



Manager
Superannuation Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: superannuationconsultation@treasury.gov.au

12th February 2014

Dear Manager,

RE: Better regulation and governance, enhanced transparency and improved competition in superannuation

The Financial Planning Association of Australia (FPA) welcomes the opportunity to comment on the Treasury's '*Better regulation and governance, enhanced transparency and improved competition in superannuation*' discussion paper. The measures which the consultation paper proposes are significant and systemic changes to Australian superannuation, and potentially have a powerful impact on the investment decisions and outcomes for retail investors.

Choice product dashboards

In our view, the relevant differences between choice products (and as between choice and MySuper products) are significant enough that a one-page dashboard will be unable to communicate the salient aspects of each product. In turn, without personal financial advice that is tailored to the individual's circumstances, using imprecise dashboards that give a false sense of comparability between MySuper products and choice products make misselling more likely. In the case that the consumer engages a financial planner, the dashboard will be too simple to contribute anything to the financial planner's recommendations.

In the worst case, a choice dashboard that imitates the MySuper product dashboard can be exploited to hide fees, understate risk, and disguise the asset distribution of the product. The perceived commensurability of choice and MySuper may encourage retail investors to invest in choice products where they do not understand the real nature of the product. This is particularly the case concerning the disclosure of asset distribution and risk, where the risk measurement on the dashboard will not reflect the choice product's exposure to several risk factors dependent on the asset distribution of the fund.

Our members have indicated to us overwhelmingly that their own research and analysis of the product disclosure for choice products entirely supplants the intended purpose of a choice product dashboard. They are also of the view that choice products, unlike MySuper products which are prescriptively regulated, require expert financial advice in order to understand their structure, compare against like products, and ultimately appraise their value to the consumer.

Notwithstanding those concerns about the suitability of a dashboard to choice products, we offer the following responses to the discussion paper.



Focus question 13: Should a choice product dashboard present the same information, in the same format, as a MySuper product dashboard? In answering this question you may wish to consider, if the choice product dashboard is to present different information, what should it include.

Our view is that the choice dashboard should include at least the following information;

- the asset distribution (by asset class) which the fund intends to invest in,
- liquidity constraints of the fund,
- an estimate of the minimum time frame to invest in the kinds of assets which the fund invests in,
- different risk measures based upon the asset allocation of the fund.

We believe that this information is necessary for a choice dashboard, as MySuper and choice products are fundamentally different products offering differing degrees of complexity.

Focus question 14: Is it appropriate to use a single benchmark (CPI plus percentage return) for all choice product return targets?

Focus question 15: Should both net investment return (investment return net of investment costs only) and net return (investment return net of all associated costs) be used to measure a product's investment return on the choice product dashboard?

The CPI-plus-percentage-return benchmark is appropriate for MySuper products primarily because the investment strategies of these funds are, as a result of regulation, roughly comparable. As the investment strategies of choice funds vary significantly, consumers may not understand the reasoning behind a return target which uses this benchmark on a dashboard. This is especially the case given that the dashboard, if modelled after the MySuper dashboard, will not give information about asset class distribution, liquidity risk, or other important measures of risk. Simply put, without context that goes beyond a perceived relationship between the return target and the simplified risk model used for MySuper product dashboard, this benchmark is not precise enough to understand a choice fund.

The dashboard should include a chart which displays the net return of the choice product over 20 years (simulated for new products), as well as a line to show the rolling return over the last five years. The dashboard should also include a warning that past performance is not necessarily an indicator of future performance. Notwithstanding our reservations regarding the scant detail available in the choice dashboard, we feel that this would give unambiguous information for retail consumers to compare the performance of various choice funds.

Where projections are made, the short term investment rate should be at the discretion of the fund trustee. However, the longer term forecast should be based on the industry's expected rate of return on each of the underlying asset class that make up the investment fund. By comparing these benchmarks, we allow investors to judge the reliability or performance claims in the dashboard.

Focus question 16: Should the choice product dashboard include both a short-term (volatility) and long-term (inflation) risk measure?

