‘Achieving the most for financial services and consumers within 100 days of Government'

FINAL

FSC Leaders Summit

Wednesday 20 July

*****Check against delivery*****

Introduction

Good morning L&G.

Let me start by acknowledging the traditional owners and custodians of the land on which we meet today, the Wurundjeri people of the Kulin Nation. I would also like to pay respect to the Elders past and present and extend that respect to other Indigenous people present.

Welcome to our FSC Chairman, deputy chairs, FSC directors, member CEOs and distinguished guests.

Thanks and welcome to PwC, our new platinum partner. This is their first year supporting our Leaders Summit and we look forward to a long and mutually beneficial partnership. I would also like to thank our other sponsors and media partners for supporting this new, refreshed conference.

So – as we gather here as representatives of the country’s biggest sector, where do we find ourselves in the wake of the longest election campaign, one of the longest vote-counting periods – facing a world of instability, and here at home, a 45th Parliament full of surprises?

[Pause] Determined to get more done for Australian consumers, our customers and clients.

The transactional cost of political change and constant industry review, re-review and reform in a sector that offers so much potential for immediate further growth – for consumers and for the economy – has been enormous.

This morning I would like to make the case that if we are really serious about Australia becoming a financial services centre, and if we are really serious about delivering the best products and services to Australian consumers, then we need to get on with implementing and finalising the legislation that has bipartisan support.

We need growth and great results for consumers – we do not need more reviews and inquiries.

Since the Global Financial Crisis in 2009 financial services has been subject to 14 major reviews or inquiries – including David Murray’s recent system wide review, the Financial System Inquiry. Each has led to recommendations requiring new legislation or regulations.

Figure 1– Financial Services Reviews since 2009

YOUR FUTURE FIRST

FSC FINANCIAL SERVICES COUNCIL

14 Major Reviews and Inquires into financial services since 2009

1. The Super System Review (the "Cooper Review")
2. Parliamentary Joint Committee on Corporations and Financial Services (PJC) (the "Ripoll Inquiry")
3. Richard St John Review and Report- Compensation arrangements for consumers of financial services
4. Senate Economics Legislation Committee inquiry into Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014 [Provisions]
5. Senate Economics References Committee Scrutiny of Financial Advice Inquiry
6. Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Lifting the professional, ethical and education standards in the financial services industry
7. Senate Economics Legislation Committee inquiry into Corporations Amendment (Financial Advice) Bill 2014
8. ASIC Report 413 Review of retail life insurance advice
9. Trowbridge Review into the Life Insurance industry
10. Productivity Commission review into Superannuation Efficiency and Competitiveness
11. Treasury consultation into Lifting the professional, ethical and education standards in the financial services industry
12. Senate Economics Legislation Committee inquiry into Corporations Amendment (Life Insurance Remuneration Arrangements) Bill 2016
13. Senate Economics References Committee Scrutiny of Financial Advice Inquiry – Additional Insurance Terms of Reference
14. Financial System Inquiry (the "Murray Review.")

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To be clear, this is not an exhaustive list. Many of these reviews have been subject to further follow up inquiries or reviews.

There are also reviews into reviews underway. The current Productivity Commission review into the superannuation industry is a classic example; a review into the recommendation of an inquiry, that itself followed a Productivity Commission review in 2012.

Unfortunately, there has been very little progress in implementing the recommendations of many of these reviews. This is not acceptable, and is to the detriment of consumers and to the industry's prospects of becoming a leading financial services centre in our region and internationally.

It wasn't always like this. The 1996 Wallis Inquiry to the Financial System – 20 years ago - is a great example of how effective and expedient implementation can help keep us ahead of the rest of the world - with our world-leading twin-peaks regulatory structure of APRA and ASIC.

Wallis was announced on 30 May 1996 and it produced a final report in March 1997. The Government responded by September, enabling legislation was introduced in March and received royal assent by June 1998, just two years after it was announced.

During this period Australia had one Treasurer, one Assistant Treasurer, and one Prime Minister.

The most recent Parliament wasted time politicising financial services – you'll remember the Senate's failure to pass minimal governance changes required to strengthen consumer protection in super funds – this parliament also created a difficult climate for evidence based policy stemming from multiple reviews.

