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Professor Ian Ramsay

EDR Review Secretariat

Financial Markets Division

Markets Group

The Treasury

Langton Crescent

PARKES ACT 2600

Dear Professor Ramsay

Response to interim report: *Review of the financial System External Dispute Resolution and Complaints Framework*

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide the attached response to the interim report: *Review of the financial system external dispute resolution and complaints framework,* released on 6 December 2016.

If you have any queries or comments in relation to the content of our submission, please contact me on (02) 8079 0808 or by email gmccrea@superannuation.asn.au, or Julia Stannard, Senior Policy Adviser, on (03) 9225 4027 or by email jstannard@superannuation.asn.au.

Yours sincerely

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Response to interim report: *Review of the financial System External Dispute Resolution and Complaints Framework*

A. ABOUT ASFA

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90 per cent of the 14.8 million Australians with superannuation.

B. GENERAL COMMENTS

This submission is primarily focussed on the experience of members, beneficiaries and trustees of APRA-regulated superannuation funds. During ASFA's consultations as part of this Review, our members have reported little or no involvement with the Credit and Investments Ombudsman (CIO). While many APRA-regulated superannuation funds are also members of the Financial Ombudsman Service (FOS), the Superannuation Complaints Tribunal (SCT) is their primary scheme for external dispute resolution (EDR) and interactions with the FOS are typically focused on issues of advice.

ASFA has been pleased to participate in this Review, which invites a discussion of matters critically important to all stakeholders in the financial services industry. ASFA has been vocal over many years in raising our concerns about the lack of funding and resourcing provided to the SCT, which has so severely impeded its capacity to perform its important role.

There is no doubt that change is needed, and this Review provides the opportunity to reform the EDR arrangements for superannuation in a way that will benefit all stakeholders – delivering more efficient outcomes for consumers, while ensuring their interests – and those of all beneficiaries – are adequately protected.

The Review Panel's interim report, *Review of the financial system external dispute resolution and complaints framework* (Interim Report) clearly articulates the difficulties currently faced by the SCT, as well as the many recognised strengths of the Tribunal model. We welcome the clarity with which these issues have been stated.

However, that same clarity of articulation is not evident in the reasoning behind many of the Interim Report's draft findings or, significantly, its major draft recommendation that the SCT be replaced with a Superannuation Ombudsman. Rather, the Interim Report simply assumes a change of model is required for superannuation-related complaints, without clearly demonstrating why better outcomes could not be achieved through changes to the existing model.

ASFA's October 2016 response to the Review's issues paper identified many areas where changes to the SCT model could achieve significant improvement. This submission builds on that response, and identifies changes that could be made to significantly improve outcomes for consumers while retaining the benefits and protections afforded by the current statutory tribunal model.

ASFA supports a strong focus on consumers as key stakeholders in the EDR process, and we consider it imperative to ensure that any arrangements put in place as a result of this Review deliver improved consumer outcomes. We note, however, the significant risks in moving away from the current SCT model - with no monetary limit on access or redress, enforceability of determinations and rights of appeal - to a membership-based industry ombudsman scheme where there is scope for limits to be imposed on the type or value of claims that may be pursued, no direct right of appeal, and the possibility that the individual will need to pursue contractual remedies against a provider to enforce a decision.

C. SPECIFIC COMMENTS IN RESPONSE TO THE ISSUES PAPER

1. Modernising EDR for superannuation – much to gain, much at stake

Draft recommendation 4: A new industry ombudsman scheme for superannuation disputes

SCT should transition into an industry ombudsman scheme for superannuation disputes.

ASFA disagrees with draft recommendation 4. While we accept many of the Review Panel's draft findings regarding issues with the SCT's current performance, we do not consider that an incontrovertible case has been made that the "dispute resolution mechanisms for superannuation are broken"[1].

Further, while the Interim Report asserts that the SCT model "will not withstand future pressures"[2], this appears to be based on an assumption of no change to the existing model, when even the most vocal supporters of the SCT – and indeed the SCT itself – have called for improvements to the model.

In proposing the replacement of the SCT with the Superannuation Ombudsman – a step which would involve significant cost and disruption for the industry, and, therefore consumers – insufficient consideration appears to have been given to effecting meaningful change within the tribunal model.

The Interim Report identifies a number of **benefits** to consumers that might be expected to flow from replacement of the SCT with a Superannuation Ombudsman, in terms of flexibility and improved service. As set out in this submission, ASFA does not dispute that the present membership-based EDR schemes perform significantly better than the SCT (as currently configured) against these benchmarks, but we do not accept that such performance is unique to a membership-based scheme or that the tribunal structure is necessarily a barrier to a service-oriented model. These issues can, in ASFA's view, be overcome with appropriate resourcing, funding, internal process improvements and enhancements to governance structures, accountability and transparency.

Further, of significant concern to ASFA and our members is the **lack of weight placed on the clear disadvantages for consumers if the statutory tribunal model is abandoned**. In this respect, it should be clearly understood that the primary concern of the superannuation industry is not with retention of the SCT for its own sake, but with preserving the many consumer protections and safeguards that are inherent in the tribunal model and stand to be lost in a move to an industry ombudsman scheme. While the interim Report asserts that the proposed Superannuation Ombudsman "would incorporate the key benefits of both the tribunal structure and industry ombudsman schemes"[3], there is genuine apprehension within the industry that implementation of a membership-based ombudsman scheme will ultimately deliver inferior outcomes for consumers.

In our response to the issues paper, ASFA highlighted the complexity which is frequently observed in superannuation-related complaints, particularly those involving defined benefit arrangements, insurance through superannuation and death benefit distributions. This complexity, which sets superannuation aside from other financial products, makes it vital that those fulfilling the EDR function have deep specialist knowledge and expertise.

Our response to the issues paper also outlined a number of aspects of the current SCT model which are so beneficial, in terms of the protections and rights provided to consumers and fund trustees, that we consider they must be retained in any superannuation EDR model going forward. Two of the most critical of these attributes relate to:

[1] The Australian Government, the Department of the Treasury, *Review of the financial system external dispute resolution and complaints framework*, Interim Report, 6 December 2016 (EDR Review Interim Report), p17
[2] EDR Review Interim Report, p17
[3] EDR Review Interim Report, p151

- the enforceability of determinations, which avoids significant issues of non-payment of determinations that have been experienced, since inception, with the FOS (and, to a lesser extent, the CIO)
- the ability to appeal directly from a determination to the Federal Court on a question of law.

It is clear, from the comparison in the Interim Report of the current SCT and the proposed Superannuation Ombudsman[4], that these vital consumer protections will be lost.

Our concerns on these points are outlined in some detail below. By way of introduction, however, we note that these protections are among many benefits of the tribunal model that currently are simply taken for granted. While it is fair to say that the average consumer may not appreciate the significance of these attributes at first glance, we fear that their absence under the proposed Superannuation Ombudsman would be sorely missed by many consumers, when confronted with the reality of a scheme which effectively operates under contract law and could result in a successful complainant having to seek contractual remedies against a trustee to enforce the Ombudsman's decision[5].

ASFA does not presume to judge the appropriateness of a contract-based EDR scheme for financial products and services that are purchased under contract. However, in ASFA's view such a model is inappropriate for superannuation products which involve a significant element of compulsion and are predominantly provided through trust structures, with trustees under fiduciary duties to act in the best interests of members. When viewed against that backdrop, leaving unsatisfied complainants to pursue remedies in contract law is, we consider, an unacceptable outcome.

Rather than proceeding straight to the conclusion that the SCT should be replaced with a Superannuation Ombudsman, **ASFA recommends that further consideration be given to specific improvements to the Tribunal's current operating structure** (as outlined in this submission) **and a substantial boost to its funding and resourcing**.

The revamped SCT should then be tasked with delivering a set of agreed outcomes and performance improvements within a 'grace period' of not less than three full financial years, timed from full implementation of the changes and receipt of the additional funding. A shorter period would, in ASFA's view, be inappropriate and unrealistic. The current backlog in complaints, and the entrenchment of manual and inefficient processes, has taken some years to develop and equally it will take some time to reverse.

At the conclusion of the grace period, the SCT's performance should be independently reviewed against its agreed outcomes by the Australian National Audit Office and, if adequate progress has not been made, a transition to an industry ombudsman scheme could be considered at that time.

1.1 Some benefits and protections in the current model are too important to lose

It is critical to fully understand the many positive aspects of the tribunal model – including important consumer protections - that would be lost in moving to a membership-based ombudsman scheme.

It is also vitally important to understand some of the aspects of superannuation which set it apart from other types of financial products.

Superannuation is, largely, a compulsory model and therefore different to other types of financial products. A number of consequences flow from the unique nature of superannuation:

- there is a need to ensure that all complainants in relation to APRA-regulated superannuation can be dealt with

[4] EDR Review Interim Report, p151-154
[5] The contractual nature of remedies is explicitly acknowledged in the EDR Review Interim Report, p153

- there is a trust dynamic, with trustees bound to act in the best interests of members
- trustees are under an obligation to fully rectify a member/beneficiary who has suffered a loss, but to more than fully rectify that member/beneficiary – for example, by awarding compensation for non-financial loss, as proposed - would cause detriment to other members/beneficiaries to whom the trustee owes fiduciary duties
- rights of appeal, enforceability of determinations and freedom of information are very important.

