

Financial Services Council Policy Priorities 2019



Who and Why

This publication outlines the Financial Services Council's (FSC) policy priorities for 2019.

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies.

Our Supporting Members represent the professional financial services industry firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

As the peak body for the financial services, the FSC advocates on behalf of its members for policy outcomes which enable the sector to deliver innovative, flexible and consumer-focused products and services.

The financial services industry is the largest industry in the Australian economy. It has also been growing strongly in the past two decades and, despite the global financial crisis, remains larger and more stable than the mining, construction and manufacturing industries.

The industry's gross value added to GDP is 8.8 percent, it employs over 450,000 people and is responsible for investing almost \$3 trillion on behalf of more than 14.8 million Australians - more than the capitalisation of the Australian Securities Exchange and larger than Australia's GDP.

Given the size of the financial services industry, the contribution it makes to the Australian economy and its role in managing the nation's savings, the FSC has outlined a set of policy priorities which are critical to the continued growth of this sector and health of the wider economy.

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\$10 Billion Paid to Australians in Need

Life Insurance - benefits paid to Australians in the last year was \$10 billion, that is \$192 million per week and \$27.4 million per day

\$3.6 Trillion in Managed Funds

Investment - there are \$3.6 trillion funds under management in Australia



\$2.7 Trillion in Super Pool

Superannuation - Australians' super pool of \$2.7 trillion is the fourth largest pension system in the world

100+ FSC Members

The FSC is the peak body for retail and wholesale funds management businesses, life insurers, superannuation funds, financial advisory networks and licensed trustee companies



25,344 Advisers Employed



Advice - there are 25,344 Advisers and 6,214 Australian Financial Services Licensees

FSC's Policy Principles

1. Public Policy Development

We will advocate for sustainable public policy that enhances the financial wellbeing of all Australians:

- We will ensure our policies are non-partisan and evidence-based
- We believe public policy should be focused on promoting a strong financial services sector while ensuring good consumer outcomes

2. Consumer Outcomes

We believe in a financial services system that promotes better consumer outcomes and living standards:

- We believe Australians have the right to access affordable, effective, and fit for purpose financial products
- We believe every Australian deserves dignity in retirement through the provision of adequate, sustainable income
- We believe consumer trust and confidence in financial services is vital

3. Economic Growth

We believe economic growth is fundamental to the prosperity of all Australians.

To achieve this, we believe:

- State and Federal budgets should be sustainable
- Measures should be taken to ensure economic sustainability in the face of an ageing population
- Taxation settings should promote efficiency and equity
- Markets should be allowed to function efficiently
- Foreign investment and trade barriers should be minimised

4. Global Competitiveness

We believe in a liberalised economy with appropriate regulatory settings. We believe in removing barriers to the export of financial services.

To achieve these outcomes, we will strive to:

- Ensure Australia is a competitive place to do business
- Improve financial services sector trade policy and its implementation in Australia
- Ensure a level playing field between Australia and our trading partners through free trade agreements
- Encourage effective co-ordination between government and industry

5. Financial Services Industry Growth

We believe a strong and competitive financial services sector is good for Australia.

We seek to:

- Ensure the industry's competitive advantage is leveraged
- Promote competition and innovation within the industry
- Drive future economic growth in Australia
- Improve Australia's international competitiveness and ability to attract capital

6. Financial Services Industry Standards

To the greatest extent possible under a self-regulatory model, we will adopt best practice in our dealings with consumers and stakeholders.

We will implement industry standards and guidance that seek to:

- Promote a long-term approach to decision-making
- Maintain sound practices that benefit consumers
- Engage in responsible and transparent business practices that centre on facilitating the best possible outcomes for consumers

Advice

KEY STATISTICS



25,344 — Number of active Financial Advisers

6,214 — Number of Australian Financial Services Licensees

Principles

The FSC supports policy settings that:

- Increase consumer trust and confidence in the financial advice industry
- Support high quality advice that provides value for customers
- Improve the accessibility and affordability of advice for Australians

A properly regulated advice industry

Australians must have confidence that any financial advice they receive is reliable and appropriate. The implementation of education, training and ethical standards for financial advisers is a vital part in achieving this goal.

We support the work being conducted by the Financial Adviser Standards and Ethical Authority (FASEA) to regulate the financial advice industry. Professional standards for financial advisers must be developed with the consumer in mind, ensuring advisers have the right skill-sets to help consumers with their financial futures.

The FSC will continue to work with FASEA and other stakeholders to develop policy which supports the provision of high quality advice for consumers.