The inability of the recent Parliament to pass enough meaningful legislation to reform and improve the financial services industry must not be repeated in the 45th term.

This lack of progress is costly. Legislation we believe will assist consumers is still not in place; uncertainty over final legislative arrangements delays investment and diverts managerial attention from creating value for consumers; and other countries are moving ahead of us particularly in the export of financial services.

Review, reform uncertainty and delay come at significant monetary cost to industry. I will provide some new evidence on the costs.

The message from our sector today is directed to our new Parliament. Everyone has come in with mandates and special interests. Fair enough. But I urge every one of you to think about the larger issues we're facing and to act in the national interest when considering them.

Passing the current set of reforms which are still in the legislative pipeline from the last parliament is crucial to the national interest, for economic growth and for greater consumer benefits.

The financial services industry looks forward to working constructively with all parliamentarians to assist them in understanding the importance of the current set of reforms that were left in legislation limbo due to the double dissolution election.

International Trends –The impact of 'Brexit'

There is a tendency to focus on domestic issues without regard to the rest of the world. Over the past few months, an important shift has taken place internationally that will ultimately shape the outlook for our industry and its ability to remain competitive.

The United Kingdom's decision to exit the European Union could have a number of negative impacts on Australian financial services. London is one of the largest financial centers in the world, with financial Services representing 30 per cent of the UK economy. A more independent UK will accelerate integration with other regions, in particular Asia, resulting in intensified competition for Australian financial services exports. London is after all closer to Beijing than Sydney.

The UK has already demonstrated an astute ability to gain entry into key Asian markets – in particular China. The China-UK Economic and Financial Dialogue is a great example. It facilitated London becoming the first Renminbi clearing center outside of Asia – something Australian policy makers quickly sought to copy. More recently, it resulted in plans to launch a London-Shanghai equity trading link – a mutual recognition scheme for distributing fund products, as well as several Chinese financial firms committing to set up bases in London.

The UK will increasingly adjust its regulatory and taxation settings to be internationally competitive.

The Government's plan to galvanise the British economy includes slashing corporate tax rates to 15 per cent. They are renewing their push for Chinese investment. They want, quote 'a super competitive economy' with low taxes and a global focus. A Brexited London may well be an even bigger competitor for us in our own back yard than it would be by remaining in the EU.

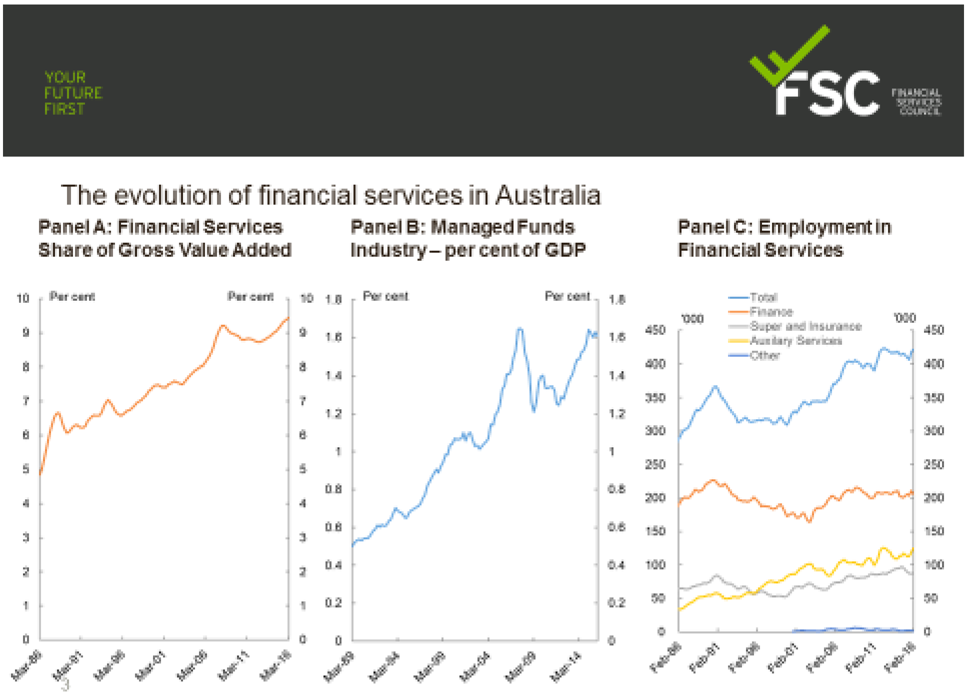
The economic and social stock take – the importance of financial services to our economy over the last 30 years

