ASFA
The Voice of Super

File Name: P547

22 October 2001

John Cosgrove
Presiding Commissioner - Review of Certain Superannuation Acts
Productivity Commission
PO Box 80
Belconnen ACT 2616
E-mail: super@pc.gov.au

Dear Commissioner Cosgrove,

ASFA Submission on Productivity Commission Draft Report

The Association of Superannuation Funds of Australia Ltd. (ASFA) would like to make this submission on the Draft Report of the Productivity Commission's *Review of the Superannuation Industry (Supervision) Act 1993 and Certain Other Superannuation Legislation*, released on 19 September 2001.

ASFA is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. Its members, which include corporate, public sector, industry and retail superannuation funds, as well as service providers to those superannuation funds, account for more around 80% of superannuation member accounts and over 80% of the superannuation assets.

The value of total assets in the superannuation system is currently over $500 billion, held in approximately 20 million superannuation accounts representing approximately 8 million superannuation fund members.

Overall Views – Draft Findings

ASFA is pleased with many of the findings of the Productivity Commission Draft Report. In particular, ASFA supports Draft Findings 6.1 and 6.2 that endorse the continued use of the trust structure and the role for representative trustees.

Overall Views – Draft Recommendations

The Productivity Commission's review is strictly limited by the Terms of Reference set by the Assistant Treasurer. It is our understanding that the Commission is to

Secretariat

Level 19
Piccadilly Tower
133 Castlereagh St
Sydney NSW 2000

PO Box 1485
Sydney NSW 1005

Tel: (02) 9264 9300
Fax: (02) 9264 8824

examine current arrangements, as summarised by the Commission itself, in terms of "those parts of the Act that ***restrict competition***, or that ***impose costs*** or ***confer benefits*** to business (considered to include superannuation funds and those who provide services to them)". (From *Fact Sheet No. 3*, emphasis added.)

ASFA has called for a wide-ranging Government review of superannuation policy, with an emphasis on the tax treatment of superannuation and the ability of current arrangements to provide adequate incomes in retirement. However, ASFA, and many other bodies, recognised and accepted the limited nature of the Productivity Commission's review, as set out in the *Competition Principles Agreement of National Competition Policy,* and chose not to comment on issues that were expressly outside of the Terms of Reference.

We are therefore surprised by both the nature and direction of the review and some of the recommendations. We question whether some of the recommendations of the Draft Report can be justified within the parameters of the Terms of Reference. This Draft Report appears to be making recommendations on wider issues such as the security of superannuation and addressing some of APRA's data-collection concerns, issues that, while worthy in their own right, appear to fall outside of this review's Terms of Reference. Further, similar recommendations have emanated from the Minister for Financial Services and Regulation in his *Options for Improving the Safety of Superannuation – Issues Paper*, released on 2 October 2001. We would be concerned if the Productivity Commission Final Report pre-emptively endorsed proposals that appear to be outside of its mandate.

This Draft Report should have restricted itself to issues relating to competition, costs and benefits for the funds and service providers – as clearly noted above. The Draft Report acknowledges that some of its recommendations actually contradict what is demanded from the Terms of Reference. At page 120, for example, it is acknowledged that licensing of all APRA-regulated funds may actually reduce competition within the sector. Yet there is little, if any, attempt to demonstrate that "the benefits to the community as a whole" outweigh the costs of licensing, as required under the Terms of Reference.

This deficiency highlights our real concern; the Productivity Commission has not received full submissions on those issues the industry viewed as outside the Commission's Terms of Reference. It is therefore difficult to see how the Commission could have considered all appropriate evidence to form a sound basis for some of its conclusions and recommendations. Put bluntly, if ASFA had known the full extent of the areas under review, our submission would have addressed those issues.

ASFA Comment.
ASFA recommends that recommendations in the Final Report be confined to matters within this review's Terms of Reference.

Options for Modifying SIS legislation – Draft Recommendations

Draft Recommendations 4.1 and 4.2
Capital Requirements

The Draft Report recommends changes to the capital requirements for Approved Trustees (and, by extension of licensing, potentially to all APRA-regulated funds), including a requirement for minimum net tangible assets separate from custodian arrangements and operating capital requirements linked to operating costs.

Changes to capital requirements must be carefully considered. We would suggest the need for strong evidence, rather than assertion, as to the benefits derived from such requirements and whether they will actually improve the overall security and quality of management within superannuation entities.

