT relief that promotes better member outcomes.
- Transition arrangements should support efficient, cost-effective transfers, in members' best interests. A fund may determine that a single project for commission removal and successor fund transfers will limit costs to members.
- Successor fund transfer rules are important. Transfers will need to be managed to ensure the members are not disadvantaged.
- Grandfathering rules also apply to managed investment schemes, wraps and investor directed portfolio services. The size, cost and complexity of transition across the broader industry should not be underestimated.

ASFA supports ending grandfathered trailing commissions with a one year transition period from the date of legislation that supports an orderly transfer to modern arrangements.

To achieve the best outcomes for members there are a number of transitional issues that must be addressed so that successor fund transfers to more modern products can occur without impediment.

5.1.2. Access to financial advice

825.16 Are there possible detrimental effects on the provision of high quality financial advice by such changes? If it is said that there are such detrimental effects, then the detriments and the reasons for the detriments should be precisely identified. For example, if it is said that it is unlikely that consumers will be willing to pay for the true value of financial advice then, amongst other things, it ought to be explained how the "true value" of financial advice is to be determined, why consumers will pay for the true value of other services but not for financial advice and why it is not sufficient to allow consumers to make an informed choice as to the specific price that is to be paid for a specific service.

ASFA is of the view that access to the different types of financial advice is vital to superannuation fund members as they consider financial decisions in the accumulation phase and in retirement. To maximise access for members to financial planning advice the options for funding these services should be as flexible as possible. ASFA considers that requiring all members to pay for financial advice upfront would significantly reduce access to such services and the likelihood of members seeking advice.

5.1.3. General, intra-fund or scaled advice

ASFA supports maintaining the status quo for general, intra-fund or scaled advice which gives trustees the option of including the cost of these types of advice in the general administration fee or charging an additional fee at their discretion. While we acknowledge that not all members will make use of this service we consider that making it strictly fee-for-service will increase the costs charged to individual users. This would discourage members from making use of it which could leave them worse off individually and as a group if, for example, the fund determined not to provide such services due to very low take-up rates.

ASFA conducted a survey on the provision of financial advice in 2014 and found that the provision of these types of advice was low cost and resulted in minimal cross-subsidisation between members[10]. Members often seek advice only after certain events in their lives turn their attention to financial matters, such as the birth of a child, a serious injury or illness, redundancy, promotion, or a change in financial market conditions. ASFA regards access to low cost advice charged through the general administration fee at such times as a significant benefit to members.

5.1.4. Full personal advice

ASFA supports members being able to pay for personal advice fees from their superannuation fund balance subject to the sole purpose test and FOFA constraints. This should only be available if a service has clearly been provided and with the member's consent.

With regard to ongoing financial advice fees, there is already a raft of opt-in, fee disclosure statement and other rules around ongoing fees and there also some exemptions if the financial planner complies with a relevant ongoing fees Code. For example the Financial Planning Association (FPA) has an ongoing fees code with ASIC approval that exempts planners from some requirements. ASFA considers that given the evolving state of financial planning regulation and standards there may in the future be a need to look at the potential benefits of stricter rules for opt-in requirements, benchmarks and reporting, and/or a link to the new Financial Adviser Standards and Ethics Authority (FASEA) that is being developed now.

ASFA is of the view that access to the different types of financial advice is vital to superannuation fund members as they consider financial decisions in the accumulation phase and in retirement.

To maximise access for superannuation fund members to financial planning advice, ASFA supports:

- Trustee discretion with regard to the charging of intra-fund advice fees from the general administration fee
- Maintaining the existing right of members to pay for full personal financial advice from their superannuation account balance if they elect to do so, and where the fee disclosure statement and opt-in requirements are being met

5.2. Selling superannuation through bank branches

825.7 Is it appropriate that superannuation be sold through bank branches? Is it reasonable to think that there is any prospect that this is likely to produce an outcome that is in the best interests of consumers?

825.8 Are there statutory reforms that are required to address this problem (if it is a problem) or are the existing laws with respect to personal financial advice and general financial advice sufficient?

The starting principle should be that the right advice or information is made available to all Australians, whether that is through a bank branch or another channel. The existing framework allows for that advice or information to be provided irrespective of channel and this is appropriate.

Singling out of one particular type of entity could trigger unintended consequences, in particular around definitions, demarcation and coverage. In line with our earlier comments in relation to structural reform, we do not consider the best way to address issues arising from conflicts is through banning particular types of entities from providing services. Instead, it is appropriate to establish a framework conducive to the provision of those advice and information services with integrity that is channel or entity agnostic.

[10] ASFA survey on the provision of financial advice by superannuation funds, Ross Clare, 2014

In that regard, the focus should be on ensuring appropriate consumer protections apply to the provision of advice and information. Such protections include adequate disclosure, suitable education and training requirements for providers and monitoring and enforcement of conduct by ASIC.

The delineation between general, intra-fund and full personal advice can be indistinct. The framework should be reviewed holistically to clarify what constitutes the different types of advice and what education and training requirements are appropriate for each (acknowledging that FASEA is reviewing education and training standards for personal advice).

ASFA considers that it would be preferable to look at these issues holistically rather than making piecemeal changes. Such changes may contribute to the existing complexity and be counterproductive.

ASFA considers the starting principle should be that the right advice or information is made available to all Australians, whether that is through a bank branch or another channel.

We do not consider that the best way to address issues arising from conflicts is a unilateral ban on particular types of entities from providing services or prescription of industry structures.