Over the last 30 years, Australia's financial services sector has grown enormously - whether you measure it in share of GDP, the quantity of financial assets or by employment.

In the mid-1980s financial services trailed behind manufacturing, construction, public services, and mining, ranking as the ninth largest industry in the economy representing 4.6 per cent of economic activity.

Panel A demonstrates that today it is our largest industry, representing 9.3 per cent of economic activity. The growth coincides with a broad shift from production industries towards service industries, a trend that was momentarily interrupted by the mining boom of the early 2000s.

Figure 2: The evolution of financial services in Australia



It is important to understand where this growth is coming from within financial services.

While industry statistics are scarce a bit of extrapolation from data sources confirm international trends in developing economies that growth in financial services over the last 30 years has been split between the wealth management industry ,including asset management, and associated services like financial advice, and products such as insurance, and the expansion of credit, or traditional banking.[1]

Panel B shows that our 2.6 trillion dollar investment management industry has more than tripled in size and represents around 1.6 times our annual economic production. This is up from 0.5 time's annual economic production in the late 1980s.

The industry as a whole directly employs over 450,000 people – panel C. Indirectly, it employs a substantially larger number via outsourced legal, accounting, technology, administration, processing and other services.

<u>These are impressive numbers. But we need to highlight the social value our sector contributes as well – the financial wellbeing and peace of mind, the wealth creation and comfortable retirements that our products, services, and our people deliver every day.</u>

Our life insurance companies paid out $7 to $8 billion worth of claims last year, ensuring that people and families affected by trauma, job loss, illness or death, at least have the financial stability to maintain their lives and livelihoods.

[1] See for example: Greenwood, R., & Scharfstein, D. (2013). The growth of finance. *The Journal of Economic Perspectives*, *27*(2), 3-28.

Australians trust their personal financial advisers. Findings from an ARC Linkage Project conducted by a team of researchers from the University of Adelaide, University of Western Australia and University of Technology Sydney shows strongly that clients of financial planners trust their adviser and find real value in that advice.

Benefits to consumers and consumer trust in advisers will undoubtedly get stronger when the enhanced adviser standards are legislated – hopefully soon.

We need to acknowledge the wealth that is created for consumers and their superannuation savings by our fund managers, who manage to deliver attractive returns and innovative new products in one of the world's lowest fee regimes, generated by intense competition.

Australia has a solid history of trustee companies, public and private, managing and growing the savings and investments of the most disadvantaged Australians through to the biggest philanthropic endowments, charitable trusts and settlements for Australians living with a disability, as well as the new wealth coming into Aboriginal communities via Native Title determinations.

Let's never forget that we have one of the best superannuation systems in the world, which while it still needs improving, manages to create innovative retirement products and options so that fewer Australians have to rely on the age pension. Every Australian must save for their retirement, and our funds do their best to manage and grow these savings.

Financial services companies are leading contributors to corporate philanthropy, putting almost $700 million back into the community via charities and foundations in the last financial year.

We have the chance to raise the bar again tonight at our gala dinner, where we will raise funds for our partner charity, the First Nations Foundation, which works to increase Indigenous financial inclusion.

However, where consumers are adversely affected by products and services our sector has rightly come under a lot of scrutiny. We fully accept that trust is a key issue facing our sector.

We are working hard to restore this trust deficit with our own initiatives in self-regulation. Examples include:

- the Trowbridge Review of Life Insurance, an independent review commissioned by industry – the first of its kind – that has led to a raft of legislative reforms and self-regulatory initiatives, including the development of a consumer Life Insurance Code of Practice to be launched later this year;
- Our colleagues at the Australian Bankers Association are addressing consumer concerns about remuneration, the protection of whistle-blowers, the handling of customer complaints and dealing with poor conduct;
- Many of our member companies have taken unilateral action on economic, social and cultural issues, such as initiating ground-breaking policies to bridge the gender gap in retirement outcomes.