These matters are considered in more detail below.

1.1.1 A contract-based EDR scheme is not a good fit for trust-based superannuation

Many financial products and services are purchased by consumers effectively under a contract of sale, with the consumer and the provider bound by the terms and conditions of that product, although the provider may also be subject to some additional obligations under legislation[6]. As the relationship between the consumer and the provider has its basis in contract law, a membership/contract-based EDR scheme is not inappropriate for such products.

In contrast, superannuation is a relationship based in trust law, rather than contract. A consumer applies for membership of a fund (or their employer may do so on their behalf). If eligible, membership will be granted and the member and trustee are subject to the terms and conditions set out in the fund's governing rules – typically, its trust deed. As with providers of non-superannuation products and services, the trustee is also subject to additional obligations under legislation[7]. Uniquely to superannuation, however, the trustee is also bound by duties and obligations imposed under trust law which go beyond those codified into the superannuation legislation.

The fiduciary nature of superannuation as a product colours every aspect of the relationship between the trustee, individual fund members/beneficiaries, and the membership as a whole. It means that superannuation trustees are obliged to act differently to the providers of other financial products and services in many key respects. One example that is extremely pertinent in this context is the fundamental obligation to act in the best interests of all members. This may have a number of consequences:

- the provider of another type of product may choose to settle a dispute at the IDR stage, despite the merits of its position, if its pursuit may prove uncommercial given the fee structure of the membership-based EDR scheme. A superannuation trustee, however, must consider the impact on the membership as a whole of settling a claim which it considers to be without basis

- where a decision is made at EDR which the trustee disagrees with, particularly if it would impact on the trustee's decisions in relation to future payment of benefits, there is a need to strongly consider any grounds of appeal or review which can reasonably be pursued (see 1.1.7 below regarding the need to retain a direct right of appeal) to ensure the trustee is appropriately handling the monies held on trust for the membership.

[6] Including licensing, conduct and disclosure obligations under the *Corporations Act 2001*

[7] Under the *Superannuation Industry (Supervision) Act 1993* and *Superannuation Industry (Supervision) Regulations 1994*, and also licensing, conduct and disclosure obligations under the *Corporations Act 2001*

1.1.2 Universal access and unlimited monetary jurisdiction must be preserved

Given the largely compulsory nature of the superannuation system, it has extensive coverage across the working age population as well as considerable coverage of retirees, given the increasing trend toward taking retirement savings as an income stream rather than a lump sum. For many Australians, their superannuation balance represents their largest financial asset and their largest asset after the family home.

As a result, ASFA considers it critical that universal access is guaranteed to the EDR scheme covering APRA-regulated superannuation. In addition, there must be no financial threshold applied to determine the eligibility of a fund member (or former member) or their beneficiary to seek EDR.

The Interim Report states that the terms of reference for the proposed Superannuation Ombudsman "could be designed to replicate the existing SCT's jurisdiction, including unlimited monetary jurisdiction"[8] (our emphasis). In ASFA's view, it would be imperative that this occurred. However, as the terms of reference would be subject to initial negotiation and potential future amendment, the promise of universal access to EDR would carry sufficiently less weight than one entrenched in statute, as is currently the case.

While ASFA strongly supports universal access to superannuation EDR, we do believe there is considerable merit in examining streamlined processes for dealing with smaller value claims (see 1.6 below.)

1.1.3 Enforceability of determinations is key

SCT determinations are currently binding on the trustee, with non-compliance reported to ASIC or APRA (as appropriate)[9]. Failure to comply with an injunction is not an offence, however it constitutes a breach of the *Superannuation Industry (Supervision) Act 1993* (SIS Act 1993), including the "RSE licensee law", and *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations 1994). It can therefore represent a contravention of the trustee's registrable superannuation entity (RSE) licence conditions, thereby imperilling their ability to operate the fund as an RSE[10]. There is also the ability for the relevant regulator, or the complainant, to apply to court for a performance injunction[11].

The robustness of the current legislative framework for enforceability of SCT determinations is such that the incidence of non-compliance, historically and currently, is negligible – the mere availability of the prescribed sanctions has been sufficient to encourage compliance.

This position must be contrasted with the incidence of non-payment of determinations experienced with the membership-based Ombudsman schemes. As highlighted during this Review:

- from 1 January 2010 to 30 June 2016, 32 financial service providers were unwilling or unable to comply with 137 FOS determinations. These determinations impact 194 consumers and were worth some $16.6 million on 30 June 2016[12] (including interest and adjusting for inflation) and $17 million as at 1 November 2016[13]
- as at 1 November 2016, there were five unpaid CIO determinations of $414,443, involving four providers and affecting seven consumers[14].

[8] EDR Review Interim Report, p152
[9] *Superannuation (Resolution of Complaints)Act 1993*, sections 64 and 64A
[10] *Superannuation Industry (Supervision) Act 1993*, section 64A, section 10 definition of 'RSE licensee law', section 29E; SIS Regulations 1994, regulation 13.17B
[11] *Superannuation Industry (Supervision) Act 1993*, section 315
[12] Financial Ombudsman Service, *Review of the financial system external dispute resolution framework - FOS Submission – Part 2*, October 2016, p52
[13] EDR Review Interim Report, p165
[14] EDR Review Interim Report, p165

Despite the SCT model clearly providing a superior outcome for consumers in this respect, the Interim Report states that, under the proposed new Superannuation Ombudsman:

> *Trustees would be contractually bound to abide by decision if accepted by complainant. Non-compliance would not be an offence but there would be sanctions available under the scheme itself, or consideration could be given to alternative regulatory action by ASIC or APRA. Complainant or the scheme operator could seek contractual remedies against trustee to enforce compliance with the decision.*

In ASFA's view, forcing a consumer who has been successful in obtaining a decision against their financial services provider to pursue remedies in court under contract law to enforce the decision is simply an unacceptable outcome.

We anticipate that in any transition to a membership-based EDR scheme, the conditions in the *SIS Act 1993* for obtaining and holding a license to operate a registrable superannuation entity (RSE) would be amended to require the trustee to become a member of the Superannuation Ombudsman (see section 2.7.1 in this submission). It would be necessary to consider whether a requirement can be entrenched that a trustee may only contract for group life insurance with an insurer that has agreed to become a member of the Ombudsman scheme (and to remain a member for a specified run-off period after that contract ends). We further expect that the terms of membership of the scheme (effectively a contract) would include a requirement that any scheme member must agree to pay any amount specified in a determination.

In theory, these contractual and regulatory provisions should have the effect that a trustee or insurer would settle the obligation under a determination of the Ombudsman scheme, rather than expose itself to potential expulsion from the scheme and, thereby, potential loss of its RSE license or its practical ability to provide insurance to trustees who are RSE licensees. However, the current level of unpaid FOS determinations does give cause to question whether the theory will be borne out in practice.

We understand that where a provider has failed to comply with a decision by one of the current membership-based EDR schemes, the operator has the ability to expel the provider from membership of the scheme. Failure to be a member of an approved EDR scheme would constitute a breach of the provider's Australian Financial Services License obligations[15].

However, as noted in the Interim Report, it appears that the option to expel is exercised very rarely. FOS expelled one provider in 2010-11 due to non-payment of a determination but none since, "because those members, who may otherwise have been expelled, have either become insolvent or have had open disputes brought by other customers"[16] (our emphasis). ASFA understands the need to ensure continuing access to EDR arrangements for other customers of a non-compliant provider. However, it a scheme operator is unable or unwilling to expel a provider from membership because such action would jeopardise the interests of other individuals with 'live' complaints against the provider, the threat of expulsion is effectively invalid as a sanction against non-compliance and the scheme operator is left with little scope to take meaningful action against a provider.

Similarly, we note the admission by FOS, acknowledged in the Interim Report, that "its unpaid determinations are unrelated to its powers, capacity or willingness to enforce its determinations and that it has used litigation to ensure compliance with its determinations where the financial services provider is solvent and there is a good likelihood of recovery"[17].

[15] *Corporations Act 2001*, subsections 912A(1)(g) and (2)
[16] EDR Review Interim Report, p64
[17] EDR Review Interim Report, p165

In ASFA's view, these factors demonstrate the inferiority of the enforceability mechanisms of a membership-based based EDR scheme compared to the statutory model of the SCT.

1.1.4 The ability to join or obtain information from third parties is important

Membership-based EDR schemes, such as FOS currently, may have the ability to join other parties to a dispute. However, the scope of parties who may be joined will be limited to other providers that are members of the EDR scheme[18].

In contrast, the SCT has extensive statutory powers to join third parties to a complaint, which are not dependant on that party being a 'member'. Broadly, these powers apply to allow the SCT to join an insurer, to a matter relating to an insured death or disability benefit[19], and a potential death benefit claimant, to a matter relating to distribution of a member's death benefit[20].

These powers reflect complexities that are unique to superannuation and not encountered with other types of financial products and services:

- Some benefits to which members and beneficiaries may be entitled are referable, in whole or part, to amounts payable under insurance cover provided under a contract between an insurer and the trustee. The provider of that cover may change over time, and there may be a need to ensure that the particular insurer that was 'on risk' is identified and any liability is correctly attributed

- Where a death benefit is payable in respect of a deceased fund member, there may be a range of potential beneficiaries and it is necessary to ensure that all have the opportunity to be heard before the distribution is made.