Issues arise due to a lack of clarity around what constitutes general, intra-fund and personal financial advice. A holistic review of these categories should be undertaken to clarify what constitutes the different types of advice and what education and training requirements are appropriate for each.

5.3. Section 68A of the SIS Act - providing benefits to employers

825.3 Is it appropriate, as a response to conduct of superannuation trustees that seeks to induce employers to select funds, or affect their decisions as to default funds, to make alterations to section 68A of the SIS Act to widen the prohibition?

Section 68A is a long standing provision of the SIS Act.

ASIC is continuing to monitor the area of employer inducements and has indicated that where it finds evidence of illegal inducements being offered it will not hesitate to take action.[11]

Broadening the provision could have a number of unintended consequences. For instance, many funds take considerable effort in order that they are easy to deal with for employers. This can include the provision of service, information and education. This is a benefit to employers but it is not something that should be made illegal for funds to pursue.

While ASFA considers the provision to be sufficient, we note the industry would benefit from greater clarity from the regulators in relation to the specific conduct that contravenes section 68A.

ASFA considers that the current section 68A provision is sufficient and that any issues relate more to its enforcement rather than its content.

Industry would benefit from greater clarity from the regulators in relation to the specific conduct that contravenes section 68A.

[11] ASIC, media release 16-038MR, *ASIC guidance to employers about super*, 17 February 2016

5.4. Payments from external responsible entities of managed investment schemes

825.6 Is it appropriate for the trustee of a superannuation funds to retain payments from the responsible entity of a managed investment scheme where that payment is derived from the investment of members' money?

ASFA considers that the key consideration in relation to payments from the responsible entities of managed investment schemes is that they do not influence the trustee's selection of investment managers.

The services provided by a trustee need to be funded and such payments may quite reasonably form part of the overall funding. For example, where a trustee needs to undertake a due diligence process in order to decide whether to include a managed investment scheme on a superannuation platform it may be appropriate to charge a set sum to the scheme to help offset the costs to the trustee of that process.

Any conflicts of interest must be carefully managed by a superannuation fund. Selection of a managed investment scheme to be included within the range of investment options offered should not be affected by the amount that the responsible entity is willing to pay to the trustee.

ASFA notes that FOFA implemented a legislative ban on conflicted remuneration and volume based fees are generally not allowed.

ASFA considers that the key consideration in relation to payments from the responsible entities of managed investment schemes is that they do not influence the trustee's selection of investment managers.

6. Regulators

6.1. Deterrence and insight

There are four regulators for the superannuation industry — APRA, ASIC, the Australian Taxation Office (ATO) and the Australian Transaction Reports and Analysis Centre (AUSTRAC). The Commission's inquiry has examined only the roles of APRA and ASIC, and ASFA's comments in this section are similarly focused solely on those two regulators.

ASFA considers that the 'twin peaks' regulatory model, which broadly gives APRA jurisdiction over prudential matters and gives jurisdiction for consumer protection, conduct and disclosure to ASIC, is the right structural approach. It is important to clearly separate prudential and consumer regulation.

However, given the issues brought to light by the Royal Commission, ASFA considers it timely and appropriate that the model is reviewed and any necessary adjustments are made to ensure both regulators are able to operate effectively to achieve their respective mandates.

6.2. Encouragement toward prompt action on (potential) misconduct:

825.25 What can be done to encourage the regulators to act promptly on misconduct or potential misconduct?

To maintain confidence in the system it is necessary that regulators act promptly and appropriately to investigate and address misconduct or potential misconduct. However, in ASFA's view, this does not mean that the pursuit of civil penalties is the appropriate outcome in all cases or that all enforcement action should automatically be made public.

While APRA has received criticism for essentially operating 'behind closed doors', that approach will, in many cases, be both appropriate and consistent with APRA's mandated focus on the stability of the system. Rather than increasing stakeholders' confidence in a particular sector or the financial services industry overall, public regulatory action may actually diminish confidence, if it is undertaken:

- frequently, for (potential) misconduct that is minor in nature and impact; or
- precipitously, in circumstances where the (potential) misconduct is not ultimately proven.

ASFA agrees with comments in relation to APRA's regulatory approach made by Treasury in its recent submission to the Commission. Treasury noted that APRA's regulatory approach is one of "consultative risk-based supervision", intended to deliver early identification and evaluation of potential risks to ensure they are addressed before they pose a threat to a regulated firm or its beneficiaries. Treasury acknowledged that the "vast majority of actions taken by APRA do not involve any formal exercise of APRA's enforcement powers. Rather, APRA works with the boards of the relevant firms as they take appropriate steps to address issues". Importantly, Treasury notes that this approach is broadly consistent with the approach adopted by prudential regulators in comparable jurisdictions and with that advocated by international regulatory standard setting bodies".[12]

[12] Treasury, Financial Services Royal Commission, *Submission on key policy issues*, 13 July 2018 (uploaded to the Commission's website as Background Paper No 24), paragraphs 107 - 108

While ASFA is of the view that the current regulatory architecture remains broadly appropriate, we accept that there is always scope for improvement. Evidence elicited by the Royal Commission has highlighted a number of instances where the regulators could have taken action earlier, or could have increased their regulatory intensity in response to indications of potential non-compliance or misconduct. ASFA considers the regulators have significant powers and before further consideration of additional powers being provided, a full capability review would be beneficial. This will support APRA and ASIC in prosecuting their mandates more effectively.

In our response to Q825.26 we have recommended a detailed review of the regulatory mandates of APRA and ASIC to identify and address any specific gaps or overlaps. In the comments immediately below, we have identified a number of matters that may — alone or in combination – serve to impede prompt regulatory action.

