ASIC

Australian Securities & Investments Commission

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to

Association of Superannuation Funds of Australia (ASFA)

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The importance of advice

As Jennifer has been stressing, for Australian consumers, quality financial advice is more important than it has ever been. Direct and indirect participation by consumers in markets for financial products and services is at an all time high. And superannuation choice has added a major dimension, with more consumers now able to choose how their mandatory savings are managed.

ASIC's job is to promote a financial services industry that is efficient, flexible and innovative in the provision of financial products and services. We must also promote the confident and informed participation of investors and consumers in the financial services industry. ASIC recognises that the needs of both business and consumers must be met, and we work hard to try to balance those needs using a variety of approaches.

This morning, I want to focus on our shadow shopping work, some areas where we see room for innovation, on advertising and on consumer education.

Shadow shopping

I have to start though with an apology. I'm afraid we have been a party to some misleading and deceptive advertising by promising you the preliminary results of our shadow shopping survey. It is still early days in terms of our analysis of the advice we have received and we are thus not in a position just yet to announce trends and findings. I will however give you a quick overview of the project so you are aware of what we are doing.

As you are probably aware, ASIC is currently conducting a shadow shopping survey. The aim of the survey is to monitor the advice that financial advisers give their clients during the early period of superannuation choice.

The shadow shopping project is well underway. With the assistance of market research firm Roy Morgan, we have recruited over 300 consumers who indicate they intend to seek professional advice about superannuation.

The survey will cover the full range of superannuation advice, namely:

- all types of financial advisers, including banks, financial planners and accountants;
- advice on retail funds, industry funds, corporate funds and self-managed super funds; and
- all states and territories.

We have gone to considerable lengths to avoid influencing how consumers go about seeking advice. Some will have an existing relationship with an adviser or accountant; some will go to their bank or super fund for help. The consumer chooses how they get advice, not ASIC.

The shadow shopping technique therefore gives strong insights into the consumer's real life experience of getting advice.

We will also be checking whether the financial advice complies with the law. To ensure the results aren't distorted, individual advisers are not being notified that they are being surveyed.

If serious legal breaches are discovered, ASIC will determine what further investigation or enforcement action is appropriate.

We will release the survey results when reliable information becomes available. A final report is expected in February.

ASIC's shadow shopping survey is just one part of its broad campaign to ensure consumers are protected during the introduction of super choice.

Super switching & fund information

I would like to spend a little time on the investigation of a consumer's current fund, where a switch to another fund is being considered.

This relates to two legal obligations, neither of which are optional:

1. Advisers can only recommend switching funds if they have made reasonable investigation into the client's relevant circumstances and into the relevant financial products. [s. 945A] This will generally involve a comparison between the current and proposed fund.
2. If a switch is recommended, advisers have an obligation to disclose the consequences of switching in the Statement of Advice. [s947D]

In most cases, the information about the client's current fund is readily available. When ASIC staff have had to review files, in most cases they have been able to find the information about the client's current fund quite readily via a PDS on the Internet or a phone call to the fund.

However, we are aware of comments by advisers that they sometimes find it hard to get info about a client's current fund. This may apply to basic details for corporate funds, sub-plans in corporate master trusts, defined benefit funds and legacy funds. Relevant information may include fees and past performance. Advisers will also often need information is unique to each client, such as the level of insurance, asset allocation, or the components of their benefit.

Advisers say that the information gathering process can sometimes be slow, costly and/or non-productive.

While most basic information should be readily available in PDSs, we acknowledge that getting this other information could be made more efficient. To address this problem, we suggested industry develop a standard information request form to facilitate both asking for data and supplying it.

It would be most efficient if information could be provided electronically.

We encourage ASFA members to help develop such a standard protocol and then to implement it.

If the current fund has good features, such as low fees, good performance, cheap insurance, suitable investment options, etc. it will be in the fund's interest to ensure the adviser has this information.

If the adviser takes reasonable steps to seek information but cannot obtain it, they can give advice without it.

Account duplication

Earlier in the year, ASIC had an informal chat with Ross Clare (Research Manager, ASFA) about the cost of duplicate super accounts. This is relevant to the relative priority given to super consolidation in policy considerations and education material.

