



ASIC

Australian Securities & Investments Commission

ASIC's Super Strategies: 2006–07

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Australian Securities and Investments Commission

The Association of Superannuation Funds of Australia

6 September 2006

Sydney, Australia

Introductory comments

- The superannuation industry has become a permanent and essential feature of the Australian financial system.

- The compulsory superannuation savings scheme introduced in 1992 has been a key contributor to superannuation funds now dominating the Australian managed funds industry with a market share of 53% and accounting for more than 70% of Australian managed funds.

- With the Australian Government's clear ambition to simplify and streamline superannuation, the industry will, no doubt, continue to grow rapidly.
 - This has been again demonstrated within the last 24 hours with the Treasurer, the Hon Peter Costello MP's, statements yesterday about superannuation reforms.

- Of course, many Australians are also keenly turning their minds towards the issue of how they are going to fund their own retirement given the introduction of compulsory superannuation savings, financial services reform and superannuation choice, together with the increasingly favourable tax treatment of superannuation.

- As representatives of the superannuation industry, your responsibility for the retirement savings of millions of Australians cannot be underestimated.
 - Now, more than ever before, consumers must have confidence in the market in which they are investing and must be in a position to make informed decisions about what to invest in.

- Of course, further regulation has kept pace with the industry's developments throughout this period.
 - Working through these regulatory requirements has not been without its challenges, from both our perspectives.

The regulatory context

- It is undeniable that the Government's agenda for regulatory reform for financial services and products over the last decade has been ambitious, but it has meant that Australia has a regime that is globally respected.
 - Following the Wallis Inquiry, we needed to contend with a new regulatory structure and many of you are now answerable to both APRA and ASIC.
 - Then followed the introduction of the *Financial Services Reform Act*.
 - Last year, most employees were given choice.
 - And, over the last couple of years, superannuation trustees have also been moving across to the RSE licensing regime that APRA is administering.

- The transition to the new regimes has imposed costs on the industry, not least because the extensive changes to the previous arrangements altered the way we were able to run our businesses, be they providing superannuation or, for ASIC, the business of regulation.
 - Of course, any discussion about costs must equally recognise a discussion on benefits. This is something I will return to when discussing ASIC's strategies in the year ahead.
 - But, I would like to pause for a moment to give you a sense of the particular difficulties in measuring the benefits of regulatory reform.
 - We are not producing a tangible product, the benefits (or otherwise) of which can be easily recognised and assessed.
 - While the new regime appears to have driven significant growth in the managed funds sector, which has also contributed to Australia's significant economic growth, it is difficult to trace the benefits of regulation back to a particular regulatory act.
 - More often than not, the benefits of our regulatory regimes are invisible and may not be seen or felt for some time after the costs have been incurred.

- Many of the requirements impose rules that govern conduct or behaviour and so, it is not possible to reliably evaluate what might have occurred in the absence of these rules.
 - If we have regulated well, much of the benefit is what you do *not* see; that is, the scandals or inefficiencies that negatively impact on consumer and investor confidence.
 - The overarching test that can be applied reliably to the Australian financial markets, therefore, is whether there is informed consumer and investor participation, and international confidence in the reliability and discipline of those markets.
- In 2006, the Government has sought to further improve the efficiency and effectiveness of Australian financial services regulation.
- The Parliamentary Secretary to the Treasurer, the Honourable Chris Pearce MP's 'FSR Refinements' projects, as they are commonly referred to, work to achieve this aim.
 - The specific proposed refinements that will affect superannuation administrators and trustees are well known to you all and I will not repeat them today.
 - Many of the refinements focus on financial product advice and disclosure. However, I remain perplexed that the industry still sees some of these issues as a challenge, a matter I will discuss shortly.
 - The Government's response to the Regulation Taskforce's report on 'Rethinking Regulation' also emphasised the need to reduce regulatory burdens to help build sustainable businesses.
 - Again, there are specific recommendations around the superannuation guarantee and superannuation taxation complexity that I do not need to discuss in this forum.
 - Instead, I would like to focus on ASIC's 'Better Regulation' initiatives, which demonstrate our efforts to increase our transparency and accessibility, and improve our engagement with you, our stakeholders. We are also working to minimise any duplication and overlap with APRA through a Joint Working Group.

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- ASIC has, and is committed to continuing to, work with the Government, industry and consumers on opportunities for further improvement.
 - Throughout the transition to our current position, we have consulted actively with industry and consumers.
 - During the transition periods for FSR licensing and superannuation choice, we held regular liaison meetings with ASFA and worked with various entities as they went through the process of obtaining a licence and understanding their obligations.
 - We have now rationalised that process through our Financial Services Consultative Committee and we continue to meet regularly with ASFA to discuss issues of concern.