The FSC has <u>set</u> the agenda across the spectrum of superannuation, funds management, life insurance, trustees and advice.

This involves extensive consultation with our members via various working groups and FSC Board Committees contributing to the development of policy positions. It also involves discussions with consumer organisations, government departments, regulators, and the Government.

As the peak industry association for financial services there are two things we ultimately aim to do in our advocacy role – create the case for good, proactive policy that benefits the industry, the nation and consumers; and we also do our best to prevent bad ideas taking hold.

In Investment management, we have successfully advocated for an improvement to the Investment Manager Regime to make it more practical. The IMR reforms remove tax impediments to investing in Australia in order to attract foreign investment here and promote the use of Australian fund managers. It will make our fund managers more internationally competitive.

We have secured a commitment from the Government to provide fund managers with more flexible structures to run their investment products and offerings. Australia's collective investment vehicle regime will be broadened to include both corporate and limited partnership structures.

Our financial services delegation to Japan and Korea last year, led by then Assistant Treasurer Josh Frydenberg, secured Japan's participation in the Asia Region Funds Passport.

And we have continued to publically push our regional investment management ambitions by commissioning the Second Johnson Report.

Figure 3

In Life insurance, we set the standard for industry led investigations with the Trowbridge Review into Retail Life Insurance. This review has culminated in legislation to improve commission arrangements in the provision of life insurance advice, a Life Insurance Code of Practice, and improved reporting requirements for the industry around lapses. We are still waiting for work to start on a product rationalisation framework for legacy life insurance products as recommended by the FSI.

In the Trustee space, we are pleased to have achieved a formal agreement between our trustee members and the National Disability Insurance Agency, ensuring that there is an appropriate exchange of information where they share clients in common. This will not only improve the efficiency of these public services, but also act as a safeguard for the delivery of care to those most vulnerable in our communities.

We put the issue of elder financial abuse on the national agenda and welcome the Australian Law Reform Commission's consultation on this growing problem.

In Superannuation, the Financial Services Council led the industry in corporate governance through self-regulation in 2013 by requiring our member funds to appoint a majority of independent directors and an independent chair to their trustee boards. The Government built on this leadership by introducing legislation into the last parliament to require the appointment of one third independent directors to all APRA-regulated trustee boards – including retail, industry and corporate funds – an important consumer focused reform that should be progressed without delay.

We have also advocated for increased competition and a more open market in the superannuation industry by expanding a consumer's right to choose their own fund and by removing anti-competitive arrangements in the default superannuation market. The Government has commenced these reforms – having introduced legislation to expand choice to all superannuation consumers – but there is more work to be done to achieve an open, competitive market in super that will benefit consumers by putting downward pressure on fees.

In Advice, we developed a framework to increase education, ethical and professional standards of advisers. In fact, in just the past few months, the centrepiece of FSC's 2014 advice framework for an independent standard setting body has been adopted by the Government.

It's a solid body of work. But the challenge we face as an industry is getting more done - not only minimising the volume of review and re-review, but also in removing the traffic jam in Canberra.

Figure 4: A traffic-jam of reform

The former Labor Government of 2007-2013 switched Prime Minister three times, Treasurer twice, the minister for financial services or superannuation four times, and had five different Assistant Treasurers.

The last three years of Coalition Government has seen two Prime Ministers, two Treasurers, and four Assistant Treasurers – with one only working in the role in a part time capacity for more than 12 months.

[Pause] Our industry has experienced 17 changes to our relevant Ministers in the past decade.

It is not as if our issues in financial services are more complex today than they were in the past. In 1997, the then Treasurer Peter Costello when responding to the Wallis Inquiry noted:

"The financial system is undergoing accelerated change through rapid technological innovation, increasing globalization and changing business strategies and consumer needs. Our regulatory arrangements must keep up."