ASFA is of the view that the regulators have significant powers and should demonstrate effective use of these prior to consideration of additional powers being provided.

ASFA considers that a detailed review of the regulatory mandates of APRA and ASIC to identify and address any specific gaps or overlaps is warranted.

6.2.1. Resourcing and capability

It is inevitable that an examination of the regulators' performance will raise questions about whether they are adequately resourced to perform their roles. ASFA considers that simply increasing resources, without deeper analysis, is unlikely to deliver a meaningful improvement in the regulators' performance. In ASFA's view, a number of factors need to be considered in relation to the resourcing and capability of the regulators.

Firstly, ASFA considers it critical that the regulators are funded to a level that is appropriate to enable them to fulfil their regulatory functions, while balancing the impost on industry and, indirectly, on consumers.

It is also important to ensure that the regulators apply their funding in an effective manner, including by directing resources to those supervisory/enforcement activities which deliver appropriate outcomes in terms of the cost-benefit differential. In this respect, we note that ASIC has recently announced its intention to increase its 'shadow shopping' activity in relation to superannuation[13]. We understand that ASIC's ability to undertake such exercises has in recent years been limited by resource constraints. This is a matter of some concern, as shadow shopping is an activity that is ideally suited to early identification of potential non-compliance or misconduct.

Secondly, it is necessary to ensure that the regulators have access to an adequate level and mix of resources, including appropriately skilled and experienced staff. This should specifically include consideration of whether sufficient resources are directed toward investigation of (potential) misconduct and the pursuit of appropriate enforcement activity. A number of actions have already been undertaken that should improve the manner in which resources are accessed and applied by the regulators, both generally and specifically in relation to enforcement. These include:

- the recent capability review of ASIC[14], ASIC's response to that review[15] and some reforms arising from it — such as allowing flexibility in terms of recruitment by removing the requirement for ASIC to engage staff under the *Public Service Act 1999*[16]

[13] James Shipton, Chair, ASIC - *The trust deficit and superannuation* – speech to Financial Services Council Summit 2018, 26 July 2018

[14] Australian Government ASIC Capability Review Expert Panel, *Fit for the future: A capability review of the Australian Securities and Investments Commission*, April 2016

- the adoption of a fully industry-funded cost recovery model for ASIC
- allocation of additional funding specifically toward increasing ASIC's enforcement activity[17]
- appointment of a second deputy chair for ASIC, with responsibility specifically for enforcement activity[18], and a second deputy chair for APRA[19]
- an operational restructure of APRA which has refocused its approach to supervision of superannuation trustees.

These actions are recent and in some cases ongoing, and ASFA is of the view it may be premature to assess their effectiveness.

Thirdly, resourcing needs should be continually monitored against changes in the regulatory environment and informed by comprehensive capability reviews of both regulators. The Financial System Inquiry (2013-14) recommended periodic capability reviews of *all* financial system regulators, to identify any gaps in their regulatory toolkit and ensure they have the required skills and culture to maintain effectiveness in an environment of rapid change.

A capability review was performed for ASIC in 2015-16. As noted above, some reforms have been implemented (or are in progress) to address key recommendations.

To date, a formal, public capability review process has not been conducted for APRA. ASFA acknowledges that some enhancements to APRA's regulatory arrangements have been made since the Financial System Inquiry. These have included changes to its internal governance arrangements and enhancement of its powers in relation to financial services more generally. Further, APRA's current corporate plan lists a number of initiatives directed at improving APRA's capability to identify, assess and respond to a changing environment. However, it does not appear that these developments have been informed by a comprehensive and independent review, with input from external stakeholders, to the extent undertaken for ASIC.

ASFA considers it appropriate that at the conclusion of this Royal Commission, a further capability review of ASIC is conducted, and a capability review is performed for APRA, to ensure both regulators are well placed to implement the Commission's recommendations.

Finally, it is important that the regulators provide an appropriate level of transparency to all stakeholders — including the Government, industry participants and consumers — as to their utilisation of allocated funding and resources. This should specifically include information on the resources allocated toward enforcement activity and the outcomes of that activity.

ASFA has also recommended that increasing transparency over the calculation, allocation and use of levies raised from industry would provide appropriate insight into regulators' activities and build confidence that the regulators are functioning well. Transparency is particularly important given ASIC has recently moved to a fully industry-funded model and the annual levy collected from trustees by APRA now involves full recovery of all supervisory costs incurred by APRA and other relevant agencies including the ATO.

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[15] ASIC – *ASIC Capability Review – ASIC Implementation Plan*, April 2016

[16] These amendments passed through Parliament on 17 September 2018, in the *Treasury Laws Amendment (Enhancing ASIC's Capabilities) Bill 2018,* and await Royal Assent

[17] The Hon Scott Morrison MP and Kelly O'Dwyer MP, Media Release, *Turnbull Government expands ASIC's armoury*, 7 August 2018

[18] Following the passage of the *Treasury Laws Amendment (ASIC Governance) Act 2018*

[19] Following the passage of the *Treasury Laws Amendment (APRA Governance) Act 2018*

ASFA considers that the regulators should provide greater transparency in relation to their use of resources on an annual basis. This should include specific reporting in relation to the resources assigned to enforcement activities and the outcomes from those activities.

6.2.2. Utilisation of reported data to inform regulators' engagement

Access to appropriate data, and insightful analysis of that data, are key factors that will help enable the regulators to identify potential misconduct early. Superannuation trustees currently report substantial volumes of data to the regulators, particularly to APRA, on a quarterly, annual and ad hoc basis. It is not clear that either regulator has yet optimised its use of this data for supervisory purposes, despite each receiving specific funding allocations in recent years to enable them to enhance their analytics.