- The focus for us now is to ensure that the financial services regime adds the value it was always intended to add.
 - Our role is not simply a matter of ensuring real-time monitoring, surveillance and investigation of industry participants.
 - It is much broader and encompasses playing our part in growing the financial services regulatory regime to maturity so that:
 - you have certainty about what the regime requires of you – it is predictable and you know what is expected of you and what you can expect;
 - your dealings with ASIC, as a regulator of the regime, will be characterised by maturity and professionalism – hopefully, on both sides; and
 - consumers and investors have confidence in the regime and participate accordingly.

Challenges confronting the industry

- I understand, of course, that your perception of 'growing the regime to maturity' is not a task that is either simple or easy to achieve.
 - Maturity often carries connotations linked to experience, which is difficult to obtain in what some might consider a relatively young regime, and against a backdrop of commercial pressures and expectations.
 - However, while the regime is still in its relatively early days, the institutions and funds typically have mature businesses with skilled and experienced management in place, and respected brands, many of which are household names.

- You are each faced with making sound business decisions in order to maximise long-term returns for members, while also safeguarding the assets of the superannuation funds for which you are responsible.
 - These are entirely appropriate objectives for you to pursue.
 - Of course, for the trustees among you, the requirement to provide benefits to your members is part and parcel of the service that you provide, given it forms the basis of the 'sole purpose test' that has been in place for some time.

- Despite these pressures, helping the regime reach maturity, in our view, should not be perceived as difficult or onerous.

- A key aspect of meeting the commercial expectations placed upon you is compliance with the law.
 - If one considers the 'spirit of the law' and its intent to equip consumers and investors with the information they need to make informed financial decisions confidently, then the broad obligations are not difficult to understand and comprehend.
 - This means that the process of 'growing the regime to maturity' is not as thorny as it may, at first, appear.
 - Indeed, ASIC is pleased to see how well the superannuation industry has adapted to the new legal requirements.

- We also recognise industry's need to achieve legitimate commercial objectives, including liability management. But these objectives cannot displace the consumer interests the legislation is designed to promote.
- Today, I would like to focus on two of ASIC's priority areas that affect the superannuation industry's passage to maturity and how ASIC intends to approach them in the coming year. They are:
 1. first, promoting quality advice; and
 2. second, providing understandable disclosure.

Quality advice

- In the last few years, we have all learnt many lessons about how to provide financial product advice and how to recognise the characteristics of appropriate advice.
- What is important to bear in mind, and implement in practice, is that advice does not need to be overly complex merely because the regulatory context has changed.
- The events leading to the enforceable undertaking that ASIC recently accepted from AMP Financial Planning highlighted issues around the provision of advice on financial products and, today, I want to discuss two aspect in particular: the use of approved product lists and switching advice.
 - As you are aware, financial product advice must have a reasonable basis and be appropriate to your client's circumstances.
 - This is quite simple, principles-based law.
 - Whether the law required it or not, surely any reputable firm would only give advice that is in their clients' interests.
 - ASIC accepts that approved product lists are a common, and perhaps inevitable, component of the advice industry.
 - Approved product lists may be a useful way for licensees to control the quality of the advice given by their employees and

- representatives; they provide a useful mechanism for ensuring advisers do not recommend products that have not been researched or do not meet key criteria.
- Approved product lists must, however, be appropriately used.
 - ASIC will not accept advertising of broad approved product lists when some superannuation funds are routinely given a 'hold status' so that advisers are prohibited from recommending those funds: this action is likely to mislead consumers.
 - Nor will we enter into the debate on the merits of investing in industry funds or retail funds.
 - The funds on approved product lists are choices for licensees, although we accept that challenges arise where advisers need to deal with clients who are already members of not-for-profit superannuation funds that are not on those lists.
 - Advisers must be aware that their primary obligation is to comply with the law, including the switching obligations; obligations to licensees regarding approved product lists are secondary to these.
- Of course, where you are advising clients to switch superannuation funds, the requirement to have a reasonable basis for advice, and disclose it, becomes starker as there is a direct point of comparison between the existing and the recommended product.
- There is also a greater potential for conflicts of interest to arise as a result of remuneration or associated product arrangements. Unless the advice is adequately researched, there is the potential for clients' interests to be compromised through higher fees (with no countervailing benefits) or the loss of important features like insurance cover.
- Our Shadow Shopping survey in the first six months of superannuation choice clearly demonstrated that good advice does not necessarily have to be about a specific superannuation fund.
- To the contrary, strategic advice appeared to be highly beneficial to clients.