The choice product dashboard should include indicators of short-term and long-term risk. The FPA's criticism of using a single benchmark to indicate choice product return targets is applicable to using a single benchmark for risk – and is particularly relevant to the SRM model. As a result of regulation, the investment strategies for MySuper products are roughly comparable, and an SRM model would help



retail customers understand the product in that context. Choice products are fundamentally different in this respect, and thus the SRM model would not reflect the short-term risk for that fund.

Superannuation board governance

The FPA supports the principles behind the discussion paper's proposals for superannuation trustee board governance. We agree that independent directors "provide an external, dispassionate perspective, enabling boards to benefit from a diversity of views and provide a check on management recommendations." Furthermore, we understand that systemically important institutions (such as banking and insurance entities) require a degree of independence on their boards in order to maintain the integrity of the financial system, and superannuation entities should not be an exception to that principle.

Focus question 3: What is an appropriate proportion of independent directors for superannuation boards?

Focus question 4: Both the ASX Principles for listed companies and APRA's requirements for banking and insurance entities either suggest or require an independent chair. Should superannuation trustee boards have independent chairs?

While we acknowledge the importance of independent directors on superannuation trustee boards, the discussion paper has not identified any reason to depart from the standards for trustee board governance which the Cooper Review proposed. Reforms to the duties of trustees and directors, such as those proposed under Recommendation 2.1 of the Super System Review's Final Report, would obviate the need for a majority of independent directors on superannuation boards. However, we would not reject a conceptually consistent and effective set of principles for superannuation board governance solely on the basis of the mandated proportion of independent directors.

Similarly, the FPA would support a requirement that superannuation trustee boards have an independent chair, so long as this change was based on policy arguments and evidence that an independent chair would secure the best benefit for the fund's members.

Focus question 8: In relation to board renewal, should there be maximum appointment terms for directors? If so, what length of term is appropriate?

Focus question 9: Should directors on boards be subject to regular appraisals of their performance?

The FPA considers that the board governance requirements, combined with reforming the SIS Act to satisfy Recommendation 2.1 of the Super System Review's Final Report, is a superior strategy to subjecting trustee directors to performance appraisal and appointment terms.

Our general view is that successful regulatory strategies should be appropriate and adapted to the institution, role, or system which is subject to regulation. Trustee directors are to act in the best interests of the fund's members, and those best interests reflect the security and growth of their retirement savings over the long term. To best facilitate this objective, the proposed regulation of this sector must encourage trustee-directors to act in the long-term interests of their members as an ethical and commercial responsibility.



As such, our view is that the Cooper Review's recommendations regarding superannuation board governance are better adapted and more appropriate to this objective than the ASX standards or APRA's banking or insurance standards. A maximum appointment term of five years for directors may be appropriate to some funds, based on the fund's method for appraising performance and accountability to members. However, this decision should be made by the superannuation fund in the interests of its members.

Focus question 10: Would legislation, an APRA prudential standard, industry self-regulation or a combination be most suitable for implementing changes to governance? What would the regulatory cost and compliance impacts of each option be?

Focus question 11: What is the appropriate timeframe to implement the Government's governance policy under each option?

In our view, an APRA prudential standard would be sufficient to implement these changes to governance. However, such systemically significant changes to Australian superannuation ought to be debated as legislation. This is particularly the case as our recommendation to clarify the existing duties of trustee directors would require legislation to implement it.

Portfolio holdings disclosure

The FPA is supportive of legislation which would offer transparency in funds for investors and financial planners. This information would assist financial planners to fulfil their best interests duty to make appropriate recommendations based on the client's relevant circumstances.

Focus question 20: Which model of portfolio holdings disclosure would best achieve an appropriate balance between improved transparency and compliance costs?

We agree that transparency requires portfolio holdings disclosure along the lines of APRA's *SRS 532.0 – Investment Exposure Concentrations* standard. However, in order to protect the intellectual property of funds, disclosure of portfolio holdings should take a risk-based approach. We view that disclosure subject to a materiality threshold of 5% would be appropriate.

Furthermore, our view is that there should only be disclosure on a full look-through basis for collective investment vehicles which are related parties of the superannuation fund or any of its board or trustees. If a materiality threshold is introduced, related-party collective investment vehicles should be excluded from consideration and disclosed on a full look-through basis.