Ross estimates there are 27 million superannuation accounts, spread between 12 million people who are (or have been) working but not yet retired. This is an average of 2.3 accounts per person. So there might be 15 million more accounts than fund members.

Of these duplicate accounts, some do not incur major administrative costs. For example, there are about 4.2 million Eligible Rollover Fund accounts. These are clearly duplicates, but might only cost about $40 million per year to administer.

There are around 3 million public sector fund accounts, compared to 1.5 million public servants. However, these are cheap to run, many are Defined Benefit, and consolidation would not cut costs significantly (if at all).

After deducting the rollover funds and public sector accounts, this leaves about 9 million other additional accounts. These would cost at least $450 million to administer (based on a conservative estimate of $50 pa each).

So the overall administration cost of unnecessary duplicate accounts might be around $500 million per year in round terms, if not more.

Duplication pushes up administration costs, as well as creating extra fees for individual consumers.

I'm interested in this because part of ASIC's brief is to enhance the efficiency of the financial system. Account duplication is one area where efficiencies may be possible, including:

- consolidation of duplicate accounts within the same fund (created due to fund merger or poor identity data).
- unwanted accounts in different funds.

Super choice should reduce the rate at which duplicate accounts are created. Mergers between funds may help as well.

We are interested in talking with industry about what other steps could be taken to reduce the wastage from duplicate accounts, such as:

- simple advice about when consolidation is clearly in the client's interests.
- making it easy for the consumer to consolidate funds,
- data matching exercises
- education activities

We are not proposing a general lowering of legal standards just because advice is about consolidation. For example, cases might arise where people inadvertently lose insurance coverage during consolidation, and then need to claim on it.

However, we are keen to facilitate consolidation advice, while still maintaining appropriate consumer protection measures. If there are steps that ASIC might take to facilitate consolidation advice – steps such as guidance or fine-tuning legal requirements – then we would welcome people's suggestions.

Unmet need for advice

ASIC recognises that many funds have taken steps to educate their members. However, we would also encourage the industry to look at whether more can be done to give fund members access to financial advice within their existing fund.

Many members have simple issues like:

- Should I consider insurance, and if so, how much?
- What investment option should I be in?
- Should I make voluntary contributions to get the Government co-contribution?
- Does salary sacrifice add up for me?
- How much super am I likely to have when I retire? Will it be enough?
- Would I be better off making extra super contributions or paying off my mortgage?

These are all strategic issues about how to operate within the member's current fund.

If the member goes to an external adviser, it may be hard to get this advice unless they switch to the adviser's preferred product. We are also conscious that it is easier to get advice later in life when you have accumulated more super. However, it is important that younger people can also get advice or guidance.

Some of these issues can be addressed through mass general advice or scenarios, some through one-on-one general advice, and some through personal advice. Jennifer has already mentioned that if you are going to give advice you should be properly licensed to do so.

ASIC has started to look at the possibility of a generic advice tool.

Advertising

I would like to spend a bit of time talking about advertising.

Super Choice has seen a number of new entrants, an increase in activity by long running advertisers and new activity by players who were previously doing little advertising.

Its great to have superannuation issues brought to people's attention. There is nothing wrong with robust competition via advertising. However, all players in the industry need to make sure their promotions are not misleading.

In this context, I want to reiterate the compliance obligations of funds and advisors, highlight the issues that are likely to be most relevant, and illustrate with a few examples.

In February, ASIC began a project to monitor advertising of superannuation in the lead up to the introduction of choice of super legislation. That project has continued since Super Choice came into effect. ASIC will shortly be releasing public versions of its monitoring of super advertising.

ASIC has identified a number of advertisements that, in our view, are likely to mislead their audiences. Some of the problems overlap with the PDS issues Jennifer mentioned earlier. Where we observe a problem in a PDS, we check to see if the same problem exists in advertising, and vice versa.

We have taken enforcement action against a number of advertisers, and there are others still in the pipeline. The advertisers have been from many different sectors of the industry – industry funds, retail funds, promoters of Self Managed Super Funds, early release super schemes and debenture offerers.

Where we take action, it is not based on a value judgement about the reputation of the advertiser or the merits of the advertised product. We just look impartially at whether the advertiser has complied with the law.