Greater access to affordable advice

Access and affordability remain a barrier for many consumers in obtaining financial advice. While some advice businesses can offer cheaper alternatives through new advice delivery methods, awareness of these services may prevent consumers from obtaining financial advice.

To this end, we support:

- Increasing Australians' access to appropriate and affordable financial advice
- Raising the financial literacy of Australians
- Promoting new methods for Australians to access financial advice

Economic Policy

Principles

The FSC supports policy settings that:

- Recognise the importance of financial services to the Australian economy
- Improve Australia's international competitiveness and ability to attract capital
- Promote medium-term fiscal sustainability
- Reduce sovereign risk and promote investor confidence in Australia

Shifting the tax mix to increase international competitiveness

Australia needs a tax system that ensures medium-term fiscal sustainability by collecting enough revenue to fund government expenditure in a way that is economically efficient and internationally competitive.

The design of the current tax system is slowing economic growth unnecessarily. The Australian tax system hampers growth, with a heavy reliance on particularly inefficient taxes such as corporate and income tax and stamp duties to raise revenues across both the Commonwealth, State and Territory governments.

In addition, states and territories are too often resorting to increases in the most inefficient taxes to fund other budget priorities.

To address these problems, ongoing tax reform is essential. The primary focus of tax reform should be to fix the mix of tax so that it improves economic growth, improves our international competitiveness, promotes investment and hard work, and raises the productivity of the country.

This would involve:

- Reducing the corporate tax rate on all businesses to 22 per cent
- Abolishing inefficient state taxes, including stamp duties on life insurance
- Adjusting the personal income tax scales and indexing them to end bracket creep
- Funding these measures through ongoing spending restraint, states making greater use of other revenue sources (such as land tax or income tax) and increasing the GST rate while broadening the base

Such a package of tax reform should be crafted in a revenue neutral way. Modelling by KPMG suggests this package could boost GDP by 2 per cent, while leaving no Australian worker worse off.¹

¹ KPMG, The Economic Impact of a GST-funded Company Tax Cut report, 2016

Investment

KEY STATISTICS



\$3.55 trillion — Total funds under management

\$2.15 trillion — Funds with resident investment managers

\$1.34 trillion — Funds with non-resident investment managers

3.5 per cent — Percentage of funds exported

Principles

The FSC supports policy settings that:

- Enhance market integrity and efficiency
- Promote sound corporate governance practices in the funds management industry
- Maintain and increase consumer confidence in the funds management industry

The Value of Funds Management

Australia holds the world's sixth largest pool of funds under management. As a key part of the financial services sector, funds management helps millions of Australians to build their financial independence and security, while contributing to Australia's wealth and GDP. To this end, we seek to raise the profile of funds management in Australia and promote that:

- Australia has a competitive and diverse funds management market
- It is of important social value, investing in and supporting key services and sectors enjoyed by Australians everyday such as healthcare providers, childcare centres and agricultural operations such as farming
- Funds management offers the ability to diversify investment portfolios, by accessing a wider range of asset classes and investment strategies that investors may find difficult accessing themselves, for example emerging markets, global equities, global real estate or hedge fund strategies
- The important role of stewardship - as large shareholders, fund managers can engage with the companies they invest in and can influence the running and governance of that company
- Consumers should be better informed about the funds management industry as an important part of their wealth creation and management process
- The funds management industry requires deregulation to further assist in delivering the best services at the lowest cost to consumers

Improve corporate governance practices in Australia

As institutional investors, we believe in strong corporate governance practices in Australia. Corporate Australia should aim to follow global best practice and improve board practices and disclosure where possible.

To this end, we support:

- Board diversity and independence
- Fair and efficient market rules and practices
- Improved reporting and disclosure by corporate Australia

Support the incorporation of Environment, Social and Governance (ESG) factors into investing

A long-term approach to investing must consider the environmental and social impacts of investment decisions. We support increased transparency to aid decision-making, efficient transition of sectors in the changing economy, the pricing of negative externalities, and a fair and competitive market economy. For these reasons, we:

- Support disclosure by investors of ESG integration and impacts
- Acknowledge that ESG integration is an important element of fiduciary duty and is in the best interests of long-term investors
- Support policy that removes regulatory barriers to investing in new sectors of the economy including development of the impact investing market
- Take an interest in climate change policy and the Government's international commitments on Australia's carbon emissions and renewable energy. As part of this, we support policy clarity on climate change and energy markets

Global Markets and Tax

KEY STATISTICS



\$154.7 billion — Financial services industry contributes to the Australian economy