As noted at section 1.1.3 above, it would be necessary to consider whether the *SIS Act 1993* could be amended to provide that a trustee may only contract for group life insurance with an insurer that has agreed to become a member of the Ombudsman scheme (and to remain a member for a specified run-off period after that contract ends). However, it is not clear to ASFA how the ability to join other third parties, which is vital for many superannuation related complaints, could be preserved within the proposed Superannuation Ombudsman.

The SCT also has broad powers, under the *Superannuation (Resolution of Complaints) Act 1993* (S(ROC) Act 1993), to obtain information from persons who are not parties to a complaint. ASFA understands that while these powers are not frequently used, they have proved important in cases such as disablement claims where an employer has declined to provide information about the complainant's duties and work arrangements. It is not clear how a membership-based ombudsman scheme could be empowered to obtain information in such instances.

[18] for example, article 7.4 of the FOS Terms of Reference provides that FOS may allow or require "another Financial Services Provider" to be joined, with "Financial Services Provider" defined in article 20.1 as "a provider of a Financial Service that is a Member".
[19] *Superannuation (Resolution of Complaints) Act 1993* (S(ROC) Act 1993), section 18
[20] S*uperannuation (Resolution of Complaints) Act 1993*, sections 18, 24A

1.1.5 Remedies must be appropriate given fiduciary obligations to other members

As noted above, superannuation is unique among financial products and services because the fund trustee is subject to a number of fiduciary duties stemming from trust law, as well as to legislative obligations.

One of those fiduciary duties, which has been codified into the superannuation legislation, is the duty to act in the best interests of all members of the fund[21]. In essence, this means that a trustee must consider not only the interests of a particular member, but the membership as a whole. The trustee must also act fairly in dealing with classes of beneficiaries and in dealing with beneficiaries within a class[22].

These duties influence the remedies that are appropriate for a superannuation fund trustee to apply to resolve a complaint from a member or beneficiary, particularly given the 'profit for members' nature of many superannuation funds.

Where a *financial* loss has been suffered as a result of a trustee's decision, action, or failure to act, it is appropriate for that loss to be fully rectified. However, consideration of a greater level of compensation, or compensation for *non-financial* loss such as pain and suffering, raises a number of important issues.

Some losses may, due to the nature of the underlying incident, be covered by an insurance policy held by the trustee. Some other losses, due to the action or inaction of a third party provider to the trustee, such as a fund administrator, may lead to payment of contractual remedies to the trustee. However, there will be some losses for which such remedies or insurance are not available, and the trustee will need to rectify the impacted member out of whatever monies are available to it.

Many funds operate under a 'profit for members' model, with the trustee holding little or no monies of its own. In such cases, the rectification of the member who has suffered loss will come at the direct expense of other members of the fund, through a reduction in the earnings that would otherwise be credited, or an increase in the administration fees that must be charged. To the extent that the losses being compensated involve subjective, non-financial components, ASFA is of the view this is inconsistent with the trustee's fiduciary duties to its membership as a whole.

It is also important to acknowledge that the potential exposure of trustees of APRA-regulated superannuation funds to additional categories of compensation may impact on the availability and cost of professional indemnity insurance, as well as the funding of the 'operational risk financial requirement' that trustees are required, under the *SIS Act 1993*, to maintain[23]. For the many funds which are 'profit for members' in nature, these costs will effectively be funded by all members/beneficiaries through higher fees or a reduction in the earnings credited.

We note that the SCT currently will withdraw a complaint as lacking in substance[24] if the complainant is unable to point to a direct financial loss. We submit that this is the appropriate outcome, given the fiduciary nature of superannuation. ASFA does not support extending the scope of potential remedies to include compensation for non-financial loss.

[21] *Superannuation Industry (Supervision) Act 1993*, subsection 52(2)(c)
[22] *Superannuation Industry (Supervision) Act 1993*, subsection 52(2)(e) and (f)
[23] *Superannuation Industry (Supervision)* Act 1993, subsection 52(8)(b)
[24] In reliance on the power in *Superannuation (Resolution of Complaints) Act 1993*, subsection 22(3)(b)

1.1.6 A contract-based scheme is not workable for contested death benefits

In a membership-based EDR scheme, a complainant who accepts a decision of the scheme is effectively required to agree to it, to create the legal arrangement that makes the decision enforceable as a contract.

Such an approach may be effective for disputes involving financial products or services where there is only a single complainant involved, as there are no competing interests which may prevent agreement. However, it will not be a workable solution for contested superannuation death benefit distributions, which comprise a substantial proportion of the complaints which proceed to the determination stage before the SCT – 32 per cent of the complaints within jurisdiction for the SCT in the 2015-16 year[25].

Superannuation law contains a broad definition of those individuals who may be considered to have been 'dependant' on a deceased fund member, and therefore potentially eligible to receive part or all of their death benefit. This includes a 'spouse' or 'child' of the member, and any person with whom the member was in an 'interdependency relationship'[26]. As family relationships have increased in complexity, there has been a corresponding increase in the incidence of death benefit disputes involving current and former spouses and multiple children – often including adult children from a previous relationship disputing the trustee's proposed distribution in favour of younger children from a more recent relationship.

The extensive 'claim-staking' process set out in the *S(ROC) Act 1993*[27] provides trustees with a level of certainty that the claims of all potential beneficiaries have been identified and assessed - a complaint regarding a proposed death benefit distribution may be made to the trustee and then potentially to the SCT, but once any such challenges have been addressed the trustee can proceed to pay the benefit without fear that another person may come forward with a stronger claim. Without the protection of the claim-staking process, trustees would be faced with a choice between conducting ever more extensive inquiries and delaying payment of the benefit, or taking the risk that another claimant may come forward after payment has been made. Given the 'profit for members' nature of many superannuation funds, any additional payment that may be required to such a claimant would impact other members/beneficiaries (for example, by reducing the pool of fund earnings available to be allocated amongst all members or reducing any existing reserves).

The prospect of a contract-based EDR scheme introduces a further complication for death benefit distributions. There would be a need for all complainants to agree to the decision made by the scheme before it could be acted upon by the trustee. That is, as well as receiving endorsement from the successful complainants, it would be necessary for the *unsuccessful* complainants to also give their agreement to the decision. While unfortunate, the reality observed by ASFA members is that the unsuccessful complainants in a death benefit dispute are no more likely to agree with the decision of the SCT than with the decision of the trustee.

Under the SCT model currently, an unsuccessful complainant must consider whether grounds exist to make an appeal to the Federal Court on a question of law. A time limit applies for lodging an appeal, after which the trustee is free to pay the death benefit to the successful complainant.

[25] SCT, Annual Report 2015-16, p22
[26] *Superannuation Industry (Supervision) Act 1993*, section 10
[27] *Superannuation (Resolution of Complaints*) Act 1993, sub-section 15(2)

Under the proposed contract-based Superannuation Ombudsman, there is a risk that an unsuccessful complainant will fail to give their agreement to the Ombudsman's decision and thereby prevent it taking effect. This would place the trustee in the invidious position of having to withhold payment to the successful complainant, or risk making the payment and exposing itself (and the assets of the fund held in trust for the membership as a whole) to legal action by the unsuccessful complainant. ASFA understands that very few matters relating to superannuation death benefits currently make their way before the courts, instead being addressed at IDR stage or by the SCT, however we anticipate that this could become a common occurrence under the proposed Superannuation Ombudsman scheme.

1.1.7 Direct right of appeal is vital

Where any party to a complaint disagrees with a determination of the SCT, that party has the right to appeal directly to the Federal Court on a question of law[28].

Such an appeal can involve considerable cost and we accept it may not be a realistic option for all consumers who are dissatisfied with a determination of the SCT, yet it remains a valuable right and must, in ASFA's view, be retained.

Given the trustee's fiduciary obligation to act in the interests of all members, it is also critical that trustees retain the ability to appeal a determination which they consider to be incorrect, especially where the matter under determination is of wider application and may impact upon the future payment of benefits by the trustee.

In addition to the right of parties to appeal to the Federal Court, the SCT may, on its own initiative or on the request of a party, refer a question of law arising in relation to a complaint to the Court for decision[29]. As decisions of a Commonwealth court, Federal Court judgments are precedential, providing valuable guidance to trustees and other superannuation industry stakeholders – including the government – on application of the superannuation law.

As the SCT is a statutory body, some of its "jurisdictional" decisions (such as the decision to withdraw a complaint) can also be judicially reviewed on the limited grounds detailed in the *Administrative Decisions Judicial Review Act 1977*[30].

Taken as a whole, ASFA considers the rights of appeal and jurisdictional review strike an appropriate balance – they provide a necessary level of accountability and scrutiny of the SCTs decisions, while ensuring that the overwhelming majority of superannuation related complaints are resolved outside the court system and at no cost to the consumer.

In contrast, if an applicant accepts a FOS determination, it automatically becomes binding on both parties – there is no further appeal or review process within the FOS model.

Where a financial services provider disagrees with a FOS determination, it is possible to challenge it in the state court system, however the grounds to do so are limited. These include that:

- the decision was not made in good faith
- the decision was the product of bias or dishonesty
- the Ombudsman misconceived the task they were required to undertake
- the decision was not made in accordance with the terms of the contract regulating the process (primarily, the FOS Terms of Reference)[31].