- The key, in my mind, is to tell consumers what they need, and are entitled, to know in a manner that recognises their special needs and circumstances so that they can make informed decisions.

Meaningful, understandable disclosure

- Of course, to comply with the law, it is not enough just to provide appropriate advice. You must also make disclosures about that advice, as well as about products that your clients are acquiring.
- The challenge for the superannuation industry in making sure that documents including PDSs, FSGs and SoAs are 'clear, concise and effective' is still a substantial one.
 - While 'clear, concise and effective' is somewhat subjective, it is easy to identify both good and bad examples of disclosure documents at the extremes.
 - However, beyond the niceties of the legal formula is the need to make sure your clients receive information that is *effective* for them. That is, information that they can understand *and* act on.
 - I remind you:
 - It is the responsibility of the product issuer, in your case the superannuation trustee, to ensure the PDS complies with all relevant legal requirements.
 - ASIC's role is not to vet PDSs. Lodgment of an in-use notice with us does not give you the regulator's 'stamp of approval'.
 - However, both ASIC and many in the industry remain concerned about the length of some PDSs.
 - Superannuation PDSs are not particularly longer or shorter than others in the financial services industry.
 - However, multiple product PDSs that are more common in the superannuation industry, of themselves, make PDSs much longer and potentially more complex than is perhaps necessary.
 - The introduction of short-form PDSs in 'FSR Refinements I' offers a classic opportunity for the industry to take advantage of. ASIC is only aware of one product issuer developing this type

of PDS and this has, no doubt, fuelled the inclusion of 'incorporation by reference' in the next round of FSR Refinements.

- We were pleased to see how well the superannuation industry adapted to the introduction of the enhanced fee disclosure regime in PDSs.
 - We will continue to monitor this regime, which is now being rolled out in the managed investments sector generally.
 - However, in the coming year, we will see how the superannuation industry will deal with the new periodic statement requirements in this area.

- ASIC will also have an increased interest in the disclosures made in the superannuation industry when members are transferred out of funds without their consent.
 - This will extend to three areas of member transfer: transfer to an eligible rollover fund; transfer to a successor fund, where the original fund is wound up; and transfer of a member from an employer-sponsored division of a mastertrust to a personal division of a mastertrust.
 - ASIC will specifically look at timing of disclosures made and whether opt-in or opt-out provisions dictate members' transfers.

- Probably the most contentious area of disclosure that continues to be a priority for ASIC is adequate disclosure of conflicts of interest.
 - Both legal compliance and clients' interests can be compromised by conflicts of interest, so it is essential that these conflicts are managed.
 - As I mentioned earlier, the commercial expectations and pressures placed upon you can affect the conflicts you encounter.
 - For trustees, key conflicts can arise where you are related to major service suppliers who – directly or indirectly – profit from the superannuation fund.
 - In the advice sector, conflicts can arise where a switch to a commission-paying fund or an in-house fund is recommended.

- One of ASIC's primary concerns stems from consistent evidence that has shown that unreasonable advice is much more likely where advisers have conflicts of interest over remuneration or in recommending associated products.
- As an industry, you must manage the challenges that this poses.
 - ASIC has said, repeatedly, that it has no intention of restructuring the industry. That remains our firm position.
 - However, together, we need to build the financial services regime into a mature system where conflicts are adequately managed and I call on you to ensure this happens.

ASIC's role

- ASIC's strategy involves taking a balanced approach to our statutory mandate.

Compliance with the law

- First and foremost, we expect compliance with the law.
 - Where you make reasonable efforts to comply, we will take this into account in seeking to resolve any issues with you.
 - But if you do not comply, either intentionally or recklessly, we will take a firm approach.
- This is reflected in our work on illegal early access to superannuation, an area where we now take more enforcement action than for any other activity regarding superannuation.
 - With the introduction of superannuation choice, consumers now have more opportunities to establish self-managed superannuation funds.
 - ASIC is working closely at a cross-agency level with APRA and the ATO to minimise transfers from legitimate superannuation funds to sham self-managed superannuation funds.
 - There is the potential for the superannuation industry to join us in getting messages out about the need to reduce incidences of this type of conduct.