ASFA is of the view that a deeper analysis of reported data could be used by both regulators to inform their regular engagement with superannuation trustees and better focus that engagement on potential areas of concern. In this respect we note that APRA has had an engagement model in place for supervision of trustees since its inception and ASIC has recently signalled that it will adopt a more intensive engagement model for superannuation.

We note that APRA's corporate plan for 2018-22 acknowledges the need to improve its use of data and notes that the "increasingly interconnected nature and complexity of financial system risks requires APRA to better leverage a broad range of data and information to enhance the quality and speed of decision making"[20]. ASFA welcomes the commitments made in the plan, including to 'articulate a well understood data strategy to enable better decision-making'. ASIC's corporate plan similarly shows an increased emphasis on the use of data to inform its supervisory activities.

ASFA considers that there is scope for both APRA and ASIC to improve their analysis of data reported by superannuation trustees to better inform their engagement and supervisory activities. This should enable the regulators to more promptly identify emerging issues and (potential) misconduct.

6.2.3. Adequacy and appropriateness of breach reporting regimes

In addition to closer monitoring of data reported under trustees' ongoing reporting obligations, it is also imperative that the regulators receive adequate and timely data in relation to breaches, or potential breaches, of the legislative regimes.

It is important to ensure that the regimes for self-reporting of breaches by superannuation trustees and other financial services providers are framed to provide timely information to enable the regulators to assess the magnitude of any (potential) misconduct, and that the regulators actively monitor and enforce compliance with those regimes.

Evidence heard by the Royal Commission to date has highlighted significant concerns with the adequacy of the breach reporting regime, and the approach taken by licensees toward compliance with that regime, for both Australian Financial Services (AFS) and RSE licensees. In particular, concerns have been raised about the time taken by licensees to identify breaches internally, investigate those breaches, and report them to the relevant regulator.

The ASIC Enforcement Review Taskforce recently examined the breach reporting obligations imposed on AFS licensees under the Corporations Act, and made a number of recommendations to clarify and strengthen the existing regime. The Taskforce considered the adequacy of the frameworks for notifying ASIC of breaches of law, including the triggers for the obligation to notify and the time in which notification is required to be made. The Review recommended that:

[20] APRA, 2018-22 Corporate Plan, page 16

- the 'significance test' for reporting of breaches should be clarified to ensure that the significance of breaches is determined objectively
- the time for reporting should be extended from 10 to 30 days, but licensees should be required to make a report if they are investigating a breach and have not determined, within 30 days, whether it meets the significance threshold.

The Taskforce concluded that implementation of these recommendations would "strengthen the reporting regime by ensuring that failures to report, objectively determined as such, can be more effectively sanctioned and increasing the incidence of reports, by requiring a report to be made within 30 days, even if a breach investigation has not been finalised"[21].

The Government has agreed in principle to the Taskforce's recommendations, but has deferred any implementation of them to enable it to take into account any relevant findings arising out of this Royal Commission.

ASFA considers that the Government should, as soon as practicable following the conclusion of the Royal Commission, provide clarification as to any intended reform of the breach reporting obligations for AFS licensees.

In contrast, the breach reporting regime for RSE licensees has not been updated or reviewed since 2007[22]. At that time, the breach reporting timeframe imposed on RSE licensees by the SIS Act was revised from 14 days to 10 business days, to align it with the timeframe specified in other prudential Acts.

ASFA sees considerable merit in a review of RSE licensees' breach reporting obligations, similar to that undertaken by the ASIC Enforcement Review Taskforce. This should consider:

- whether the legislative regime requires modification; or
- if issues in relation to breach reporting by RSE licensee can be addressed by providing clearer guidance as to licensees' obligations under that regime — for example, regarding the appropriate interpretation of the factors that must be taken into account when determining whether a breach is 'significant' — and more stringent monitoring of compliance by APRA.

ASFA is of the view it would be beneficial to conduct a review of RSE licensees' breach reporting obligations — similar to that undertaken by the ASIC Enforcement Review Taskforce — to identify and address any impediments to the timely provision of information to APRA.

ASFA supports alignment — to the extent possible — of the breach reporting regimes administered by APRA and ASIC.

6.2.4. Strengthened communication and co-operation between the regulators

As noted above, access to information is a key factor that may enable a regulator to act more promptly to address (potential) non-compliance or misconduct. Each of the regulators has access to considerable volumes of data that should, if analysed effectively, provide insight on emerging risks (both sector-wide and entity-specific). In some cases, it may only be possible to draw those conclusions where data is shared. Given the overlap between their regulated populations and the division of regulatory responsibilities, it is vital that the regulators are in close communication and work co-operatively to identify and address potential risk areas.

[21] ASIC Enforcement Review Taskforce Report, December 2017, recommendations 1 and 4
[22] In the context of the *Financial Sector Legislation Amendment (Simplifying Regulation and Review) Act 2007*

ASFA acknowledges that the regulators have mechanisms in place for information sharing, however we consider that these should be subject to a process of continuous review and improvement, to ensure they are operating effectively. As recently noted by Treasury, the regulators' ability to effectively share information is affected by legislative restrictions to maintain confidentiality, systems to make sharing information simple and accessible, and the capabilities of staff to identify information of common interest[23]. ASFA has commented above on the need to assess (and, if necessary, enhance) the regulators' capability and to improve data analytics. To the extent that the regulators perceive any legislative restriction to effective communication and co-operation, ASFA would support action to remove it.