So it would seem that the challenges remain the same.

What has changed? We all have more choice, and we have an increased appetite for change.

We have a more diverse political landscape and our electorate seems more willing than ever before to elect minor parties and independents to seats in the upper and lower houses. Our political leaders seem more willing to restructure themselves and their ministries over and over - embedding delay into the system.

I'm pleased therefore to note we still have the same Minister. We congratulate Kelly O'Dwyer, who will be sworn in as Minister for Revenue and Financial Services. Continuity is paramount – and Kelly already has a strong understanding of our issues.

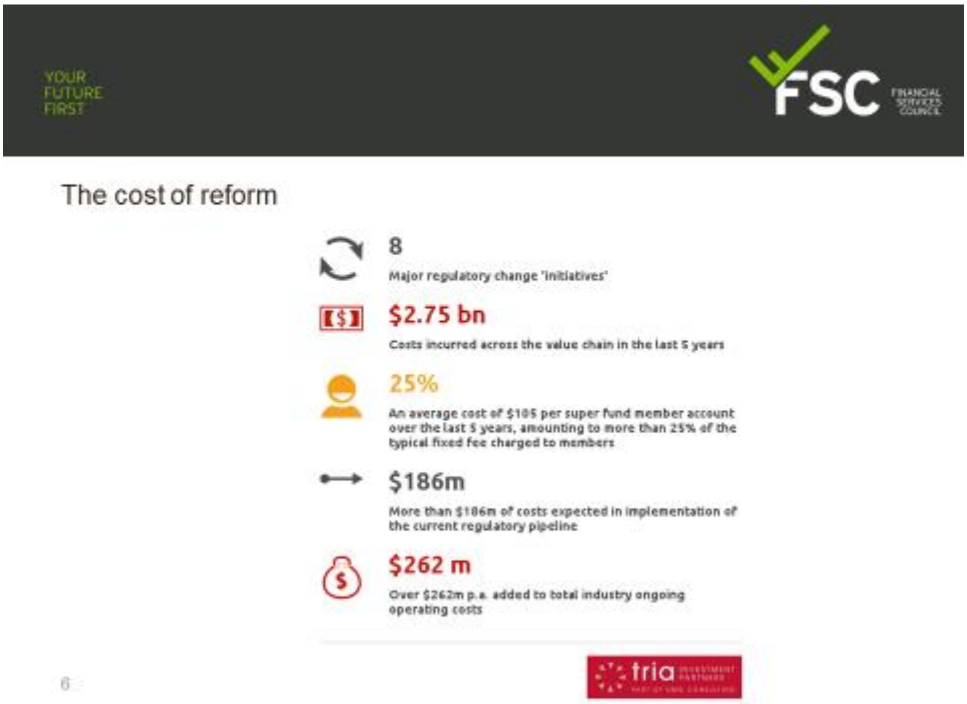
There is a broader need, however, to examine how our system can operate more efficiently. Four or even five year terms for Government would allow politicians to concentrate on long-term issues and focus on developing efficient regulation.

<u>Today I am launching new research by independent consultancy Tria Partners examining the cost to the industry and consumers of ongoing regulatory reform in the financial services industry.</u>

Tria Partners has concluded that across the financial services industry, the past five years of reform has cost $2.75 billion, which is estimated to reach almost $3 billion once the current reforms being debated by parliament are fully implemented.

In turn this creates a very real cost to consumers, estimated at $105 per superannuation account over the past five years – equivalent to 25 per cent of the typical fixed fee charged to superannuation fund members.

Figure 5 - Reform and delay mean significant cost for industry and consumers



Regulatory reforms to the financial services industry have been necessary to address structural issues and improve consumer outcomes, however the cost of these reforms to consumers, as revealed for the first time at the FSC Leaders Summit, are substantial.

Regulatory reform must be 'fit for purpose' to ensure that excessive cost is avoided and our superannuation, life insurance and financial advice sectors can continue to deliver high quality services for the lowest possible cost. Quality regulation requires detailed consideration and development by legislators, and a well-functioning parliament.

We urge the parliament to get the politics out of considerations and focus on best outcomes for consumers.