Facilitating business

- Of course, upholding the laws of the Commonwealth is only one aspect of our role. We also have an important role in business facilitation.
- Our 'Better Regulation' initiatives directly address this.
- A key aspect of our agenda in the coming year is to develop greater expertise in systematically analysing the impact of our regulatory decisions on business.
 - As I mentioned earlier, this will involve developing effective measures of business costs and ways to quantify benefits. Indeed, it will form part of the Government's broader initiatives in this area following its response to 'Rethinking Regulation'.
 - After all, we consider that responsible regulation – be it working with you to facilitate consolidation or simpler SoAs, considering scaleable advice obligations or granting relief where appropriate – requires a clear understanding, and balancing, of the costs and benefits of adopting a particular regulatory response.
 - I invite the superannuation industry to contribute to these debates.

Protecting consumers and investors

- Our business facilitation role must, of course, be balanced with the need to protect consumers and investors.
 - This is particularly so given we receive some 7000 inquiries on our Infoline each year relating to superannuation.
- Although the most recent research indicates improvements in Australian financial literacy levels, it nonetheless shows that many consumers are still not actively planning for their retirement and that superannuation is still not fully understood by all Australians.
 - Of course financial literacy is not the silver bullet, but it does present as a key ingredient.

- In the coming year, ASIC is specifically working towards helping consumers to make better choices and interact with the superannuation industry in a more informed manner.
 - We will continue our ongoing work on improving the superannuation calculator, providing comparative superannuation fee data, letting consumers know the reasonable returns to expect over the longer term and educating consumers generally about superannuation.
 - Indeed, we have two key superannuation education initiatives proposed over the next twelve months.
 1. The first will focus on developing an online superannuation education program for high school students on the verge of leaving school. The elements of this initiative will include developing the basic messages, developing student resources and developing teacher resources so that teachers feel confident teaching the material.
 2. The second will involve running a consumer education campaign to complement our focus on disclosure where consumers are transferred out of funds without their consent. The emphasis of this campaign will be consumers who are changing jobs and would like to remain with their previous employer's fund, given potential impacts on the fees they will pay and insurance coverage they might or might not retain.
- ASIC will also undertake research to both understand the motivations of consumers and what drives their behaviour.
 - In my view, this will enhance our ability to drive strategies aimed at more effectively assisting consumers at the front end of transactions (that is, when they are making a decision to switch superannuation funds).
 - This knowledge is vital in determining how best to communicate with consumers.
 - ASIC welcomes any input from the superannuation industry, including their research.

Perspectives on industry's role

- I have spoken about a range of ways in which ASIC and industry play their parts in growing the financial services regime to maturity.
 - However, while ASIC may set certain expected standards, I would respectfully suggest that you must take responsibility for setting your own benchmarks, which may see your approach go well beyond what we contemplate.

- ASFA, as the key and respected representative body of the superannuation industry, is in a key position to assist you in this pursuit.
 - Indeed, I understand that your upcoming national conference will focus on 'going the distance' and emphasises a long-term vision for the superannuation industry.

- I would like to conclude today with a summary of my perspective on the role of the superannuation industry and how your role can be enhanced in the future.

- From a leadership viewpoint, I think your role is clear.
 - The threshold legal requirements of the financial services regime are set and the time for debating those are over.
 - You must now continue to go about 'getting on with your businesses' of providing superannuation, striving for a sustainable future for your individual members, as well as the broader economy and community.
 - To do so, you must aim for the provision of quality advice and understandable disclosure. There are myriad ways that you can achieve this best practice, including:
 - continuing to develop guiding principles, like those that ASFA has developed on dealing with the enhanced fee disclosure regime for periodic statements;
 - providing model documents, similar to the model SoA ASIC released last year;

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- guiding consumers to make appropriate choices and offering advice and education within your fund; and
 - getting your systems sorted out to facilitate account consolidation, both in and out of your funds.
- Of course, you should also continue to build and leverage off partnerships both within the superannuation industry, as well as across it.
 - ASIC is most certainly committed to doing likewise.
 - I have discussed some of our arrangements to ensure we have regular and effective financial services liaison.
 - I would also like to take the opportunity to highlight ASIC's Business Consultative Panel, which comprises senior business leaders and reflects a wide cross section of the Australian business community, including representatives from the superannuation and funds management industry.
 - This Panel – like our Consumer Advisory Panel – provides a forum for more effective and open dialogue between ASIC and the business community on current and emerging market issues and risks. It is another of our 'Better Regulation' initiatives.
 - We encourage you to also bring ideas to the table, including telling us how we can improve as a regulator.

Concluding remarks

- In conclusion, I want to emphasise ASIC's commitment to continuing to work with the Government, industry, consumers and investors to work through the current challenges in the superannuation industry for the benefit of all Australians.