In addition, given the commonality of their regulated populations, ASFA sees scope for APRA and ASIC to undertake a greater level of joint supervisory action — as has occurred recently in relation to life insurance claims and claims-related disputes[24]. In such cases, publication of joint reports or guidance material is particularly beneficial as it provides:

- clear messaging to industry participants regarding the regulators' expectations without any potential for inconsistency between the regulators
- positive confirmation to all stakeholders regarding the ability of the regulators to work collaboratively across their shared regulatory responsibilities.

APRA and ASIC should continue to work actively toward strengthening their communication and co-operation regarding general and specific risks and behaviours in financial services.

6.3. Allocation of regulatory responsibilities

825.26 Is the present allocation of regulatory roles appropriate to achieve specific and general deterrence from misconduct?

825.27 Given that what we are fundamentally concerned with is conduct that in subtle but ongoing ways negatively affects the retirement outcomes of consumers, are either of the regulators best placed to carry the responsibility to protect consumers should the balance between them be restructured or significantly altered?

Given the increasing scale and complexity of the Australian financial services industry, it is important that the roles and responsibilities of the regulators are continuously monitored, and are not seen as 'carved in stone'.

ASFA acknowledges that questions have been raised — both within the context of the Commission and more broadly — regarding the allocation of regulatory responsibilities between APRA and ASIC. In particular, we note concerns about the extent to which ASIC's mandate has increased in breadth since its establishment in 1998.

ASFA is of the view that the present allocation of regulatory responsibilities remains broadly appropriate. Specifically, we consider that APRA's primary focus should remain on prudential regulation and the stability of the financial system and that ASIC should maintain regulatory responsibility for conduct, disclosure and consumer protection.

[23] Treasury, Financial Services Royal Commission, *Submission on key policy issues*, 13 July 2018 (uploaded to the Commission's website as Background Paper No 24), paragraph 124

[24] ASIC Media Release 18-150MR, APRA and ASIC release new life-claims data, 24 May 2018

However, we accept that this distinction may not always be clear-cut in practice, and that there is the potential for 'grey areas' to develop. Accordingly, ASFA would support a detailed review of the regulatory mandates for APRA and ASIC, to identify any gaps or overlaps — whether actual or perceived — and ensure that these are clearly addressed.

One area that has received specific attention during the Commission relates to supervision of dual regulated entities, in particular structures where an entity may be the RSE licensee for a superannuation fund and also the responsible entity for a managed investment product. As we have expressed in our earlier section on this issue, ASFA considers improvements to governance and conflicts management can address the concerns that have been raised.

We anticipate that a review of the regulatory mandates might lead to some rebalancing of regulatory responsibilities for particular aspects of the legislative regimes between APRA and ASIC. We do not, however, believe the evidence currently supports a substantial revision of the current regulatory structure.

Further, while ASFA acknowledges discussion about the desirability of introducing an additional regulator solely for superannuation and retirement products (a 'pensions regulator'), we do not consider it warranted or appropriate at this time, though as the number of people moving into drawdown increases we suggest reconsidering this possibility in future. While it might be expected that vesting regulatory responsibility for 'pensions' in a single regulator might deliver some efficiencies and streamline the regulatory process, it would undoubtedly cause considerable disruption in the short to medium term. Further, given the complexity of the superannuation/pensions sector and its interrelationships with the broader financial services sector, isolating regulation for superannuation/pensions may serve to create an artificial silo and compound issues in relation to regulator communication and co-operation.

ASFA considers the current allocation of regulatory responsibilities between APRA and ASIC to be broadly appropriate, but would support a detailed review of the regulatory mandates to ensure that any specific gaps or overlaps (actual or perceived) are identified and addressed.

ASFA does not support the creation of a specific 'pensions regulator' at present.

6.4. Responsibility for consumer protection

Australia's superannuation sector is, predominantly, a defined *contribution* rather than a defined *benefit* model. A defining characteristic of the defined contribution model is that the net retirement outcomes of consumers are impacted by investment returns and are not guaranteed. While ASFA agrees that it is critically important to protect consumers from misconduct we note that this will not, in and of itself, guarantee an increase in returns or in net outcomes for consumers.

While improvement is always possible, ASFA considers that ASIC has generally performed its consumer protection role in an effective manner. We have identified above a number of factors that may assist in encouraging ASIC to take action against (potential) misconduct more promptly. At this time, ASFA considers that ASIC should retain the responsibility to protect consumers of financial services and products, and does not support the transfer of that responsibility to another body.

ASFA considers that ASIC is best placed to carry the responsibility to protect consumers.

7. Engagement by superannuation funds with Aboriginal and Torres Strait Islander people

7.1. Appropriateness of identification procedures

825.9 Are the identification procedures used by superannuation funds appropriate for their Aboriginal and Torres Strait Islander members?

(i) If those procedures are appropriate, are those identification procedures sufficiently understood and implemented by staff on the ground?

(ii) If those procedures are not appropriate, what should be changed?

In 2016 the Indigenous Superannuation Working Group worked closely with AUSTRAC on developing new compliance guidance encouraging funds to look at more flexible approaches to identification requirements for Aboriginal and Torres Strait Islander peoples, including accepting alternative forms of identification where possible, for the purposes of the *Anti-Money Laundering and Counter Terror Financing Act 2006* (AML/CTF Act)[25]. We believe these identification procedures are appropriate for their Aboriginal and Torres Strait Islander members.

Superannuation is different to other financial services because the majority of people do not apply to become a member of a superannuation fund but instead are enrolled by their employer.

