FSC FINANCIAL SERVICES COUNCIL

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# Future of Super

**Thursday 18 May**

I'd like to start by thanking *Super Review* for the opportunity to speak to you today about the impact of the Federal Budget on the financial services sector.

In the lead up to the Budget it's near impossible to separate rumour from leak from kite flying.

Budget Day is arguably the busiest in the calendar for Parliament House as journalists, lobby groups and other stakeholders jostle in the halls for an inside line on what surprises might lurk within.

Rest assured the party from the Financial Services Council that made the journey down to Canberra left no stone unturned in preparing for all eventualities … and then joined everybody else in tearing up our drafts once our senior policy managers emerged from the lock-up with the good oil.

While there are a number of measures in this year's Budget which will have impacts on our sector, which I will come to, in general terms – and in fitting with the post-budget Fairfax-Ipsos poll which saw 44 per cent of respondents say they were 'satisfied' with the overall budget versus 43 per cent who were 'dissatisfied'– we were pleased to see no material impacts to superannuation savers from a taxation or financial planning perspective.

This was vastly different from Budget 2016 when we were slugged with 12 major changes to super. In the frantic hour post-lockup our priorities were emailing our analysis to our 100 plus member organisations and getting it to the media.

Last year I spent an adrenaline charged several minutes on the SKY Business set with David Speers analysing these massive shifts to super – most of which were designed to severely crimp the amount people could contribute, tax advantaged, into super.

We deemed the changes tough, very tough, but ultimately fair. The FSC's position on super is that it is not, and should never be, a vehicle for intergenerational wealth transfer.

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The tinkering with superannuation that has occurred in almost every Budget does erode confidence in the system. It introduces additional complexity which turns consumers off, not to mention adding to the cost of doing business, as funds have to adapt their systems. This year we commended the Government for steering clear of pulling major superannuation policy levers.

**Fresh consumer protections should end calls for Royal Commission**

The significant – indeed unprecedented – new consumer protections introduced in this Budget should end calls for a Royal Commission into the financial services industry.

Despite more than a decade of intense scrutiny and a raft of continuous reform, including over 15 major reviews and inquiries – at a cost borne by our sector of more than $3 billion – and overseen by 17 different ministers in the financial services portfolio – the Government announced a package of even more stringent measures and new powers for the prudential regulators.

There will also be a one stop shop for consumers to raise complaints about financial institutions.

This significantly increased regulatory oversight of financial institutions - which should not be finalised without further consultation with industry - must surely mean an end to the politicisation of the financial services industry.

A Royal Commission has been rendered unnecessary.

**Banking Executive Accountability Regime**

Partially hidden from view by the headline $6.2 billion levy on Australia's five largest banks, the Budget contained a significant new reform package called the Banking Executive Accountability Regime, – aka the BEAR – a suite of new regulatory requirements on banks and other financial institutions that includes the capacity for APRA to block the hiring of new executive employees and the registration of executives.

This is what we know: Under the new regime, prior to appointing senior executives and directors, Authorised Deposit-taking Institutions (ADIs) will need to advise APRA and, once appointments have been made, register the new roles and responsibilities with the regulator.

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APRA will also be given stronger powers to remove and disqualify senior executives and directors from all APRA-regulated institutions. The accountability regime also introduces new powers and penalties that set expectations for how ADIs and their executives conduct their business consistent with good prudential outcomes.

The Government has said these expectations would cover matters such as “conducting business with integrity, due skill, care and diligence” and “acting in a prudent manner.”

For those that fail to meet these expectations, a new civil penalty of up to a maximum of $200 million will apply for larger ADIs and $50 million for smaller ADIs. APRA will also be able to impose penalties if ADIs do not appropriately monitor suitability of their executives to hold senior positions.

These reforms, along with recent legislation raising the professional standards of financial advisers and addressing conflicted remuneration in life insurance, mean consumers are better protected than ever before.

Senior executive remuneration at ADIs will also be under the microscope with new rules requiring a minimum of 40 per cent of an

ADI executive's variable remuneration – and 60 per cent for certain executives such as the CEO – to be deferred for a minimum period of four years.

APRA has also been given stronger powers in this area to require ADIs to review and adjust their remuneration policies when APRA believes they are producing inappropriate outcomes.