[28] *Superannuation (Resolution of Complaints) Act 1993*, section 46
[29] *Superannuation (Resolution of Complaints) Act*, section 39
[30] Marita Wall, *Resolving the Issue*, Superfunds, August 2014
[31] Marita Wall, *Resolving the Issue*, Superfunds, August 2014

Many legal practitioners take the view that it may be extremely difficult to make out a successful case on these grounds. For example, comments include:

- "Given that the powers given to FOS under the Terms of Reference are broad and discretionary, it is difficult to conceive of a misapplication of the Terms of Reference that would be sufficient to ground a breach of contract that would justify overturning a FOS decision"[32]
- "No FOS determination has ever been successfully overturned by a court" for breach of contract[33].

Some state courts have held that decisions of the FOS predecessor entity were subject to judicial review, following English case law which suggested that judicial review may extend to decisions made by a private organisation in certain circumstances, essentially where that private organisation is in effect performing public law duties. However, the currently accepted position, set out in a 2012 decision of the Victorian Supreme Court[34], appears to be that decisions of FOS are not subject to judicial review. This is because FOS exercises only private law functions, and the fact that FOS was created to fulfil a statutory purpose is insufficient to support the conclusion that FOS operated in a public law context[35].

The limited ability of a financial services provider to challenge a determination of an industry ombudsman scheme such as FOS is, in ASFA's view, inconsistent with the fiduciary obligations owed by the trustee to the members/beneficiaries as a whole.

1.2 The test is not tied to the model, but is appropriate for superannuation

Draft finding 12(b): SCT is hampered by restrictive legislation which contains a narrow definition of fair and reasonable in comparison to industry ombudsman schemes.

ASFA notes that the test to be applied by the SCT in conducting EDR is prescribed in the *S(ROC) Act 1993* and should be seen as a feature of that legislation, not as an inherent attribute of the tribunal model. The test could, if considered desirable, be changed by legislative amendment. It is not necessary to transition to an ombudsman scheme in order to change the EDR test for superannuation.

Having said that, it is not clear to ASFA that the current SCT test is as deficient as claimed.

Draft finding 12(b) asserts that the 'narrow' test, used in the current 'restrictive' governing legislation, has 'hampered' the SCT – as such, it appears to be suggesting that the test is the cause of the perceived lack of flexibility in the SCT's operations.

ASFA does not agree that this is the case. As set out in our response to the issues paper, and re-stated in this submission, the primary cause of any lack of flexibility is the inadequate funding and resourcing provided to the SCT over a long period. The lack of operational accountability and autonomy may also be a contributing factor. However, the current test is, in ASFA's view, extremely flexible. It allows the SCT to consider all trustee decisions (with some specific exceptions) and has not required change despite major evolution in the superannuation environment and product offerings.

[32] Duncan Marckwald, Corrs Chambers Westgarth, *Challenging FOS decisions – and how to avoid the need to do so*, 11 September 2015
[33] Marita Wall, Greenfields, *A financial, credit and investment disputes ombudsman*, 7 December 2016
[34] *Mickovski v Financial Ombudsman Service* [2012] VSCA 185
[35] See, for example, Lander & Rogers, *Financial Ombudsman Service Update – review of FOS decisions*, 31 August 2012

The Interim Report notes that:

> *Like the industry ombudsman schemes, SCT should be able to permit broader considerations to inform decision making, using 'fairness in all the circumstances' and there should also be flexibility to take into account more than the legislation, such as industry codes.*[36]

ASFA notes that the SCT can already, under its current test, "take into account more than the legislation". In reviewing a decision, the SCT effectively stands in the shoes of the trustee. It has all the powers, obligations and discretions conferred on the trustee[37]. The SCT must not do anything that would be contrary to law, the fund's governing rules or the terms of any contract of insurance (if relevant)[38], but this should not be interpreted as meaning the trustee can *only* take into account legal considerations. To the extent that a trustee is required, to discharge its fiduciary obligations, to take into account any statements of industry best practice – or, should they exist, codes of practice – so too would the tribunal be required to consider them when reviewing the trustee's decision.

The scope of the SCT's power under the current test - to rectify any unfairness and unreasonableness, reflects the fiduciary nature of the trustee's obligations (and those of the SCT, standing in the trustee's shoes):

- the trustee is required, in making a decision on a matter, to consider what is fair and reasonable to the particular complainant, and also what is fair and reasonable to the membership as a whole
- it is recognised that there may be a range of possible outcomes resulting from a trustee decision made following due process - there is no single 'correct' or 'preferable' outcome[39] – and "even if the Tribunal's factual findings differed from those of the previous decision-maker, the Tribunal might nonetheless be satisfied that, in the circumstances, the decision under review was in fact fair and reasonable in the relevant way"[40]
- the SCT must affirm the decision if satisfied that the decision, in its operation in relation to the complainant (and, in a death benefit matter, another party to the complaint who has an interest in the death benefit) "was fair and reasonable in the circumstances"[41]. ASFA understands that the requirement that the SCT affirm a decision in these circumstances may have led to a perception that the SCT process is more favourable to trustees. This is not the case, it simply reflects (as noted immediately above) that there is no single 'correct' decision and if the trustee's decision was one of a range of fair and reasonable decisions, it should not be overturned
- If not satisfied that the decision was fair and reasonable, the SCT may exercise its determination making power to remit the matter to the decision-maker, vary the decision, or set it aside and substitute its own decision
- to do more than fully rectify a complainant would risk causing detriment to other members/beneficiaries. It would not be 'reasonable', and would be inconsistent with a model based on fiduciary obligations. As a result, the SCT's determination making power may only be exercised for the purpose of placing the complainant "as nearly as practicable in such a position that the unfairness, unreasonableness, or both, that the Tribunal has determined to exist in relation to the trustee' decision … no longer exists"[42].

[36] EDR Review Interim Report, p125
[37] *Superannuation (Resolution of Complaints) Act 1993*, subsection 37(1)
[38] *Superannuation (Resolution of Complaints) Act 1993*, subsection 37(5)
[39] Jevtovic; *Cameron v Board of Trustees of the State Public Sector Superannuation Scheme* [2003] FCAFC 214
[40] *Board of Trustees of the State Public Sector Superannuation Scheme v Edington* [2011] FCAFC 8
[41] *Superannuation (Resolution of Complaints) Act 1993*, sections 37 – 37C
[42] *Superannuation (Resolution of Complaints) Act 1993*, subsection 37(4)

ASFA considers the latter to be appropriate given the trust context and the fiduciary obligations owed by the trustee (and the SCT, standing in the trustee's shoes) not only to the particular complainant, but to the members/beneficiaries as a whole.

1.3 Changes to governance would deliver key improvements

Draft finding 11:

a) SCT governance arrangements are in need of modernisation. The current situation, with the Chairperson performing a dual role as a CEO as well as Chair of the Tribunal and lacking financial delegations, has resulted in a misalignment of accountability and powers and does not align with good public sector practice.

b) There is a lack of direct input by consumer and industry experts in the governance of SCT.

c) The current appointments process for Tribunal members can be lengthy making it more difficult for SCT to manage its operations and to quickly respond to emerging issues.

Draft finding 14(a): The governance model of industry ombudsman schemes, with even numbers of directors with industry and consumer expertise and an independent chair, assists in ensuring that schemes can operate independently of industry, despite being industry funded.

While ASFA agrees that the governance model outlined in draft finding 14(a) delivers independence, it should not be inferred from this that the current SCT model lacks independence. The Interim Report itself acknowledges that the strengths of the SCT, as identified in the submissions on the issues paper, include that it has "actual and perceived independence derived from government"[43].

While change is not necessary for the purpose of independence, ASFA concurs with each of the points outlined as part of draft finding 11 for modernisation of the SCT's governance model. However, we are of the view that each can readily be addressed whilst retaining the statutory tribunal structure of the current SCT. No part of draft finding 11 is so significant that it justifies setting aside the tribunal model.

In particular, we recommend changes to the governance arrangements as follows:

- the government should retain power of appointment of the Chair/CEO (however described)
- a governing board should be appointed, comprising representatives from industry and consumer bodies
- the board should have accountability and responsibility for the operation of the tribunal
- the power to appoint suitably qualified and experienced individuals to hear and resolve complaints should also rest with the board, without the need for ministerial appointment.

The advantages of this modified governance structure is that the board would have full control over how the tribunal operates – including sufficient operational autonomy for it to be flexible and adaptable.

The Interim Report notes that:

> As SCT does not have a corporate legal identity, in practice, this means that ASIC enters into all contracts on behalf of SCT and makes all payments, including staff salaries, payments to tribunal members, third party providers or to ASIC (for rent and corporate services ASIC provides). Staff of SCT are ASIC employees, employed under the ASIC Enterprise Agreement and SCT is co-located in ASIC's Melbourne office.[44]

[43] EDR Review Interim Report, p13; see also p17
[44] EDR Review Interim Report, p

This lack of autonomy, and the heavy reliance on ASIC, has had many negative impacts, not least on governance and accountability. However, while the Interim Report appears to accept this as an inevitable consequence of the statutory tribunal model, it is not clear that this is the case.

ASFA would question whether it is not possible to amend the *S(ROC) Act 1993* to establish the Tribunal as a legally autonomous body, capable of directly employing staff and handling its own funding allocation. We note that the Administrative Appeals Tribunal[45], for example, is empowered to employ staff under the *Public Service Act 1999* and has the ability to administer its own financial affairs.