451,000 — Australians employed

Principles

The FSC supports policy settings that:

- Promote the development of Australia as a regional financial services centre
- Reform Australia's trade and regulatory policy settings to increase the attractiveness of Australia for foreign investment
- Enhance the competitiveness and efficiency of Australia's taxation system for foreign investors in managed funds
- Increase international regulatory recognition for Australia's financial services regime
- Improve regional awareness of the scale and capability of Australia's financial services sector

Unfinished Johnson Report recommendations

In 2009, the Australian Financial Centre Forum completed its report 'Australia as a Financial Centre - Building on our Strengths'². Known as the Johnson Report the recommendations were intended to improve the Australian financial sector's ability to capitalise on its high levels of expertise and significant opportunities in offshore markets.

There have been important steps to implement key recommendations from the Johnson Report, including:

- Asia Region Funds Passport — the Passport will provide the architecture to support cross-border sales of managed funds between Japan, Korea, Thailand, New Zealand and Australia. It commences in February 2019. Once operational, the Passport will permit Australian-domiciled investment funds to be sold directly to retail investors in participating jurisdictions and vice versa. The FSC supports further expansion of the Passport over time
- Collective Investment Vehicles — most collective investments in Australia occur through unit trusts, a type of vehicle that is unfamiliar to many foreign investors. The Government is currently implementing a new corporate collective investment vehicle, to increase foreign investor usage of Australian based fund products. The FSC argues this vehicle should have a competitive cost structure and not be hampered by over regulation. If supported by the right regulatory settings, there are opportunities for the Passport to one day revival the Undertakings for Collective Investment in Transformable Securities (UCITS) regime

- However, one important issue remains unresolved, that is, the withholding tax applying to non-residents in Australian funds. Australia's withholding tax regime is particularly complex. Numerous types of withholding tax apply to foreign investors with differing rates based on the type of income and the investor's country of origin. The regime — it raises very little money, based on FSC analysis, yet provides a considerable deterrent due to its complexity

The FSC strongly advocates for a simpler, more competitive approach to be adopted, particularly removing the withholding tax applying to funds that are in the Asia Region Funds Passport.

Trade agenda and implementation

The FSC supports free trade and the Government's agenda in securing both bilateral and multilateral agreements with Australia's major trading partners. In particular, the growing middle class and ageing population in Asia provides an untapped opportunity for Australia's financial services sector.

We seek a new domestic policy process including:

- A framework for mutual recognition arrangements with regulators in the region (that is, implementation of free trade agreements in financial services)
- Industry input into negotiations of free trade agreements
- An Australian Securities and Investments Commission (ASIC) Commissioner dedicated to international cooperation and free trade agreement implementation
- A collaborative trade body — this body should coordinate with Government departments and regulators responsible for financial services trade policy including the Department of Foreign Affairs and Trade, the Treasury and ASIC

² http://afcf.treasury.gov.au/content/final_report/downloads/AFCF_Building_on_Our_Strengths_Report.pdf

Life Insurance

KEY STATISTICS



29 – Number of companies

\$10 billion – Claims paid in the last year

Principles

As the peak body representing Australia's life insurance industry, the overarching key principle is to rebuild consumer trust and confidence in the industry.

The FSC supports policy settings that:

- Ensure life insurance is accessible and affordable
- Promote the benefits to consumers of providing group insurance in superannuation
- Promote product innovation
- Support positive mental health

Improving the quality of life insurance in Australia

The Life Insurance Framework Reforms (LIF Reforms), which provide for, amongst other things, maximum commission caps and mandatory clawback within the first two years of a policy, commenced on 1 January 2018.

The FSC believes that the LIF Reforms will improve consumer outcomes by reducing the misaligned incentives and inappropriate policy replacement disclosed in 'ASIC Report 413 Review of Retail Life Insurance Advice'¹³ and elsewhere. Further, it considers that the LIF Reforms allow for the continuation of upfront commissions and ongoing commissions at levels that appropriately reimburse the financial adviser for the significant amount of work undertaken at the commencement of the policy and throughout the life of the policy.

Also vital to the LIF Reforms is appropriate monitoring of these arrangements to ensure they succeed in ending misaligned incentives. An ASIC review of the reforms is scheduled for 2021.

The FSC supports reviewing the application of the reforms in 2021, which is only one year after the full maximum commission caps apply. It does not consider that adviser remuneration with respect to life insurance products should receive further Parliamentary scrutiny before this time.