These powers are without precedent in Australia and unintended consequences must be carefully avoided – so we have strongly urged the Government to consult with industry before implementation of the Bank Executive Accountability Regime.

**Bank levy**

Grabbing the headlines of course was the Major Bank Levy which will apply to the Big Four and Macquarie Bank and is estimated to raise $6.2 billion over four years.

I'm sure most of you will have digested the detail but the levy will apply to ADIs with liabilities of at least $100 billion from 1 July 2017 with the $100 billion indexed in line with nominal GDP.

It is calculated quarterly as 0.015 per cent of licensed entity liabilities for an annualised rate of 0.06 per cent and will include corporate

bonds, commercial paper, certificates of deposit and Tier 2 capital instruments but will not apply to Tier 1 capital, deposits of individuals or businesses, or other entities protected by the Financial Claims Scheme.

IN other words, an ADI's liabilities excludes the assets and liabilities held or managed by FSC members - there is a clear delineation for prudential purposes between the assets of an ADI and those of an insurer or superannuation fund.

Our members include the banks’ wealth and insurance businesses, not the banking institutions, whose industry organisation is the Australian Bankers Association. There have been forests felled in the post-Budget days to accommodate the commentary on the levy.

I do not plan to add to it. We, like everyone else with a super funds invested in the banks, watched value wiped off those stocks as the story leaked out on the eve of the Budget.

Hopefully this will be short-term.

**One-stop complaints shop**

The Budget also confirmed the introduction of a one-stop shop for consumers to resolve disputes with financial services companies.

The Australian Financial Complaints Authority (AFCA) will commence operation from 1 July 2018.

It will be industry funded with the expected cost still to be confirmed.

The new body will be able to hear disputes of a higher value so that more consumers and small businesses will have their disputes heard without going through the process of seeking resolution in the courts.

The AFCA will absorb the Financial Ombudsman Service, the Superannuation Complaints Tribunal and the Credit and Investment Ombudsman, however the FSC understands that matters brought to the AFCA will be treated in the same way as comparable matters currently brought before those existing organisations. For example, superannuation related matters determined by the AFCA will be binding, as they are at the Super Complaints Tribunal.

Collectively, this new authority and the executive accountability regime lays out a blueprint for strengthening consumer trust in the financial services industry.

In saying that, the current Super Complaints Tribunal works well and we would welcome its current structure remaining under the new organisational framework.

Taking the new regulations as a whole, the FSC calls on all parties to finalise this package of reforms so that we can bring an end to the politicisation of the financial services industry. These changes will have significant ramifications for the sector and we expect to be fully consulted before implementation.

**Housing package**

Turning back to superannuation; we – along with many others - argued strongly pre-Budget that the nation's compulsory savings pool should not be raided to address short-term economic topics du jour, like first home deposits or to plug the deficit. That approach would undermine the system, erode confidence of consumers and conflict with the Government's own proposed purpose of super: to

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provide income in retirement to substitute or supplement the Age Pension.

This didn't eventuate, thankfully. With the compulsory 9.5% super guarantee ring-fenced, the design of the newly announced First Home Super Saving Scheme promotes saving for first home buyers, without diluting the current superannuation nest-egg provided by our universal superannuation system.

There will be additional flow-through effects which could in turn boost the retirement incomes of super members.

Think about it.

We know that because of our uncompetitive and flawed default super system most people, particularly younger Australians, are disengaged from their superannuation. Many cannot tell you the name of their superannuation provider, let alone their balance or investment options. In fact, less than a third of Millennials read their super statements and 40 per cent do not know their balance.

Yet deep in the Australian national psyche is the desire to own property, our own home.

Enabling first home savers to use the superannuation architecture to achieve their dream of owning property, provides a number of valuable touch points between superannuation funds and providers.

Super funds have an opportunity to contact a targeted cohort of members, to talk to them about the new initiative. There is an opportunity to engage this group so that they no longer see their fund as something they can ignore until they near retirement but rather as a means to get onto the housing ladder sooner.

Engaging with super will prompt people to merge multiple accounts; to consider their insurance cover and review their investment options. The boost to their capital that they receive saving for a deposit via their super fund, will teach them that super is the best place for their savings over the long-term. This will surely prompt salary sacrifice contributions above the levels we see today.

To criticise the policy – as a few have - as contrary to the sole purpose test or the thin end of the wedge to allowing wholesale raids of super for housing, is to support the status quo, wholesale consumer disengagement..