1.4 Funding must be certain, adequate and transparent

Draft finding 8:

b) SCT funding has been steadily decreasing with current resourcing levels neither sufficient nor sustainable.

c) There is a lack of transparency of current funding and budget arrangements.

Draft finding 14(b): Where EDR schemes have sufficient funding flexibility, it allows them to respond quickly to changes, such as an increase in the number of disputes received.

It is essential, in ASFA's view, that the SCT receives a funding injection sufficient to enable it to increase its resourcing and implement the new processes necessary to return it to efficient operation.

While we welcome the recent provision of $5.2 million in additional funding, awarded in the 2016/17 Budget, we note that this money was primarily earmarked for reducing the SCT's existing backlog and while it is also to be used to improve internal processes, it will not be sufficient to effect the material change that is required. It is also extremely premature to be making any judgments about the impacts this funding has had on the SCT's performance – while announced in May 2016, the appropriations process is such that the funding was only quite recently made available to ASIC for disbursement on the SCT's behalf.

Given the importance of an effective EDR mechanism in preserving confidence in superannuation and the significant costs that would be involved in implementing the proposed Superannuation Ombudsman scheme in place of the Tribunal, we consider it appropriate that the industry should contribute toward funding the current shortfall.

In addition to the matter of funding the backlog and necessary reforms to the SCT, there is a need to implement a sustainable model for the Tribunal's ongoing funding.

As outlined in our response to the issues paper, given the SCT is the complaints handling body for all APRA-regulated funds, we are comfortable with its funding continuing to be collected by APRA via the annual supervisory levy process. We see little merit in incorporating the funding collection in the new ASIC levy (to take effect from the 2017/18 financial year) or introducing an entirely new administrative process.

However, it is essential that a new formula is implemented for determining the amount of funding to be allocated for the SCT's purposes – the funding should not simply be added into the current levy components. In particular, ASFA considers that:

- the annual supervisory levy should include a new component specifically attributable to funding the SCT
- the new SCT levy component should include an element, potentially quite significant, that is directly referable to its projected complaints volumes

[45] Constituted under the *Administrative Appeals Tribunal Act 1975*

- consideration could be given to introducing a user-pays element to the component, with a view to incentivising trustees to resolve complaints at the IDR stage where possible
- the SCT's projected funding needs should be specifically detailed in the discussion paper released by APRA and Treasury each year as part of the process for setting the supervisory levy, with any variance between the proposal and the final funding allocation explained in the explanatory documents accompanying the levy determination and any Cost Recovery Implementation Statement published by APRA. This is essential to provide transparency over the amount actually allocated to the SCT, which has been absent for some years
- the allocation of funding to the SCT should not be impacted by any fiscal constraints imposed on APRA or ASIC, such as periodic efficiency dividends
- the necessary governance changes should be made to enable the SCT to have direct control over its funding allocation (see 1.3 above)
- the SCT's utilisation of its funding should be audited and detailed reporting provided in its annual report.

1.5 Accountability can and should be enhanced

Draft recommendation 6: Ensuring schemes are accountable to their users

Both new schemes should be required to meet the standards developed and set by ASIC.

At a minimum, ASIC's regulatory guidance should require the schemes to:

- ensure they have sufficient funding and flexible processes to allow them to deal with unforeseen events in the system, such as an increase in complaints following a financial crisis or natural disaster
- provide an appropriate level of financial transparency to ensure they remain accountable to users and the wider public
- be subject to more frequent, periodic independent reviews and provide detailed responses in relation to recommendations of independent reviews, including updates on the implementation of actions taken in response to the reviews and a detailed explanation when a recommendation of an independent review is not accepted by the scheme
- establish an independent assessor to review the handling of complaints by the scheme but not to review the outcome of individual disputes. In addition, ASIC's regulatory guidance should require the new scheme for financial, credit and investment disputes to regularly review and update its monetary limits and compensation caps so that they remain relevant and fit-for-purpose over time.

Draft finding 9(b): Transparency and accountability of operations is important for efficiency and performance and is currently lacking.

Draft finding 15: Regular independent reviews of an EDR scheme's performance and procedures are an important feedback and accountability mechanism to ensure they continue to evolve and improve. Independent Assessors have the ability to promote scheme accountability and improve scheme decision making processes.

While disagreeing that the SCT should be replaced with the proposed Superannuation Ombudsman, ASFA agrees that all financial services EDR arrangements should meet a set of standardised minimum standards.

The measures suggested as part of draft recommendation 6 appear, in ASFA's view, to be an appropriate starting point. However, any such standards should be subject to a separate consultation process prior to their implementation, to ensure the end product is optimised to achieve accountability and transparency over the schemes' operations, comparability between the outcomes of individual schemes over time and between schemes, and improved consumer confidence.

ASFA agrees with draft finding 9(b) regarding a need to improve transparency and accountability of the SCT's operations.

In our response to the Review Panel's issues paper, we specifically noted the absence of any regular, independent review of the SCT and recommended that a formal review process be implemented. We consider that the use of an independent assessor, as proposed in draft finding 15, would be an appropriate component of a package of measures to improve accountability of the SCT, such as reforms to the SCT's governance structure (see 1.3 above) and funding arrangements (see 1.4 above). When taken as a package, these measures should provide the increase in transparency and accountability needed to ensure the revamped SCT remains on track to deliver effective outcomes for all stakeholders.

1.6 A service model can be adopted, regardless of the structure

Draft finding 8(a): The delays experienced at SCT, particularly in relation to TPD and death benefits complaints, are unacceptable and have serious implications for the effectiveness of SCT as a dispute resolution forum.

Draft finding 9(a): The legislative prescriptions on how SCT is currently permitted to handle complaints inhibit its ability to choose the most appropriate dispute resolution mechanism.

Draft finding 10(a): Compared to industry ombudsman schemes, SCT is restricted in its ability to adapt and reform itself to address issues and future challenges because it requires involvement by government and legislative change.

Draft finding 10(b): SCT can improve its stakeholder education and outreach activities.

Draft finding 12(a): Consumers can find it difficult to access and navigate SCT.

ASFA agrees that the current service issues at the SCT, in particular the significant delays in resolution of complaints, are simply unacceptable. However, while unfortunate, it must be acknowledged that they are inevitable given the Tribunal has, almost since its inception, been inadequately funded and resourced. **The issues are not, in our view, a consequence of the complaints model adopted, so much as the execution of that model**.

ASFA agrees that a service-oriented model would bring benefits in resolving superannuation complaints more efficiently and improving consumer confidence in the process. However, **there is no reason why a service model cannot be adopted within the statutory tribunal model**.

As noted in our response to the issues paper, the SCT already has significant capacity to adopt more flexible processes, and ASFA welcomes recent initiatives implemented by the SCT to deliver a more consumer-friendly experience, for example:

- we understand that a streamlined process was adopted in November 2016 for complaints where the only issue in dispute is the distribution of a death benefit, involving a limited investigation followed by early conciliation
- according to the SCT's 2015/16 Annual Report the introduction of process improvements saw an increase in efficiency during that year. In particular, efficiency gains resulted in the average number of complaints finalised per member of staff rising to 70.4, compared with the five year average of 60[46].

The *S(ROC) Act 1993* contains relatively little prescription as to the processes that must be adopted, however it appears that even a modest amount of prescription has had the unfortunate outcome of overly constraining the Tribunal's operations.

[46] Superannuation Complaints Tribunal, Annual Report 2015/16, p3

While ASFA considers some aspects of the industry ombudsman schemes to be inappropriate for superannuation, we readily acknowledge the process efficiencies these schemes have been able to realise and their service-oriented approach. While some legislative change would be required in order to allow adoption of similar processes by the SCT, the potential benefits to customer service would in ASFA's view be significant. In particular, we recommend that further consideration be given to initiatives such as:

- providing an exception to the requirement that the Tribunal must attempt conciliation in all cases

  Where a complaint is of relatively low value but was not successfully resolved at the IDR stage, it is likely that it involves either a fundamental disagreement as to the facts or a perceived matter of principle. In either case, it is questionable whether forced conciliation will deliver an outcome. Proceeding straight to a review may, in such cases, be the more efficient approach.
- implementing a 'fast-track' process similar to that adopted by FOS to expedite handling of low-value complaints and less complex cases

  For simple and low-value complaints, FOS has adopted a fast-track process which involves an adjudicator early in the process. The adjudicator reviews the information, tries to resolve the dispute via telephone conferences (either jointly or separately with each party), provides a preliminary view and then, if required, makes a determination. We see merit in exploring a similar process for low-value superannuation complaints.

While more and faster progress is clearly required, we are of the view that the statutory tribunal structure is not an insurmountable barrier to this. We are confident that significant process efficiencies could be achieved with appropriate funding and resourcing, and relatively modest amendments to the Tribunal's governing legislation.

Similarly, ASFA agrees with the criticisms in the Interim Report regarding the limited stakeholder education and outreach activities undertaken by the SCT – in fact, our response to the issues paper highlighted these concerns. However, the capacity to increase stakeholder education and outreach will flow naturally from increased funding and resourcing, and more service-oriented operating processes. The statutory tribunal structure is not, of itself, a barrier to stakeholder education or outreach.