³ <https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-413-review-of-retail-life-insurance-advice/>

The Life Insurance Code of Practice

The FSC's Life Insurance Code of Practice (Code) commenced on 1 July 2017. It committed life insurers to strong standards of customer service and provided meaningful protections to consumers in the key areas of product design, sales practices, underwriting and claims. Insurers were required to provide additional support to vulnerable consumers, who often require assistance navigating the insurance process.

A second draft iteration of the Code was launched for public consultation on 12 November 2018 (Version 2). The Code was amended to take into account concerns raised in different public, regulatory and government inquiries, including the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

The FSC has worked with ASIC, consumer advocates, mental health groups, general practitioners and geneticists for 18 months to develop Version 2.

Version 2 has been designed to lift standards in product design, sales, underwriting, customer service, complaints and claims handling. More than 30 significant changes have been made to practices that govern the way FSC member life insurers will treat customers.

It includes changes that aim to:

- Ensure fair outcomes for customers making a claim
- Binding trustees of superannuation funds to the Code
- Reforms to underwriting, claims and mental health

Version 2 also includes a moratorium on genetic testing in life insurance, which enables Australians to obtain up to \$500,000 of life cover without having to disclose an adverse genetic test result.

Streamlining the regulatory framework to encourage product innovation

Rigidities in insurance regulatory architecture have contributed to underinsurance as providers have not been permitted to develop a wide array of innovative products.

Australia operates under a highly segmented insurance framework. The FSC considers that this framework is stifling innovation in insurance products and the ability of insurers to meet consumers' needs.

Development of innovative insurance products could be fostered under a streamlined, consolidated prudential framework that would enable providers to deliver multi-purpose products.

A more effective regulatory framework would allow better priced and more consumer-focused product offerings. This would improve the efficiency and effectiveness of insurance markets in Australia by minimising regulatory compliance costs. Improving these market rigidities would assist in reducing the level of underinsurance.

Remove unnecessary regulatory barriers that enable life insurers to offer targeted rehabilitation benefits

Current legislation prevents life insurers from providing payments for treatment for Australians at risk of long-term incapacity where they are not covered by private health insurance or are languishing on public healthcare waiting lists.

Numerous research reports have also shown that returning to work can play a hugely important role in a person's recovery. 'The Australian Faculty of Occupational and Environmental Medicine in 2011⁴ showed if a person is absent from work for 20 days, the likelihood of them returning to work is approximately 70 per cent. This falls to 35 per cent, if a person is absent from work for 70 days.

According to research undertaken by Cadence Economics for the FSC ('Cadence Report'⁵), the reforms could provide benefits to a pool of up to 10,118 people per year.

In addition, the proposed reforms mean an estimated 87 people per year could be prevented from becoming totally and permanently disabled as a result of receiving additional healthcare intervention paid for by life insurers.

The Cadence Report estimated that early intervention by life insurers could improve return to work times by an estimated five weeks, from 18 to 13 weeks.

Aside from the dramatic improvements to the quality of life of some vulnerable Australians, conservative estimates suggest allowing insurers to participate in early intervention could also save the government \$1.12 billion in healthcare costs over the next two decades.

Supporting mental health and life insurance

Mental health is an important matter of public interest to the community and life insurers alike. The FSC has developed a *Mental Health Standard* to ensure life insurers who provide information to consumers receive an appropriate level of education and training in awareness of mental health.

Furthermore, the new FSC life insurance industry data project is a strong commitment by Australia's life insurance industry to increase transparency and to further enhance consumer outcomes.

The data project will address what has been one of our major shortcomings — the absence of an industry approach to the collection of aggregate industry data. It will also provide the evidence the industry requires to better design the products of the future.

To help better support consumers with mental health conditions, the FSC will continue to focus on mental health initiatives. Research shows the extensive health benefits of work and life insurers can play an important role in helping people with mental illness get back to good health and work. The FSC's focus on removing unnecessary regulatory barriers that result in poor consumer outcomes will also assist with this.

4 https://www.racp.edu.au/docs/default-source/advocacy-library/realising-the-health-benefits-of-work.pdf?sfvrsn=fca12f1a_10

5 https://www.fsc.org.au/_entity/annotation/2ea56b79-8676-e811-814e-e0071b686a81

Superannuation and Retirement Incomes

KEY STATISTICS



\$2.7 trillion – Superannuation pool is the fourth largest pension system in the world

\$1.8 trillion – APRA-regulated funds

221 – Number of APRA-regulated funds with more than four members

65 per cent – APRA-regulated funds managed of Australia's superannuation assets

Principles

The FSC supports policy settings that:

- Support a fair, efficient and competitive default system
- Increase coverage of the Superannuation Guarantee and ensure adequacy of retirement savings
- Simplify consumer decision-making and improve transparency
- Improve retirement outcomes for all Australians
- Promote effective regulation and governance across the superannuation system
- Promote a sustainable tax structure that assists the majority of Australians to achieve self-funded retirement

The superannuation system should aim to deliver dignity and independence for Australians in retirement by providing replacement income that is adequate to provide a comfortable standard of living.