Accordingly, trustees are not currently in a position to perform 'know your customer' due diligence on these members prior to providing the designated financial service of receiving contributions. Instead there is a general exemption from the customer identification requirements which permits funds to identify a member at the point in time where the member is rolling over or being paid their benefit.

Given that funds generally do not fully identify members who are enrolled by their employer until the point when a benefit is being paid, there are two aspects to customer identification at this time:

1. for the purposes of the AML/CTF Act
2. for general risk management purposes – to confirming that the person with whom the fund is dealing is the member who is entitled to the benefit.

As such, while funds who conform to the AUSTRAC guidance can be considered to have complied with their obligations under the AML/CTF Act, it is open to funds to determine identification procedures with respect to the second purpose - to ensure that the person they are dealing with is the member - which are appropriate to the risk appetite and risk assessment of the fund.

(i) If those procedures are appropriate, are those identification procedures sufficiently understood and implemented by staff on the ground?

There is room for improvement in the level of awareness by some funds of the AUSTRAC compliance guidance into their procedures. To this end the Indigenous Superannuation Working Group put together a free letter template that organisations can use to inform others that the guidance exists, in order to raise awareness of the existence of the guidance.

Notwithstanding this, as discussed above, a trustee is also under an obligation to ensure that the person with whom they are dealing is the member who is entitled to the benefit. Accordingly a trustee may impose identification procedures to a standard that exceeds those contained in the AUSTRAC Guidance material.

[25] http://www.austrac.gov.au/aboriginal-andor-torres-strait-islander-people

(ii) If those procedures are not appropriate, what should be changed?

ASFA considers the identification procedures developed by the Indigenous Superannuation Working Group working closely with the AUSTRAC are appropriate.

7.2. Requirements to record members identifying as Aboriginal or Torres Strait Islander people

825.10 Should superannuation funds be required to record whether their members identify as Aboriginal or Torres Strait Islander people?

It should not be mandatory for superannuation funds to record whether their members identify as Aboriginal or Torres Strait Islander people.

If it were to be made mandatory this would raise a range of implications such as

- for what purposes would it be used and/or reported
- whether there would be any need for verification, including the complexities surrounding the concept of 'identification as an Aboriginal or Torres Strait Islander'
- the practicalities regarding 'back-capture' of data and/or the period of time it would take for the data to be built up gradually.

825.11 Should those superannuation funds who do not currently permit the early release of superannuation on the basis of severe financial hardship do so?

This question is much broader in its application than just being with respect to Aboriginal and Torres Strait Islander people.

It is important to note that, over and above a member meeting the threshold income support eligibility criteria, a trustee retains discretion to determine

- whether, in their view, a member is in severe financial hardship; and
- the amount which should be released in the circumstances, up to the maximum $10,000 per annum permitted under the regulatory requirements.

As a matter of public policy it has been determined that, where a member is experiencing severe financial hardship, it is appropriate to release an amount of their superannuation. Given this, there is an argument that it should be available to all members (other than perhaps defined benefit members), irrespective of the fund of which they are a member.

Amongst other things this would serve to reduce the incidences where a member uses a fund which does permit early release simply as a conduit to their benefit, whereby the member rolls-over their benefit into the second fund simply for the purpose of being able to access their benefit from that fund.

7.3. Accounting for lower life expectancy of Aboriginal and Torres Strait Islander people

825.12 Should the lower life expectancy of Aboriginal and Torres Strait Islander people be taken into account in the decision-making processes of superannuation funds when considering how to administer or release the funds of Aboriginal and Torres Strait Islander people? If so, how?

The conditions under which benefits can be released are heavily prescribed in the SIS Act and regulations. If a trustee were to take into account the lower life expectancy of Aboriginal and Torres Strait Islander people in their decision-making processes when considering how to release their funds, to the extent that their funds were released early, this would amount to a breach of the regulatory requirements.

Whether the lower life expectancy of Aboriginal and Torres Strait Islander people should be taken into account when considering whether/when their funds can be released is an important public policy question. Due to lower life expectancy Aboriginal and Torres Strait Islanders people will not receive the benefit of superannuation in the way that it has been designed for the majority of the population.

ASFA's view is that there should be a public policy focus should be on improving life expectancy for Aboriginal and Torres Strait Islander people.

The public policy focus should be on improving life expectancy for Aboriginal and Torres Strait Islander people. ASFA would support the government reviewing superannuation settings such as temporarily lowering the preservation age, to provide better access to superannuation benefits for Aboriginal or Torres Strait Islander people. Improving poor life expectancy outcomes must however remain the longer term policy priority.

7.4. Amending binding death nominations to reflect kinship structures

825.13 Should the categories of person permitted by legislation to be the subject of a binding nomination be changed to reflect Aboriginal and Torres Strait Islander kinship structures? If so, how should the categories be broadened?

Binding nominations can be made in favour of a member's dependants and/or the member's estate.

'Dependant' is defined broadly to include people who are financially dependent on the member and those who are in an 'interdependency relationship' with the member. Both of these concepts can have a broad interpretation, as has been found to be the case in a number of Superannuation Complaints Tribunal determinations.

Notwithstanding that these definitions are capable of a broad construct, should the definition of 'dependant' be deemed to be too narrow then ASFA would support consideration being given to broadening the category of 'dependant' to accommodate Aboriginal and Torres Strait Islander kinship structures.

8. Other Policy Issues and System Changes

8.1. Consolidation of multiple superannuation accounts

825.23 Is it appropriate, as a response to the conduct of superannuation trustees that might inhibit the consolidation of multiple superannuation accounts of a person, to introduce some form of "stapling" so that a person's account for receipt of default contributions is linked to the person and travels with the person when she or he changes job? Is this is a practical method of addressing this type of conduct noting that it is not suggested to be misconduct?