ASFA agrees that the SCT's consumer interface could be greatly improved, and our submission in response to the issues paper made suggestions to this effect. That submission also acknowledged the impact that delays in resolving – or indeed progressing - complaints has on consumers, and the need for the SCT to do more to assist vulnerable consumers and those who may have language issues. Each of these issues could be readily addressed, given adequate funding and resourcing.

That aside, we are concerned that some of the comments in the Interim Report about the consumer experience may be attributable to a perception and perhaps an expectation that the SCT, being a tribunal, will be difficult to access and navigate. It is not clear that any formal consumer testing has been done to support these claims.

ASFA expects that that the consumer experience is also detrimentally influenced by the current website - which resembles that of a government department much more than that of say the FOS or CIO - and the inefficient and overstretched service model. It is interesting to speculate whether a typical consumer, presented with a revamped and adequately funded and resourced SCT, operating with an improved and more consumer-friendly interface and service model, would truly appreciate that they are dealing with a 'tribunal'. ASFA suspects that many – or indeed most – would not, at least not until such time as the particular protections afforded by that operating structure (enforceability, rights of appeal) became relevant.

While we note the assertion in the Interim Report that the SCT is very legalistic and specifically that it involves a high level of legal representation[47], ASFA understands that the level of legal representation is in fact comparable for all the current EDR schemes. It is also worth noting that that the highest level of legal representation observed before the SCT relates to contested death benefit distributions - which frequently involve a level of interpersonal conflict - rather than those complaints which might be expected to be more factually and legally complex (such as insurance related claims and those involving defined benefits).

2. Other matters

2.1 Increased ASIC oversight

Draft recommendation 7: Increased ASIC oversight of industry ombudsman schemes

ASIC's oversight powers in relation to industry ombudsman schemes should be enhanced by providing ASIC with more specific powers to allow it to compel performance where the schemes do not comply with EDR benchmarks.

Draft finding 17: ASIC's limited oversight powers do not allow it to take targeted action to address problems within a scheme.

Information request 5: *On what matters should ASIC have the power to give directions? For example, should ASIC be able to give directions in relation to governance and funding arrangements and monetary limits?*

The Interim Report notes that ASIC's current powers of oversight in relation to the industry-based EDR schemes are "limited". While the Interim Report recommends that these powers be enhanced, little detail is given as to what is envisaged – although it can be inferred from information request 5 that it may include the ability to give directions to an EDR scheme operator.

In particular, the Interim Report notes that:

> "While ASIC's policy guidance sets out the EDR benchmarks that schemes are required to meet, ASIC's oversight role has not extended to compelling scheme performance on specific operational matters or an active involvement in the resolution of individual disputes"[48].

It is not clear to ASFA that it is appropriate for ASIC to have an "active involvement in the resolution of individual disputes", with the exception of satisfying itself that the EDR scheme is conducting itself appropriately and in accordance with its Terms of Reference and any relevant legislative requirements. ASIC is a regulator, not an adjudicator.

The Interim Report further notes that:

> *"in circumstances where an approved industry EDR scheme fails to meet one of the approval criteria in ASIC Regulatory Guide 139, ASIC's powers are limited to either varying the approval, for example by imposing a condition, or revoking the approval… These limited powers mean ASIC is unable to take appropriate action to address a specific problem with a scheme and continue to ensure that scheme users are provided with effective outcomes."*[49]

[47] EDR Review Interim Report, p117 and 124
[48] EDR Review Interim Report, p133
[49] EDR Review Interim Report, p133

To the extent that ASIC's additional oversight powers are limited to ensuring compliance by schemes with a suite of EDR benchmarks set out in regulatory material, ASFA is not opposed to this recommendation. It will, however, be necessary to ensure that any such benchmarks are carefully developed as part of a consultation process with stakeholders, and that the consequences of non-compliance are appropriate and measured, to minimise any potential impact on consumers and financial services providers.

ASIC currently has no formal oversight role of the SCT[50] but – as acknowledged in the Interim Report[51], the SCT is subject to oversight from a number of sources:

- the SCT's jurisdiction, powers and operations are open to judicial scrutiny by way of an appeal to the Federal Court on a question of law and judicial review (refer 1.1.7 above for discussion of why this is critical)
- complaints relating to the SCT are currently – and ASFA recommends that they should continue to be – subject to investigation by the Commonwealth Ombudsman. The Interim Report notes that complaints in relation to the SCT have decreased over the last five years (with only four complaints in 2015-16), and no administrative deficiency has been found in any complaint lodged with the Ombudsman to date[52].
- the SCT's operations are also scrutinised by Parliament, including through the formal tabling of the annual report.

In addition, the Interim Report recommends[53] – and ASFA does not oppose – the appointment of an independent assessor to investigate complaints by users into the handling of a dispute by the schemes.

In this context, it is not immediately clear what value would be added by imposing another layer of oversight of the SCT.

However, to the extent that a set of EDR benchmarks is developed by ASIC for EDR schemes, and these extend to the SCT as well as to the proposed Financial, Credit and Investments Ombudsman, it would not be inappropriate for ASIC to have oversight of compliance with those benchmarks.

2.2 Use of panels

Draft recommendation 8: Use of panels

The new industry ombudsman schemes should consider the use of panels for resolving complex disputes. Users should be provided with enhanced information regarding under what circumstances the schemes will use a panel to resolve a dispute.

Draft finding 16:

- Panels play an important role in resolving complex disputes, however, they do impose costs on the system.
- There is currently a lack of transparency around when a panel will be used.

The Interim Report expresses a clear preference for a higher use of panels in resolving complaints. Historically, the SCT resolved more complaints using panels than individual members than it does currently, and it appears that the move to more single member determinations has been driven by fiscal constraints more than anything else.

[50] EDR Review Interim Report, p50
[51] EDR Review Interim Report, p93
[52] EDR Review Interim Report, p93
[53] EDR Review Interim Report, draft recommendation 6; refer also section 1.5 in this submission

While not opposed to the use of panels, ASFA notes that their value in superannuation related complaints stems from the access they provide to relevant expertise, for example through the use of actuarial or medical experts in appropriate cases. In contrast, the draft recommendation appears to propose the use of panels whose membership is representative of industry and consumers, and not necessarily aligned to the expertise that may be relevant or necessary to resolving complaints on a case by case basis.

ASFA agrees that there should be a level of transparency around when a panel may be used. This should include a general outline provided both on the websites of EDR schemes and as part of the acknowledgement of receipt of a complaint/dispute, with more specific and detailed information provided to the parties when use of a panel is proposed.

2.3 Varying time limits

The Interim Report suggests that the terms of reference for the proposed Superannuation Ombudsman "could provide [the] scheme with flexibility to extend time limits for disability and death benefits complaints in exceptional circumstances"[54].

Currently, consumers are required to lodge complaints about disability and death benefits with the SCT within specific time limits, with the SCT unable to hear complaints that have been lodged out of time[55]. In particular:

- For a claim relating to payment of a total and permanent disablement (TPD) benefit:
  - If the person permanently ceased employment because of the physical or mental condition that gave rise to the claim for the TPD benefit – the claim for the benefit must have been made to the trustee within 2 years of the person permanently ceasing employment, and the complaint must be made to the SCT within 4 years of the trustee's decision
  - if the person did not permanently cease employment because of the physical or mental condition that gave rise to the claim for the TPD benefit – the complaint must be made to the SCT within 6 years after the making of the trustee's decision[56]
- If a person was advised of the 28 day prescribed period within which they must lodge a complaint regarding a trustee's decision in relation to a person's objection to payment of a death benefit – the complaint must be made to the SCT within 28 days[57] (this time limit would not apply in the event that a trustee failed to advise a period within which the complaint must be lodged with the SCT).

These time limits provide certainty to the trustee that the complaint is closed once the relevant time period has elapsed. This gives the trustee operational certainty and, in the case of death benefit distributions, allows the trustee to pay the benefit in accordance with its distribution decision, without fear that the unsuccessful applicant may take action for incorrect payment.

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[54] EDR Review Interim Report, p152

[55] Some other time limits also apply. For example, if a trustee has given a person a copy of the contributions report it has made to the ATO and advised that the person has 12 months to make a complaint to the SCT, any complaint relating to that report must be lodged within that time (*Superannuation (Resolution of Complaints) Act 1993*, subsection 15CA, *Superannuation (Resolution of Complaints) Regulations 1994*, regulation 5A). In addition, the SCT has a discretion not to deal with a complaint if the decision or conduct complained about is more than 12 months old (*Superannuation (Resolution of Complaints)) Act 1993*, subsection 22(3)(a)).

[56] *Superannuation (Resolution of Complaints)) Act 1993*, subsection 14(6A), (6B). Note that these time limits apply in respect of decisions made from 1 July 2013

[57] *Superannuation (Resolution of Complaints) Act 1993*, section 14(3) and (4), *Superannuation (Resolution of Complaints) Regulations 1994*, regulation 5

If the proposed Superannuation Ombudsman (or, for that matter, a revamped SCT) to "extend time limits for disability and death benefits complaints in exceptional circumstances" has the potential to reduce operational certainty for trustees. In ASFA's view, it would be critical to publish clear guidelines specifying the types of 'exceptional circumstances' in which the discretion could be exercised, and setting an endpoint beyond which the discretion will not apply. Even with such guidelines, ASFA is concerned that the discretion may cause trustees to defer making any payment, in contested disability and death benefit matters, until they feel they have an adequate level of certainty that their payment will not be further challenged.