ASIC has previously provided guidance in relation to three of the more difficult areas of financial services advertising – statements about future matters, the use of past performance information and comparative advertising.

I will touch on a few areas where problems have arisen.

Who is the audience?

An important consideration in assessing whether an advertisement is misleading is the audience for that particular ad. For mass-market advertising, some in the audience will be knowledgeable about superannuation, but most will have quite limited knowledge. Assessing whether consumers will be misled does not involve an expert's interpretation. It depends on the ad's potential impact on the less knowledgeable part of the audience – average or below average.

An ad that is fine in an industry publication may be misleading in a mass market publication.

For example, an industry insider may recognise a distinction between a "retail" fund and a "corporate" fund, but few members of the public would.

Fine print

The next issue is the use of fine print or qualifying statements. "*The big print giveth and the small print taketh away.* "

At law, whether an advertisement is misleading will depend on the overall impression that it creates, not whether the true picture can be found if consumers try hard enough. If the prominent claim is misleading on its own, small print or a rapid voice-over is not going to fix it.

Past performance

The use of past performance information can be very powerful in advertising. ASIC released a *Guide on the Use of Past Performance in Promotional Material* in 2003 to highlight the potential problems. For example, we said:

> A promotion with information about past performance has a greater risk of being misleading if it is presented in a way that creates the impression that substantially the same returns will be achieved in the future.
>
> A promotion may be misleading if it uses past performance information from:
>
> (a) an inappropriately short time period; or
>
> (b) a time period selectively chosen to show better performance.

To reduce problems with consumers being misled by short-term performance figures, the Guide sets a five year performance figure as an industry standard in promotions. This prevents cherry picking results, and gives consumers more meaningful long-term information.

For example, ASIC took enforcement action against Colonial First State in 2004 over a series of ads with prominent past performance figures.

One advertisement prominently stated that its Geared Share Option had returned 48.5% over one year.

At the time the ads were placed, the particular fund had been available for almost two years. The longer term 'life of fund' return was around 0%. Therefore, ASIC's view was that using the 48.5% figure on its own was likely to mislead readers.

In addition, in one advertisement, Colonial First State used an out of date performance figure when the more recent figure was significantly lower.

This matter was resolved by way of Enforceable Undertaking.

Level of risk

Another area where consumers can be misled is about the degree of risk. ASIC has taken action against a number of debenture issuers about their ads. We were concerned that some ads had overstated the safety of investing in debentures, especially for unsophisticated investors.

For example, Fincorp used taglines such as:

- *'Invest with certainty!'… 'Prudent investors require certainty'*
- *'They also want a strong measure of security so they can sleep soundly at night'*
- *'First ranking investors can enjoy peace of mind through a First Ranking Charge'.*

Fincorp had to publish corrective advertising and offer refunds to investors.

Projections

If there is advertising of future financial information without reasonable grounds, the advertisement will be misleading.

It should be clear from any advertisement that these forward-looking statements are not guaranteed to occur. We are aware that consumers want certainty and simplicity, it should only be given where warranted.

One case that received some attention was the ad campaign by Industry Fund Services. Before and after the introduction of Super Choice, IFS ran a large-scale advertising campaign on behalf of a group of industry superannuation funds.

The ads highlighted projected final retirement payouts based on differences in the current cost structures of industry and retail master trust funds.

While ASIC encourages consumers to consider the effect of fees on their superannuation, it is important that consumers be aware that fees are likely to change over the long term. Accordingly, while projections can be helpful in illustrating the long-term effects of fees or investment returns, they should not be confused with predictions of actual outcomes. Advertising that fails to reflect this is likely to be misleading. While other industry players had strong views on these ads, ASIC formed an impartial view and enforced it. We take the same approach with all players.

This particular matter was resolved by way of Enforceable Undertaking, where IFS agreed to amend their ads. In my view, the amended ad has a meaningful qualification about the limitations of the comparison, while still being an effective advertisement.

Fees

ASIC has raised concerns with a number of funds about promotional material that draws un-stated distinctions between fees, charges and other costs, or only tells part of the story.

The superannuation industry has historically recognised distinctions between:

- fees paid to a fund
- costs recovered from consumers but payable to third parties (such as underlying investment managers); and
- costs netted off before a fund return is declared.