ASFA Position.
ASFA intends to provide in-depth consideration of the capital requirement issue as part of our response to the *Options for Improving the Safety of Superannuation – Issues Paper.*

Draft Recommendations 4.3 and 4.4
Performance of the Compliance Audit and Actuarial Function

The Draft Report recommends review by APRA of the current requirements for performance of the compliance audit and actuarial function. ASFA strongly supports the need to have audit and actuarial functions performed by suitably qualified professionals. The current arrangements have, for the most part, achieved a good outcome in terms of compliance and security without overt regulatory intervention or any unnecessary restriction to competition.

Auditor quality and independence have recently been examined by the Senate Select Committee on Superannuation and Financial Services, which, last month, released its report on auditing of superannuation funds. One recommendation would require the auditor to demonstrate a degree of competency in superannuation. This is worthy of consideration. However further examination of the Senate Committee's recommendation should be done in an open and consultative fashion, fully involving the regulators, the superannuation industry and relevant professional bodies. Further, any changes in this area must recognise the wider issue of reform in auditing practices more generally, for instance, the recent report made by Professor Ian Ramsay.

ASFA Position.
ASFA strongly supports the need to have audit and actuarial functions performed by suitably qualified professionals and counsels that existing standards must not be compromised.

ASFA recommends that any changes to the current requirements in the statutory functions of auditors and actuaries be done with the full involvement of the relevant industry and professional bodies and that any new system not impose unnecessary costs on industry.

Draft Recommendation 5.1
Age and employment conditions for preservation and contributions

ASFA supports reform to this area of SIS. We believe, if properly done, such changes will address the compliance burden faced by many superannuation funds as well as meet the Community need for more flexible retirement arrangements. ASFA considers the current rules relating to both contributions and the cashing of benefits for people who have reached preservation age are complex, inequitable, difficult to apply and not suitable for the modern workforce.

ASFA Position.
ASFA advocates the adoption of a policy that would permit a gradual or phased retirement for people after age 60. Whilst individuals should have options about when they work and/or retire, ASFA recognises the need for an upper age limit for the provision of tax concessions for superannuation contributions.

Draft Recommendation 5.2
Non-Resident Issues

The Draft Report recommends simplifying access and transfer arrangements for non-residents.

ASFA supports such measures and would like to comment on specific issues.

Transferring benefits from overseas

When transferring benefits from overseas jurisdictions to Australia, Australian law requires the transfer to be made within six months of becoming a resident if all of the benefits are to be exempt from tax.

Unfortunately, the requirements of the country of origin that must be satisfied in relation to the type of fund suitable for transfer in Australia generally make it virtually impossible for this tight timeframe to be met. While there is little that can

be done to achieve change in the requirements of the country of origin, ASFA believes consideration should be given to amending the Australian time limit requirement.

ASFA Position.
ASFA recommends that the time limit should apply not to the actual transfer of the benefit into an Australian fund but to a requirement to notify the Australian Taxation Office, as the entity assessing the taxation status of the transferred monies, that an application for the transfer has been made. This could be implemented with appropriate safeguards to ensure that appropriate efforts were being made to effect the transfer.

Superannuation contributions in respect of foreign nationals

This issue relates to the situation where a foreign national is temporarily working in Australia but remunerated by their 'home' employer.

The superannuation guarantee legislation only provides an exemption from SG in respect of these arrangements for a narrow class of visa holders. In respect of other, usually lower classified, employees the employer effectively pays superannuation twice.

The government seems to favour remedying this by having reciprocal arrangements in respect of Australian nationals employed overseas by Australian employers. While ASFA agrees that this solution would be suitable and notes an exemption in relation to the Superannuation Guarantee being negotiated with Portugal in the context of a 'double social security agreements', generally reciprocal agreements between governments in this area have been rare. Most have been confined to agreements in relation to social security benefits. Relying on the reciprocal government agreement route for superannuation guarantee is taking too long to fix the problem.

ASFA Position.
ASFA recommends that there should be no requirement for Superannuation Guarantee contributions in respect of foreign nationals working temporarily in Australia but remunerated by their 'home employer to the extent that equivalent superannuation benefits are provided in the 'home' jurisdiction in respect of the Australian remuneration.

Superannuation benefits of people permanently departing Australia

ASFA has always accepted that foreign nationals on working holidays in Australia should be subject to the Superannuation Guarantee. However ASFA also believes that these people, on permanent departure from Australia, should be able to remove their superannuation from the system. While ever the ongoing maintenance cost of these usually small accounts is an impost on the earnings of all fund members, the

retention of the money in the superannuation system cannot be justified in terms of a retirement income policy for Australians.

ASFA Position.
ASFA recommends measures that would enable temporary visitors to access their superannuation when permanently departing Australia.