2.4 Addressing systemic issues

Draft finding 13:

Although it can refer issues to regulators, a shortcoming is that SCT is not required to resolve systemic issues relating to complaints handling.

As noted in the Interim Report, the SCT is not currently required to resolve systemic issues relating to complaints handling. The governing legislation does, however, require the Tribunal to notify APRA and/or ASIC on a case-by-case basis where it becomes aware that "a contravention of any law or of the governing rules of the fund may have occurred"[58], or a breach in the terms and conditions relating to an annuity policy, a life policy or a retirement savings account[59]. This reflects the view that such matters are best investigated and addressed by the relevant regulator.

Investigating and addressing systemic issues would represent a significant increase in the scope of the SCT's role. ASFA queries whether it would not usurp the role and responsibilities of the regulator, which is in a position to issue updated regulatory requirements and/or guidance where issues of general (systemic) application come to light. ASFA would, however, endorse a requirement on the SCT to more closely monitor the trends and themes that may be emerging in complaints before it, and to provide early notification of such matters to the regulator(s).

Either proposal – to investigate and resolve systemic issues, or alternatively to monitor and report on emerging issues - would have some resourcing impacts, which would need to be addressed as part of the overall package of reforms discussed in this submission. There is, in ASFA's view, nothing in the tribunal structure which necessarily prevents the Government pursuing amendments to the SCT's governing legislation to require it to undertake either role, if considered appropriate.

[58] *Superannuation (Resolution of Complaints) Act 1993*, section 64
[59] *Superannuation (Resolution of Complaints) Act 1993*, section 64A

2.5 Internal dispute resolution

Draft recommendation 9: Internal dispute resolution

Financial firms should be required to publish information and report to ASIC on their IDR activity and the outcomes consumers receive in relation to IDR complaints. ASIC should have the power to determine the content and format of IDR reporting.

Draft recommendation 10: Schemes to monitor IDR

Schemes should register and track the progress of complaints referred back to IDR.

Draft finding 18:

- Effective EDR is supported by effective IDR.
- Data on IDR outcomes is limited and inconsistent and this means that it is difficult to determine how effective internal dispute resolution currently is and whether it is improving over time.
- Tracking by EDR bodies of disputes referred back to IDR is an important element of the framework and could assist in encouraging firms to reach a solution or identify systemic issues in IDR.

Information request 6:

- *What IDR metrics should financial firms be required to report on?*
- *Should ASIC publish details of non-compliance or poor performance IDR, including identifying financial firms?*

ASFA concurs with the finding that effective internal dispute resolution (IDR) mechanisms are essential to support effective EDR.

IDR processes for trustees of APRA-regulated superannuation funds are governed by section 101 of the *SIS Act 1993* and provisions of the *Corporations Act 2001* and *Corporations Regulations 2001*. To monitor their compliance with these provisions, superannuation trustees, as a matter of course, track the progress of disputes subject to IDR.

However, as there is currently no requirement for trustees (or other financial services providers) to report on their IDR processes and outcomes, it is to be expected that the data generated during the monitoring process will vary between providers and there will be little consistency or comparability.

APRA is of the view that it would not be inappropriate to require financial services providers, including superannuation trustees, to report some level of data to ASIC. However, we note the following:

- careful consideration would be needed to ensure the content of any reporting is appropriately formulated to ensure consistency and true comparability. For example, it would be necessary to ensure that all providers are required to report using consistent definitions of 'complaint' or 'dispute', as relevant
- it would be necessary to avoid drawing comparisons between different types of providers that are subject to different requirements – for example, trustees of APRA-regulated superannuation funds should not be compared to other types of providers that are not subject to the requirements in section 101 of the *SIS Act 1993*
- there is no existing mechanism for superannuation trustees to provide data to ASIC on a regular basis, however APRA collects some data on behalf of ASIC through its framework of quarterly, annual and ad hoc returns, lodged electronically via the Direct-to-APRA (D2A) system. This mechanism should also be utilised, in ASFA's view, for any reporting obligations imposed on superannuation trustees in relation to IDR

- It would be beneficial for ASIC to regularly publish an assessment of IDR performance, by type of financial service provider, as for example, it currently reports on surveillance and reviews it undertakes on providers' compliance with specific requirements.
    - Any assessment released by ASIC should **not**, in ASFA's view, identify particular providers either for 'good' or 'poor' IDR performance. Where ASIC identifies aspects of a particular provider's IDR processes that it considers constitutes worthy of highlighting to other providers, this can be achieved via a media release or similar communication, or an update to any relevant guidance material
    - Where ASIC considers that a provider has demonstrated poor performance against its IDR obligations, that is a matter that should be addressed directly with the provider, with enforcement action taken if necessary (at which time the provider may be identified, under existing processes). To the extent that the provider's performance involves matters of wider application, ASIC could notify other providers via a media release or similar communication, and/or update any relevant guidance material

2.6 Superannuation code of practice

Draft recommendation 5: A superannuation code of practice

The superannuation industry should develop a superannuation code of practice.

As acknowledged in the interim report, ASFA is currently collaborating with a number of other industry stakeholders and participants to develop a code of practice in respect of group insurance in superannuation.

ASFA notes the Panel's recommendation that industry should also collaborate to develop a wider code of practice, "to cover matters such as the industry's key commitments and obligations to consumers on standards of practice across all services provided". We note that this would be an extensive and far-reaching undertaking – especially in light of the significant volume of regulatory change facing trustees and providers currently.

Development of a code of practice could perhaps be considered once the insurance code of practice is in place, however we note that superannuation trustees are already bound by an overarching fiduciary duty as well as substantial legislative prescription in relation to their activities.

2.7 Transition issues

As stated throughout this submission, ASFA does not support the recommendation that the SCT be transitioned to a Superannuation Ombudsman, and does not consider a compelling case to have been made for such a change.

However, it is in ASFA's view important to be aware of the potential transition issues, should the Panel make a final recommendation to the Government that a Superannuation Ombudsman be implemented.

These transition issues will be considerable. ASFA was pleased to see some acknowledgment of this in the Interim Report, with the comment that the Panel "supports a staged process for implementation, recognising that such an approach may better manage transitional issues"[60].

Some of the matters that will need to be considered are outlined below.

[60] EDR Review Interim Report, p23

2.7.1 Extensive amendments to legislation and ASIC regulatory requirements

The transition will require extensive amendments to a range of legislation and ASIC regulatory requirements, including:

- The *S(ROC) Act 1993* – including to provide that the SCT is unable to hear complaints lodged after the specified cutover date, preserve a right of appeal to the Federal Court for complaints heard by the SCT, and maintain an operational existence for the SCT during the runoff period (see 2.7.6 below)
- The *SIS Act 1993* and *SIS Regulations 1994* – including to:
  - remove existing provisions regarding the enforceability of SCT determinations
  - make membership of the Superannuation Ombudsman an aspect of the 'RSE licensee law' and therefore relevant to a trustee's RSE licensee status
  - allow a trustee to act in accordance with a determination made by the Ombudsman without breaching the prohibition on direction of a trustee (this is not an issue under the current model as an SCT determination operates according to law)
- The *Corporations Act 2001* – to remove references to the existence of the SCT as the EDR scheme for superannuation
- The *Corporations Regulations 2001* – to remove references to the existence of the SCT in provisions requiring providers to inform individuals of certain information regarding the making of complaints
- ASIC regulatory material governing approval of EDR schemes – this may include amendments to existing regulatory guides RG 139 *Approval and oversight of external dispute resolution schemes* and RG 165 *Licensing: internal and external dispute resolution*, or the publication of one or more new regulatory guides.

There will be a need to consult with industry on the amendments to each of the above, to ensure unintended consequences – and impacts on consumers – are minimised.

As mentioned in section 1.1.3 above, consideration may also need to be given to amending the *SIS Act 1993* to provide that a trustee that is an RSE licensee may only enter into a contract for group life insurance with an insurer that is also a member of the Ombudsman scheme.

2.7.2 Establishment, approval and staffing of the Superannuation Ombudsman

The establishment and staffing of the Superannuation Ombudsman could realistically occur in two phases:

1. It will be necessary to prioritise the initial establishment of the legal structure of the Ombudsman, and the appointment of key personnel including the Ombudsman and the governing body, so work can commence on drafting of the terms of reference/membership. There may be a need for an interim board to be appointed to facilitate this work, to be replaced at a later date. Finally, ASIC will need to formally approve the Ombudsman as an EDR scheme.
2. Appointment of those staff who will be involved in administration and/or resolution of complaints could occur while the terms of reference are being settled. A number of important considerations should be borne in mind:
   - It will be necessary for the Ombudsman to have full operational capacity as at the cutover date, so it may immediately commence to receive complaints. It must be recognised that the Ombudsman may inherit an immediate workload. Some consumers may delay lodging a complaint in the lead up to the cutover due to confusion about the process, while complaints that had been lodged with the SCT but had not actually commenced to be addressed may need to be transferred to the Ombudsman in order to minimise the SCT's runoff period(see 2.7.6 below)

- Given the need to maintain the SCT during the runoff period, and the fact that the SCT's staff are employees of ASIC and its Chair, Deputy Chair and Tribunal members are statutory office holders), it will not be possible for the new entity to simply absorb the current personnel.