We do not comment on whether or not this proposal would require collective investment vehicles to disclose their asset holdings, or if that would be a desirable outcome. While it is very important for superannuation fund holdings to become more transparent, this proposal has commercial and policy implications which are significantly broader than the superannuation space.

Where disclosure on a full look-through basis is required, an information gap of two to three months would permit a balance between transparency and preservation of intellectual property and strategic advantage. The disclosure gap would also facilitate portfolio holdings information to be disclosed at a product level rather than an entity level. While entity-level portfolio holdings disclosure would allow investors and financial planners to assess some risks, it does not give enough information to make informed recommendations.



It is also important that disclosure on a full look-through basis will allow investors and analysts to distinguish between where funds hold assets directly, and where funds invest in other funds.

Competition in default super

The FPA's consistent position has been that the default superannuation market should be competitive, and as free as possible from the intermediation of courts and government. If an employee-choice model will not be effective, employers should be free to elect a MySuper product as the default fund for their employees.

Focus question 27: Does the existing model (which commences on 1 January 2014) meet the objectives for a fully transparent and contestable default superannuation fund system for awards, with a minimum of red tape?

Focus question 28: If not, is the model presented by the Productivity Commission the most appropriate one for governing the selection and ongoing assessment of default superannuation funds in modern awards or should MySuper authorisation alone be sufficient?

It is inappropriate for the Fair Work Commission, or any other court, tribunal, or government delegated organisation, to evaluate or recommend MySuper products. By prescribing any selection of funds to an award, the Fair Work Commission is implicitly recommending those products to the employee. An assessment by the Fair Work Commission or another entity of product compliance with MySuper standards is appropriate.

One of the weaknesses of an employer-choice model is that superannuation outcomes for employees who elect to contribute their superannuation to a default fund will be partially determined by their employer's discretion. Employers are not often in a position to understand the economic circumstances and best interests of their employees, so assigning this duty to the employer may pose problems. However, the Fair Work Commission is no better equipped to fulfil this role than the employer. This presents a difficult policy problem, and the government's response to the discussion paper and its resulting submissions should ensure that default superannuation options are chosen with the employee's best interests in mind.

Focus question 29: If the Productivity Commission's model is appropriate, which organisation is best placed to assess superannuation funds using a 'quality filter'? For example, should this be done by an expert panel in the Fair Work Commission or is there another more suitable process?

Focus question 30: Would a model where modern awards allow employers to choose to make contributions to any fund offering a MySuper product, but an advisory list of high quality funds is also published to assist them in their choice, improve competition in the default superannuation market while still helping employers to make a choice? In this model, the advisory list of high quality funds could be chosen by the same organisation referred to in focus question 29.

As stated above, there should be no 'quality filter' beyond financial advice and the best interests of the employee, and no organisation which can assess the superannuation product beyond its compliance with MySuper and other regulations. Creating an 'advisory list' of funds is anti-competitive and does not meet the best interests of the employee.



Focus question 31: If changes are made to the selection and assessment of default superannuation funds in modern awards, how should corporate funds be treated?

All superannuation funds should be afforded the same rights and obligations during hearings or any other process instituted to prescribe superannuation funds to awards.

Thank you again for the opportunity to comment on the '*Better regulation and governance, enhanced transparency and improved competition in superannuation*' discussion paper. If you have any questions, please contact me on 02 9220 4500 or dante.degori@fpa.asn.au.

Yours sincerely,

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¹ The Financial Planning Association (FPA) represents more than 10,000 members and affiliates of whom 7,500 are practising financial planners and 5,500 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
- We banned commissions and conflicted remuneration on investments and superannuation for our members in 2009 – years ahead of FOFA.
- We have an independent conduct review panel, Chaired by Professor Dimity Kingsford Smith, dealing with investigations and complaints against our members for breaches of our professional rules.
- The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices. This is being exported to 24 member countries and the 150,000 CFP practitioners that make up the FPSB globally.
- We have built a curriculum with 17 Australian Universities for degrees in financial planning. As at the 1st July 2013 all new members of the FPA will be required to hold, as a minimum, an approved undergraduate degree.
- CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional bodies, eg CPA Australia.
- We are recognised as a professional body by the Tax Practitioners Board.