Draft Recommendation 5.3
Simplifying Risk Management Statements

The Draft Report recommends simplification of the Risk Management Statement (RMS) for Derivatives. ASFA supports changes that would reduce associated compliance costs for superannuation funds. The view of many in the industry is that the RMS requirements initially focussed trustee attention on derivative investments, in the wake of the Baring's collapse. However, the RMS requirements are now seen by many as costly and burdensome, with modest benefit for trustees.

It has come to our recent attention that APRA intends to review the current RMS requirements set down in Superannuation Circular II.D.7. ASFA intends to co-operate with this review.

ASFA Position.
ASFA will work with the regulator to improve the effectiveness and relevance of Risk Management Statements.

Draft Recommendation 6.1
Exempt public sector schemes

"There should be no expansion of the current list of exempt public sector superannuation schemes. Consideration should be given by governments to the feasibility of closing exempt schemes which are open to new members. Any new schemes should be subject to SIS legislation."

The list of exempt public sector superannuation schemes is contained in Schedule 1AA of the Superannuation Industry (Supervision) Regulations.

The listing of an exempt public sector scheme in the regulations is a declaration that the scheme is subject to Commonwealth, State or Territory government supervision under their respective enabling Acts and that the regulator recognises that the rules of the scheme conform to the principles of the SIS legislation, even though they are not formally subject to it.

If the underlying reason that these schemes are listed in a schedule and not directly regulated by SIS is because of constitutional difficulties then the Commission's draft recommendation is in fact a proposed ban on Commonwealth, State and Territory Governments providing a corporate superannuation scheme for their employees.

ASFA Position.
ASFA recommends that any final recommendation on these schemes be made only after full investigation of the legal and constitutional issues involved.

Draft Recommendation 7.1
Licensing

As noted above, ASFA believes that this recommendation may fall outside of the Terms of Reference of this study. We also query some of the arguments put forward in the Draft Report that support the use of Approved Trustees / licensing. On the matter of voluntary contributions, Clare (*Superannuation Contributions - Recent Trends* January 1999, ASFA Research Centre) cautions against interpreting the high proportion of voluntary contributions to retail funds as indicating support for the current tax regime on contributions or accumulation. One might extend this to query whether voluntary contribution flows should be used to endorse a particular industry sector or specific structure. Clare further notes:

> "While further research would be necessary to quantify the impact of each of these factors, it is likely that growth in retirement income products such as annuities and allocated pensions would be responsible for most of the recorded growth in member contributions to retail funds. The strength of these "contributions" is driven by social security means testing provisions which encourage the taking of income streams and by the favourable tax treatment of the earnings on investments supporting such products."

Further, in his analysis of ATO statistics on the short-lived "savings rebate", Clare notes that voluntary contributions were strongly favoured by persons earning between $40,000 and $70,000. However, those on lower salaries, who are more likely to be in industry funds, not surprisingly were less likely to make such contributions.

This could lead one to conclude that the level of voluntary contributions to retail funds may actually be a reflection of current industry structure and decisions about the use of retail funds immediately prior to commencing an income stream. It would also bring into question any categorical conclusion that such trends reflected community endorsement of the approved trustee structure.

The Draft Report also claims that there have been "few failures of funds managed by approved trustees". A low incidence of failures is also the case among those funds not managed by an approved trustee.

While assertions are made that the Approved Trustee regime, and the accompanying capital requirements and additional tests of competence and integrity, will improve the security and quality of superannuation fund management – the evidence to confirm this remains scarce.

We support APRA having sufficient and appropriate information on funds to effectively and efficiently regulate them. However we believe licensing would be a blunt instrument to achieve this end. It is likely that a licensing regime will fail to capture funds operating at the margin. Any recalcitrant, defunct or dormant funds will merely continue to exist as unlicensed funds.

Other means of capturing the necessary information should be considered. For instance, all non-SMSF funds are required to notify APRA within 60 days of being established that they wish to become a complying fund. This may be the point at which APRA could collect the necessary information to assist prudential supervision. This would create a better "registration" process. This may be of greater benefit to both APRA and the industry than a "licensing" process.

However we recognise that requesting more information and/or licensing up-front will not deal with funds already in existence. This will need to be addressed by improvement (in timeliness and content) of annual returns to APRA and a more active pursuit by the regulator of recalcitrant late returns, or non- returns. We note and support recent statements by APRA of their determination to strictly enforce the annual return lodgement rules in 2001.