In their draft report released 29 May 2018, the Productivity Commission recommended 'stapling' consumers to a single superannuation account.[26] As noted in ASFA's response we consider there are pros and cons associated with the implementation of such a policy.[27]

Combined with a range of other mechanisms (current and prospective), the 'stapling' proposal would help further reduce the stock of unintended multiple accounts in the system over time. However some members might remain in default superannuation products that, while once suited to their circumstances, would become less suitable for them over time – especially with respect to insurance requirements and asset allocations.

To address this, an alternative option that could be explored would involve people defaulting afresh every time they start a new job. If a default member did not choose a new fund upon changing jobs, the individual would be reallocated to a default fund (based on stronger MySuper authorisation or some other criteria). The balance of the individual's current active default account would be rolled into his/her new default account, thereby addressing the risks around disengagement and account proliferation. Individuals who join the workforce for the first time, or who do not have an active account (and do not make a choice), would be allocated to a default product.

It is important to consider there has been very good progress in reducing the number of multiple accounts in the system. Over recent years there have been a number of initiatives to encourage members to consolidate their accounts and to reduce duplicate accounts. The majority of people now have only one account.

Funds have made considerable efforts to engage members to consolidate their accounts, including educating members about the effect of fees on multiple accounts and facilitating consolidation. A number of funds also regularly undertake activities to identify duplicate accounts and, once satisfied they are for the same member, to merge the accounts together.

For some time now a number of funds have also participated in 'cross fund matching' with Eligible Rollover Funds (ERF) whereby a fund has an agreement with an ERF to share information for the purpose of identifying accounts in the ERF which belong to one or more of the members of the fund.

An indicator of the success of funds' initiatives in consolidating accounts is the number of accounts per member, which is trending downwards – from around 2.5 to 1.9 accounts per member over the course of the last decade.

[26] Productivity Commission, Draft Report, *Superannuation: Assessing Efficiency and Competitiveness*, draft recommendation 1, April 2018

[27] ASFA, submission to the Productivity Commission, Draft Report, *Superannuation: Assessing Efficiency and Competitiveness*, 13 July 2018

It should be borne in mind that there are some members who make an active choice to maintain multiple superannuation accounts – to maintain insurance cover, to retain a right to a defined benefit or to access different investment options or otherwise manage investment risk.

A number of government initiatives have also addressed multiple accounts, directly or indirectly, including

- greater utilisation of MyGov to facilitate account consolidation
- an increase to the balance of lost inactive accounts to be transferred to the ATO from $4,000 to $6,000
- use of ASIC's MoneySmart website to raise member awareness
- the transfer of 'accrued default amounts' to MySuper by 1 July 2017
- expanding Single Touch Payroll to provide for new employees to choose their super fund through online access to pre-populated choice forms when enrolling as a new employee.

ATO data shows a steady trend in the reduction of multiple accounts between 2013 and 2016, as demonstrated in the table below:[28]

Number of superannuation accounts	**2013**	**2014**	**2015**	**2016**
1	55.13%	54.90%	56.68%	60.00%
2	25.82%	25.91%	25.48%	24.53%
3	10.78%	10.85%	10.25%	9.20%
4	4.55%	4.59%	4.21%	3.59%
5	1.99%	2.02%	1.82%	1.49%
6 or more accounts	1.72%	1.72%	1.57%	1.19%
TOTAL	100.00%	100.00%	100.00%	100.00%
1 or 2 super accounts	81%	81%	82%	85%
3 or more super accounts	19%	19%	18%	15%

ASFA is supportive of continuing to reduce unintended duplicate accounts. However, there are pros and cons to 'stapling' consumers to a single superannuation account. Consolidating accounts into a new, appropriate default each time a member changes jobs is another option worth considering so that individuals are consistently defaulted into arrangements suitable for their most recent circumstance.

[28] ATO, Super accounts data overview, https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/Super-accounts-data/Super-accounts-data-overview/

8.2. Director appointments - obligations on shareholders of trustees

825.14 Is it appropriate for shareholders of RSE Licensees to retain a broad discretion to appoint and remove directors? Or should there be an obligation imposed on shareholders to exercise such powers in the best interests of the members?

As outlined in our earlier submission to you, ASFA has supported recent improvements to the superannuation governance standards implemented through legislation and prudential standards.[29]

APRA's recently enhanced prudential standards require boards to maintain a skills matrix and require trustees to seek third party evaluation of the performance of the board. Trustees must meet fit and proper requirements prior to appointment that satisfy the Trustee Board and regulators as to their capacity to discharge their duties in the best interests of members.

It is appropriate that shareholders of RSE Licensees retain a broad discretion to appoint and remove directors. Ultimately it is up to the trustee directors to ensure the fund is operated in the best interests of members.

Once appointed, trustees will have access to insights and information relating to fund members, not typically available to the shareholder, that will support them to appropriately discharge their obligations.

The most recent changes to revised SPS 510 and SPG 510 commencing 1 July 2017, require the following of RSE licensee Boards:

- the Board must have a governance framework which includes, at a minimum, the Board's charter (or equivalent document) and policies and processes that achieve appropriate skills, structure and composition of the Board;
- the Board must have a written policy which sets out requirements relating to the nomination, appointment and removal of directors that support appropriate Board composition and renewal on an ongoing basis;
- a Board Remuneration Committee must be established and the RSE licensee must have a Remuneration Policy that aligns remuneration and risk management.