The current superannuation system with its massive defaulting numbers, assumes, in fact encourages, ambivalence. Initiatives like the Budget's First Home Super Saving Scheme that promote engagement and choice, will surely result in more innovative products with lower fees.

The other major super initiative in the Budget is the retirement house downsizing option. We support the Government's efforts to remove barriers to downsizing by enabling older Australians to contribute windfall gains of up to $300,000 from the sale of their home to superannuation, without breaching super caps.

The policy does not exempt the sum from the pension asset test so it remains to be seen how much take up there will be, but the additional flexibility it provides for older Australians who, under the current system may be incentivised to stay in homes that are unsuitable for them as their mobility deteriorates, is certainly positive.

It could also ease the supply problem in urban areas, freeing up larger homes for younger, growing families.

**Tax relief for merging super funds**

The extension of Capital Gains Tax relief for superannuation fund mergers is a practical measure to promote better consumer outcomes.

Since December 2008, tax relief has been available for superannuation funds to transfer capital and revenue losses to a new merged fund, and to defer taxation consequences on gains and losses from revenue and capital assets. This tax relief was due to lapse on 1 July 2017.

The tax relief will be temporarily extended as the Productivity Commission completes a review into the efficiency and competitiveness of Australia's superannuation industry.

Extending this relief will remove tax as an impediment to fund mergers and facilitate industry consolidation, which will in turn lead to better retirement outcomes through reduced costs.

The long tail of under-performing super funds must be given every encouragement to merge with better performing funds for the benefit of consumers and the long-term sustainability of the system.

**Open data and Fintech**

The final pieces in the financial services Budget jigsaw relate to financial technology and the use of data.

Consumers will have access to and control over their banking data with the introduction of an open banking regime in Australia.

Increased access to data will improve the information available to consumers and better enable innovative business models to create new products.

We'd like to see Australia take its place as a leading global FinTech hub and the new package in the Budget should boost that goal.

**Productivity review into competition**

Finally, while not a Budget measure, I want to say a few words about the newly announced Productivity Commission review into the state of competition in the financial system, commencing on 1 July 2017.

The Commission is to review competition with a view to improving consumer outcomes, the productivity and international competitiveness of the financial system and economy more broadly, and supporting ongoing financial system innovation, while balancing financial stability objectives.

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The FSC supports open competition across all parts of the financial system, particularly in superannuation, and looks forward to being part of the consultation process.

When it comes to super, as we have long advocated, choice and competition are the central pillars of the system we believe will be the best policy for future generations – the system we call Super 2.0.

Super 2.0 is a set of policy conditions that are flexible and enable the development of an efficient and innovative super system over time.

Super 2.0 – based on choice, flexibility and competition, will kick start an arms race in innovative new super products and services.

Our 25 year old system has done a good job but it needs to modernise and be made fit for purpose – to deliver the best savings system for the generation of Australians entering the workforce today, who will have dozens of jobs, many of them in the gig, or uber-ised economy.

Opening the default super structure to choice and competition would  mean that funds would have to actively compete for and chase new members and talk to them in a way that engages them, on the right platforms – digital platforms.

Importantly too, it would help close the current gender gap in super – which we know starts to open up when men and women are in their 20s, when they're in their first jobs.

Getting young people – particularly young women – engaged with their super via an innovative, flexible and competitive new system will help close the gender gap.

We can no longer afford to be ambivalent about gendered wealth inequality.

**Further consultation needed**

To summarise, the Budget has introduced a raft of stringent new regulations and consumer protections - and commendably has avoided unduly moving the superannuation goalposts.

As I said, the housing package delivers a savings vehicle to first home buyers that promotes engagement with their retirement savings - and at the other end of their superannuation journey, provides flexibility.

We support the removal of barriers to innovation in FinTech.

However, the new regulations have taken the industry by surprise.

We look forward to consulting with the Government, Treasury and the regulators ahead of their introduction.

Finally – an ideal Budget will be when there is no tinkering with superannuation – in its Super 2.0 form of course - when this excellent piece of public policy is removed from the annual budget cycle and any changes or reviews are instead linked to the five-yearly Intergenerational Report.

Utopia will be when superannuation, and indeed all financial services – the biggest contributor to the nation's economic wealth – is no longer a political football.

Thank you.