ASIC does not consider that many consumers would be aware of these differences. Accordingly, consumers are likely to be misled by advertising that relies on such distinctions.

For example, an advertisement stating that consumers can avoid “complex and expensive fees” by choosing a fund with “one low administration fee” is likely to be misleading if the fund also recovers other fees or costs. Consumers are likely to think that the single administration fee is the only cost associated with the fund.

Think of the maxim: *the truth, the whole truth and nothing but the truth.*

Look at it from the perspective of the average member or potential investor.

Comparative ads

It is a basic tenet of comparative advertising that ads may be misleading where they do not compare like with like. Within the superannuation industry this can be difficult, particularly as the new choice of fund regime inevitably involves consumers making comparisons between very different types of funds (eg. self managed super, retail master trusts and industry funds). While ASIC accepts that some comparisons may be appropriate, it is important that important differences in funds or sectors being compared are not ignored, downplayed or concealed.

Our concerns have included:

- comparisons that were not properly defined;

  eg. "our cost is(x), which is much cheaper than you'll pay in a retail fund", where the comparison is in fact only with a sub-set of retail funds.

- referring to a ranking without adequately disclosing that the ranking related only to a particular sector of the industry;

- relying on concepts that are understood within the industry, but are likely to be confusing for consumers unfamiliar with those distinctions.

  eg. "best retail fund", without explaining that "retail" funds do not include industry funds.

If you see promotions that may be misleading, email a complaint to ASIC.

ASIC has investigated a number of cases, including both industry sector funds and retail funds. However, we will not be involved in all cases. In comparative advertising between two competitors, they also have the option to take legal action themselves.

Education

Of course, protecting consumers is not just about policing industry conduct; it is also about empowering consumers to make informed decisions about their super. I think all of us here would recognize that prior to the introduction of super choice, the average level of knowledge about, and engagement with, super by Australians was low. In the lead up to, and post 1 July 2005, a great deal of effort has gone into encouraging consumers to understand and think about their super arrangements – both through the efforts of the Government's super choice education campaign, which ASIC was a participant in, and through the myriad of education initiatives undertaken by industry – many of which were terrific.

While no one would pretend that we are anywhere near where we need to end up on super financial literacy, research findings suggest that there has been some movement in the right direction. Another of ASIC's goals is to continue that momentum to further equip consumers with the skills and motivation to understand and take an active interest in their super.

Some of the projects we are currently working on include:

- Helping consumers to better understand their super statements. This is an initiative we plan to work closely with ASFA on, as we know they are also doing work in this space. The importance of this can be seen from the yet to be released results of the most recent ANZ national financial literacy survey which found that 30% of Australian's with super didn't read their super statement because they found them too difficult to understand.

- We are also working on a super education resource for Indigenous Australians that will cover a broad range of superannuation related issues, including from angles of particular relevance to some Indigenous Australians.
- Another area we are interested in undertaking educative work on is helping consumers to better understand the information that is available from the various superannuation research/comparative services and how to understand the differences between the various services. Since we know consumers find it difficult to compare funds, we suspect these services will play an increasingly important role in the future.
- Finally, we are talking with the big corporate employers of young people about using their communications vehicles to get superannuation education messages to young people just starting out in the work force.
- We are also planning a mini education campaign about consumers having their status changed from being employer-sponsored members to being personal members. We will be seeking to ensure that trustees are aware of their disclosure obligations to explain the implications of any changes in fees or insurance arrangements resulting from the shift. Consumers also need to know what to consider when deciding whether their old employer's fund is still appropriate if they change jobs.

Conclusion

Hopefully both Jennifer and my presentations have given you a flavour of some of ASIC's current work around superannuation. We haven't covered everything, especially in the law reform area and our ongoing thinking about improving access to affordable, good quality compliant advice. Rather than go on though, I will stop here and open things up to questions since it is always when we get down to a two-way dialogue that most of us, including ASIC, gets the greatest benefit from these events. And, since I know we share a common interest in ensuring that Australians make good superannuation choices which will maximize their retirement incomes, I would hate to reduce the time to publicly discuss matters of mutual concern to us all.