On 17 May 2018 APRA wrote to RSE licensees to inform them as to the outcomes of APRA's board governance thematic review, which commenced in late 2016 and continued over the course of 2017, "to assess how the superannuation industry has responded to SPS 510 and identify better practices and opportunities for improvement in targeted areas of governance…….The review particularly focussed on board appointment and renewal policies and practices, and board performance assessment approaches."

We note that as part of their post-implementation review of the prudential framework, APRA will shortly update their prudential standards to reflect the outcomes of their thematic review focused on board appointment and renewal policies.[30] APRA has indicated they expect to release the outcomes of the post-implementation review by early 2019.

ASFA considers that APRA's post-implementation review of the prudential framework is the most appropriate mechanism to ensure the appropriateness of standards in relation to superannuation governance arrangements.

It would not be desirable to impose what are effectively trustee obligations on the shareholders of trustees. Such an approach would be impractical and create unnecessary overlap and duplication by conflating the role of the shareholder and the trustee.

[29] ASFA, submission to the Royal Commission, 12 July 2018
[30] APRA, letter to all RSE licensees, *Board Governance Thematic Review*, 17 May 2018

8.3. Consistency of political advertising with section 62 of the SIS Act

825.1 Is political advertising consistent with the intention behind section 62 of the SIS Act? Is any amendment to the SIS Act warranted, and if so, why?

In 2015 in Answers to Questions on Notice before the Senate Economic Legislation Committee, APRA said that spending on campaigns related to superannuation and pensions was not necessarily inconsistent with the sole purpose test. It stated that if the activity is characterised as an expenditure or investment made in good faith and the trustee puts forward cogent reasons for believing that this will result in an improved retirement income outcome for the members (or for the protection of that retirement income), then the trustee's conduct would be unlikely to be in breach of the sole purpose test (even if others might disagree with the trustee's reasoning).[31]

Provided the advertising is relevant to superannuation and retirement and has the objective of improving outcomes for members then it is warranted, as has been found by APRA. The reality is that superannuation funds operate within a complex and ever changing political and regulatory landscape.

8.4. Elevating the threshold for MySuper authorisation

825.21 Is one way of addressing and discouraging misconduct on the part of superannuation trustees to seek to encourage improvements to outcomes for members whose contributions are made to MySuper products or is the link too tenuous to justify recommending any system changes to the default system?

825.22 Is it appropriate, as a response to misconduct of superannuation trustees, to apply an additional filter to MySuper authorisations so as to require outcome assessments? If so, what are the general parameters for such a system change and who is appropriate to apply the test?

ASFA does not consider that there is a link between amending the MySuper settings and discouraging or addressing misconduct. Regardless of this, we consider that strengthening the MySuper regime would be beneficial for consumers.

ASFA supports elevating the threshold for MySuper authorisation to raise the standard for all MySuper products. One effect of this would be to encourage underperforming funds to merge, thereby facilitating an orderly transition towards better performing counterparts.

ASFA considers that a 'balanced scorecard' approach assessing a range of factors could be adopted, to determine whether the best interests of members are being promoted.

Any prescriptive criteria to lift the bar for MySuper should consider factors such as investment performance (long-term and risk-adjusted) and include qualitative and quantitative factors such as:

- success in achieving investment objectives
- quality of governance (including investment governance)
- fees and costs charged to members
- quality and value of insurance
- the provision of member services
- the trustee's risk management processes
- innovation including use of (and capacity to use) technology.

[31] APRA, Answers to Questions on Notice, Senate Economics Legislation Committee, 9 June 2015

Any prescriptive criteria must be transparent and easy to measure. Selecting the right metrics is critical as these parameters will determine the barriers to entry and ongoing participation in the default segment. The settings should support the sustainable delivery of high quality MySuper products to the market, on an ongoing basis.

ASFA considers that APRA should apply the test. We note that APRA is already applying an outcomes test to both MySuper and Choice products.

ASFA supports elevating the threshold for MySuper authorisation to raise the standard for all MySuper products.

The settings should support the sustainable delivery of high quality MySuper products to the market, on an ongoing basis.

9. Conclusion

Because our representation is broad, across all parts of the industry, ASFA tries to play an "honest broker" role backed up by evidence based research. Appendix 1 sets out our principles for assessing public policy. ASFA engages extensively with our membership to research, debate and consider feedback on important issues.

When analysing proposed policy settings, ASFA draws on its extensive research to assess the proposal according to its impact on sustainability, adequacy and equity of the system, as well as to identify the consequences (both intended and unintended) for superannuation fund members.

Australia's superannuation system underwrites the health of our economy, fosters innovation in investment products and reduces the financial burden of the Age Pension on future generations. For these reasons and to maintain public confidence in the system it is so important to get the policy settings right.

Appendix 1 – ASFA Policy Principles

1.1 • **Principle:** ASFA should be an "honest broker", aiming to inform debate to improve outcomes for fund members.

1.2 • **Principle:** The impact on fund members and other stakeholders is understood and is evidence-based.

1.3 • **Principle:** The issue is a priority in ASFA's strategic plan or is significant in nature, for example because an existing position has become indefensible from the perspective of fund members'.

1.4 • **Principle:** The likely impact of the policy will be to improve equity, efficiency, simplicity and/or adequacy in the system.

1.5 • **Principle:** The policy will increase sustainability and fund members' confidence in the system.

1.6 • **Principle:** A compromise can be reached despite a diverse and valid range of views across ASFA members.

1.7 • **Principle:** ASFA is likely to be perceived as credible in advocating a position.