Superannuation should also reduce the burden of the aging population by reducing reliance on the age pension.

Promote policy settings that improve adequacy of retirement savings

- Increase the rate of Superannuation Guarantee contributions to 12 per cent by 2022
- Maintain tax settings that promote adequate retirement outcomes for all Australians
- Increase coverage of the Superannuation Guarantee to keep pace with the changing nature of work, including the rise of the gig economy

- Implement a staged increase in the preservation age, linked to the age pension eligibility age, and increases in life expectancy, while preserving a reasonable gap, accompanied by an early release mechanism for those unable to work later in life
- Increase stability of the system by reducing frequency of regulatory and tax changes
- Defend the existing tax rules for super against adverse changes, including proposals to remove refunds of franking credits

Ensure a fair and competitive default system

- Promote competition in superannuation to deliver lower fees and better products for consumers:
 - Remove the default superannuation fund from the industrial relations system, and remove barriers in industrial law to consumers choosing their own superannuation fund
 - Allow an employer to select any APRA-approved MySuper product to be the default fund for their workplace
- Support reforms that would raise standards of governance in the superannuation industry, including requiring all trustee boards to have a minimum number of independent directors and an independent chair

Improve retirement outcomes for all Australians

- Implement a retirement incomes covenant to ensure super funds consider the retirement needs of their members
- Support development of high-quality, innovative products to manage risks in retirement, including longevity risks
- Increase transparency to simplify consumer decision-making
- Implement policies that will promote consumer engagement, increase financial literacy and bolster confidence in the system

Technology and Innovation

KEY STATISTICS



650+ – Fintech startups in Australia

Over \$927 million – Australian Fintech sector investment in 2016

Principles

The FSC supports policy settings that:

- Maintain and increase consumer confidence in using technology to obtain financial services
- Improve the accessibility of technology for all Australians
- Advocate for innovative financial solutions to serve Australians

Promote greater understanding of the benefits of technology within financial services

Technology-based solutions for the provision of financial services is a growing industry in Australia.

However, some Australians continue not to understand the benefits that technology-based solutions can deliver.

The FSC is committed to encouraging greater understanding of the benefits that technology can provide for consumers through easier access to services which will benefit their financial future.

Engage closely with the Government and relevant stakeholders around the increased use of Fintech

The financial services environment is changing. New companies and innovative methods of business transactions are allowing a growing number of people easier access to their finances through technology-based solutions such as Robo-Advice. The use of emerging technologies needs to be balanced against considerations such as cybersecurity.

The FSC will continue to work with Federal, State and relevant stakeholders to promote the use of Fintech.

Financial Sector Regulation

Principles

The FSC supports policy settings that:

- Promote best practice regulation
- Ensure regulation is technology neutral
- Ensure regulation does not create undue burden

Best practice regulation

FSC believes the regulation making process can be improved by:

- The government committing to be bound by its Best Practice Regulation Handbook in relation to regulatory proposals that impose compliance costs on the industry
- The Productivity Commission conducting an annual review of new legislation, regulations and other legislative instruments which affect the financial services industry, including the impact of overseas regulation, with the aim of identifying redundant regulation and/or ways of making existing regulation more efficient
- Considering regulatory impact as a whole, rather than as individual parts

Technology neutral regulation

The FSC supports development of technology neutral regulation to ensure both new and existing requirements can be met in a technologically neutral manner. This will allow innovation to occur, which will drive operational efficiencies and reduce costs. In addition, it will encourage development of new products and distribution strategies to benefit consumers.

Existing regulations should be reviewed to determine how to achieve neutrality and new regulations should be tested as part of the development process, to ensure they are truly neutral.

Cost/benefit analysis of increases in regulation

Australia's international competitiveness must be considered when additional laws and regulation are created. A cost/benefit analysis should accompany each new legislative initiative to ensure that the benefit of additional regulation outweighs its cost to the industry, and therefore the consumer. The same approach should apply to significant non-legislative rules such as ASIC Regulatory Guides. Existing regulations should also be reviewed to ensure that appropriate rationalisation of existing products can occur and advances in technology can be adopted.

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