ASFA has offered to assist APRA in developing a set of indicators for inclusion in annual returns which would be useful to a risk manager. Any information collection by APRA to address existing gaps must be accompanied by a strong and effective presence in the field. Further, where possible, data matching with the ATO and ASIC could improve APRA's own data. These efforts would likely be far more effective for collecting necessary information than imposing an anti-competitive licensing regime.

ASFA Position.
ASFA would support "registration" measures that are not anti-competitive and do not impose significant costs, and would be willing to assist in the development of appropriate processes. However both this and licensing seem to fall outside the Terms of Reference of this review and so should not be included in the final report.

Draft Recommendation 8.1
Replacement of the SCT

The Draft Report recommends the abolition of the Superannuation Complaints Tribunal (SCT) and its replacement with an industry-run complaint resolution scheme.

We fail to see any strong evidence that the SCT has in any way acted as a barrier to competition or efficiency. Further there is no convincing evidence that the SCT has failed to meet its role as a dispute resolution forum. Earlier concerns over the SCT's constitutionality have since been resolved. Anecdotal evidence from some ASFA members indicates a marked improvement in the overall administrative efficiency of the SCT over recent times.

The existence of the SCT further reflects that superannuation is different from other financial products – that given compulsion and its role within our country's retirement income policy, superannuation funds perform a quasi-public policy function. This demands a higher degree of oversight than other financial products.

As a statutory tribunal, the SCT maintains significant and necessary powers that do not exist for complaints resolution schemes, for instance the ability to replace the decision of a trustee with its own. There is also no maximum amount for matters to be dealt with by the SCT– this stands in stark contrast to many of the approved complaints resolution schemes which have a monetary cap for complaints.

Further, all APRA-regulated superannuation funds and their members are covered; there is not an issue of jurisdiction, for instance, if an entity is not a member of a scheme.

ASFA Position.
ASFA strongly supports the continued role of a statutory complaints body (such as the SCT). ASFA regards this as an essential element to maintain public confidence in compulsory contributions – a key element in the government's retirement income strategy.

Draft Recommendation 8.2
Extending Time-Limit on Disability Claims

ASFA is supportive of providing a discretion to the SCT on the one-year time limitation in the following situation:

> Where the Fund / trustees have not been able to finalise its internal review or decision within the one-year time limit and, as a consequence, it is impossible

or unreasonable for the member to lodge a complaint to the SCT within the time period currently specified.

However, ASFA considers that it is important that a member lodges a claim as quickly as possible so that the circumstances (and liability to the fund) can be assessed promptly. ASFA therefore does not support the provision of a wide discretion to the SCT that would permit "old" disability claims to be re-opened where the member's condition deteriorates and / or the member collects fresh evidence. This would be clearly problematic with new evidence and post-dated medical evidence varying from the circumstances originally relevant and considered by the Trustees. It may also have a detrimental impact on the ability of super funds to provide disability cover.

ASFA Position.
ASFA recommends that the SCT be given discretion to extend the one-year time limit on disability claims, but only for narrowly prescribed circumstances.

Draft Recommendation 8.3
Naming Funds in SCT Determinations

The Draft Report recommends that funds be named in SCT Determinations. The practice of not naming funds is done to protect the confidentiality of complainants, particularly in respect to disability and death claims. Any "naming and shaming" campaign should be aimed at raising awareness over systemic failures, rather than focussing on individual, and potentially isolated, determinations. Action to investigate perceived systemic failures would be better undertaken by ASIC following referral from the SCT of specific cases where the Tribunal believes that there is sufficient evidence to warrant an ASIC investigation.

ASFA Position.
ASFA does not support naming by the SCT. ASFA recommends that the SCT, ASIC and the industry consult on the best way to deal with systemic failures, including the issue of naming.

Draft Recommendation 9.1
Require Minister and APRA to Table Details regarding Application for Compensation under Part 23 of SIS

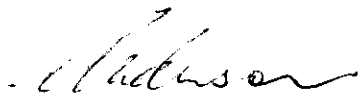
The Draft Report recommends a transparent process for dealing with Applications made under Part 23 of SIS.

The report notes that while there has been no experience of the use of Part 23 provisions, they appear to be an effective mechanism. ASFA questions this statement as it has become clear in recent times that the trigger mechanism for financial assistance is uncertain. At the very least there are timing issues for members in the delivery of financial assistance.

ASFA Position.
ASFA recommends that the operation of this legislation, designed to provide financial assistance, be reviewed.

If you have any questions or comments on the items raised in this submission, please feel free to contact Michaela Anderson or Brad Pragnell on 02 9264 9300.

Yours sincerely,



Dr Michaela Anderson
Director, Policy and Research