And stop kicking the can down the road. The cost of inaction and delay is even greater – and can't be measured.

Our 45th Parliament must pass the legislation in the pipeline. It can implement lasting solutions by passing the backlog of legislation from last term, and from previous reviews – and commit to it in the first 100 days of government.

Life insurance

- We need to pass the Life Insurance Reform laws. Every day we fail to pass this legislation, is another day with inappropriate incentives in the market. There is bipartisan support for these measures, so they should be swiftly implemented.

Superannuation

- Enshrine in legislation the objective of the superannuation system with bi-partisan political support – the objective must be for adequate retirements for Australians, not narrowly tied to the age pension – and calibrate the tax settings to that objective.
- Implement reforms to promote choice and competition in superannuation to deliver lower fees and better products for consumers.
- Improve governance standards by requiring all funds to appoint independent directors.
- Remove regulatory, tax and social security barriers in order to open the retirement income market to new and innovative products.

Advice

- Increase education and professional standards of financial advisers by legislating a new independent standards setting body responsible for establishing adviser standards.

Trustee Services

- Legislation is required to reform the current licensing regime, providing greater consumer protection and ensuring competitive neutrality.

Investment Management and Global Markets

Expedite the outstanding 2009 Johnson Review 'Australia as a financial centre' agenda items, including:

- Continue with timeframes committed to in the May Budget for development of Corporate Collective Investment Vehicles by 1 July 2017 and a Limited Partnership CIV by 1 July 2018.
- The withholding tax rate for receipts from Passport funds should be simplified with a five per cent applying only to 'withholdable' income.

<u>Financial services is the next opportunity we have to lead the world and deliver more Australian jobs in an otherwise uncertain economic environment.</u>

In order to fully exploit our natural advantages in funds and wealth management we need to embrace globalisation and free trade. Money knows no borders, except where there are uncompetitive tax regimes.

In agriculture we removed tariffs and ensured our farmers became the world's most efficient and effective producers and exporters. Same with mining.

<u>A Deloitte Access Economics report we commissioned in 2014 found that if Australia could grow overseas-sourced funds under management to equal that of Hong Kong over the next decade, the benefits would be significant – GDP would grow by $4.2 billion, tax revenue by $1.2 billion and nearly 10,000 Australians jobs would be created.</u>

<u>But in reality, how close are we?</u>

The Second Johnson Report shows that only one of the original recommendations relating to funds management has been satisfactorily completed. Another ten have either been commenced or committed to. Further, over the last seven years new barriers have emerged, including uncompetitive withholding tax arrangements.

While wholesale tax reform unfortunately looks near impossible in the short-term, it should surely be within the ability of the government to reform one small part of the 10,000 page Tax Act – the simplification and reduction of withholding taxes.

With the Asia Region Funds Passport, we have a brand new export trade structure for financial services in our region for retail clients – but without a simplified withholding tax regime it will not work.

It's not as though replacing the current system will create a big hole in tax revenues - tax revenue collected from retail investors in the Passport countries is tiny – just $5 million – an asterisk in the Budget papers.

We know we have no time to lose.

So what can we, the industry, and the 45th Parliament of Australia achieve for the financial services sector, consumers and the economy:

1. The parliament gets back to work and implements the backlog of reforms in life insurance, financial advice and superannuation that have emerged from the plethora of reviews and inquiries into the financial services industry– and then takes a step back to allow the corporate regulator to enforce the law.

2. End the reviews and inquiries– we do not need a royal commission that would defer consumer orientated reforms another two years when we already have the pathway to a stronger, consumer focused industry before us

3. We now have a properly resourced regulators so there are no excuses. We believe in regulation that is strongly enforced. We cannot say we need new laws when we haven't enforced the existing laws.

4. Being a heavily regulated and technically complex sector – compliance and regulation are paramount, as they must be – means our world is replete with jargon and eye-wateringly difficult detail. We, the financial services industry, need to be better at explaining what we do and how we do it, the value of our work and the great benefits our services and our products deliver.

Finally, the industry rises to the challenge of restoring trust in financial services by recognising it is also our responsibility to better deliver for consumers.

Thank you.