2.7.3 Settling conditions of membership/terms of reference

Once the Superannuation Ombudsman has a legal existence, it will be necessary to develop the conditions for membership/terms of reference. It will be critical to ensure these are subject to a wide-ranging and extensive consultation with all stakeholders, including the APRA-regulated superannuation industry, the regulators ASIC and APRA, consumer advocates, and the public more generally.

Given the significant implications for consumers and trustees alike, it is important that an appropriately lengthy consultation period is provided and it should be recognised that the terms or reference may undergo a number of drafts, each of which should be subject to consultation. Appropriate consultation is critical in order to minimise the risk of unintended consequences.

ASFA notes that due to the particular characteristics of superannuation, it may be necessary for membership of the Ombudsman scheme to be broader in scope than trustees of APRA-regulated funds. In particular, there may be a need to ensure that membership is available to insurers that provide group life insurance to such trustees.

2.7.4 Membership application process

As it appears that the structure of the Superannuation Ombudsman is to be largely mirrored on the existing industry EDR schemes (FOS and the CIO), there will be a need for superannuation trustees to become members of the Ombudsman scheme. Effectively, this will involve meeting the conditions for membership set out in the terms of reference and any other constituent documents, and paying the relevant membership fee.

As noted above, it may be necessary for membership of the Ombudsman scheme to be available to insurers that provide group life insurance to trustees of APRA-regulated funds.

2.7.5 Implications if a trustee does not become a member

The transition process will need to contemplate how to manage the situation where any superannuation trustee fails to apply for membership of the Superannuation Ombudsman, or is not accepted for membership, ahead of the cutover date.

It is envisaged that membership of the Ombudsman would be a requirement under ASIC regulatory guidance (see 2.7.1 above), and therefore failure to obtain membership might jeopardise the trustee's Australian Financial Services Licence (AFSL). Similarly, ASFA would expect that the requirement to hold membership of the Superannuation Ombudsman would be made part of the 'RSE licensee law' under the *SIS Act 1993* (see 2.7.1 above), and therefore a prerequisite to holding or retaining an RSE license.

However, the potential loss of an RSE license or AFSL is a significant sanction that should not lightly be invoked, given the consequences for all members/beneficiaries of the fund. It is important, in ASFA's view, that the requirements allow for an appropriate regulatory response which does not jeopardise the status of the fund and/or trustee for a comparatively trivial matter (for example where there is a minor defect in the membership application which is promptly rectified).

2.7.6 Management of complaints underway as at cutover

ASFA suggests that all complaints lodged from a certain date should fall under the jurisdiction of the Superannuation Ombudsman, while the SCT should retain carriage of any complaints that it had commenced to consider.

It would, in ASFA's view, be inappropriate to automatically transfer any complaint that had begun to be considered by the SCT to an industry-based ombudsman scheme, where it would be subject to a different test, different processes, and substantially different potential outcomes. However, there may be scope to consider allowing consumers to opt to have their complaint transferred.

In either case, there will inevitably be a period of 'runoff' during which the SCT will operate alongside the Superannuation Ombudsman, until it has concluded all open complaints. It would also be appropriate, in ASFA's view, for the existing right of appeal to the Federal Court to remain open in respect of complaints heard by the SCT.

2.7.7 Maintaining funding for the SCT during the runoff period

During the runoff period it will be important to ensure that adequate funding is maintained for the SCT. It would be inappropriate for consumers to suffer impeded service simply because their complaint was heard during a period of enforced change in the EDR arrangements for superannuation.

It will be necessary to carefully consider how any funding needs during this period should be met. The SCT is currently funded by all APRA-regulated funds via the annual financial institutions supervisory levy. That is appropriate given all APRA-funds currently have the potential to have complaints referred to the SCT.

From the cutover date, however, the SCT will cease to be relevant for all APRA-funds other than those with open complaints before the Tribunal. APRA would question whether it is appropriate for funds that do not have open complaints with the SCT to continue to fund its ongoing cost. Similarly, we consider it inappropriate that the entire operating cost of the SCT, during the runoff period, be funded by those funds with open complaints simply because they are a party to a complaint which happened to be heard by the SCT during a period of enforced change in EDR arrangements. In ASFA's view, the only appropriate solution would appear to involve a funding allocation from consolidated revenue for the runoff period.

2.7.8 Lead time must be adequate for industry to prepare

The change in EDR arrangements would have significant implications for superannuation trustees and it is vital that they be given adequate time to prepare.

At a minimum, trustees may need to change internal processes around complaints handling, there will be considerable changes to disclosure and communications materials (Product Disclosure Statements, websites, letter templates), and significant staff training will be required (both complaints specialists and general contact centre staff). It is also likely that trustees will consider it prudent and/or necessary to obtain legal advice on matters relating to membership of the Ombudsman scheme, and the impacts on complainants, to inform these process, disclosure and communication changes.

Disclosure, communication and consumer interface will be significantly complicated by the fact that two separate – and quite different – EDR regimes are likely to be in operation during the runoff period.

2.7.9 An extensive education campaign will be needed

Given the considerable 'brand recognition' enjoyed by the SCT, it will be necessary to mount an educational campaign to ensure that consumers, advisers and stakeholders (including industry commentators and the media) are aware of the changes to EDR arrangements for superannuation and their implications, as well as the likely dual operation of the Ombudsman and the SCT during the runoff period.

Consideration will need to be given to how such a campaign might be appropriately funded.

2.8 Compensation scheme of last resort

Observation 1: Compensation scheme of last resort
The Panel is of the view that there is considerable merit in introducing an industry-funded compensation scheme of last resort.
Draft finding 7:
Where a consumer does not receive the compensation due to them because of a financial firm's lack of resources, it has a negative impact on both the individual consumer and the broader financial system.

ASFA does not support any proposed industry-wide compensation scheme that has the potential to involve cross-subsidisation by the APRA-regulated superannuation sector of losses incurred within other sectors. As set out in this submission, APRA-regulated superannuation has attributes which differentiate it from other types of financial products. The sector already has a targeted compensation scheme in place, which has been invoked in appropriate circumstances in the past.

ASFA agrees that consumer confidence is impacted when a consumer does not receive the compensation due to them. However, we note that cases of non-payment of determinations and other failures to compensate have not been experienced uniformly across the financial services industry, in fact they have been primarily confined to particular sectors. We also note that the occurrence of a failure or misconduct within a sector that is significant enough to trigger the proposed compensation scheme is likely to itself impact consumers' confidence not only in that sector but also potentially in the broader financial system.

In ASFA's view, consumer confidence might be more effectively supported by implementing measures directly targeted to those sectors where most issues are experienced.

ASFA notes that Richard St John, who during 2010-12 conducted an extensive inquiry of compensation arrangements in financial services, concluded that greater efforts were required to secure compliance by individual providers, before it would be appropriate to consider any compensation scheme of last resort. ASFA considers the following comments by Mr St John to be particularly apposite (our emphasis):

> *I have concluded that it would be inappropriate, and possibly counter-productive, to introduce a more comprehensive last resort compensation scheme to underpin the current relatively light compensation regime for financial advisers and other providers of financial services.* ***Given the limited regulatory measures to protect retail clients from the risk of licensee insolvency, it would be inappropriate to require more responsible and financially secure licensees to underwrite the ability of other licensees to meet claims against them for compensation****. There would also be an element of regulatory moral hazard should a last resort scheme be introduced without a greater effort first to put licensees in a position where they can meet compensation claims from retail clients. It would reduce the incentive for stringent regulation or rigorous administration of the compensation arrangements.*

> ***Priority should be given**, in any move to bolster the protection of retail clients, **to a more rigorous approach to compliance by licensees to provide greater assurance that they will be in a position to compensate their own clients through their insurance arrangements and the capital resources they have at risk**.*
>
> *To put it another way, **the regulatory platform for financial advisers and other licensees needs to be made more robust and stable before a safety net, funded by all licensees, is suspended beneath it**. I see this as a necessary step **before further consideration is given to a scheme under which the cost of uncompensated claims against one firm would be passed on to other firms who are not so remiss**. This would be consistent too with the more robust regulatory approach to the providers of services elsewhere in the financial system, including prudential regulation, where last resort protection is offered to consumers.*[61]

2.8.1 A compensation scheme of last resort already exists for APRA-regulated funds

As acknowledged in the Interim Report, the APRA-regulated superannuation sector already has in place arrangements which effectively provide a compensation scheme of last resort. Part 23 of the *SIS Act 1993* provides protection for members of a regulated superannuation fund (other than a self-managed superannuation fund or SMSF) or an approved deposit fund, where there has been a loss as a result of fraudulent conduct or theft, causing substantial diminution of the fund leading to difficulties in the payment of benefits.

Where an 'eligible loss' has been established, the Minister may approve a grant of financial assistance to the trustee of the impacted fund. A levy is then raised on all APRA-regulated funds to recoup the grant. To date, Part 23 has been utilised only a handful of times since it was established in 1993, with levies raised in respect of the 2001-02, 2002-03, 2003-04, 2004-05, 2010-11 and 2012-13 years.

We note the comment in the Interim Report that a "pooled superannuation trust and a self-managed superannuation fund are not eligible" for assistance under the Part 23 scheme[62]. This is a true statement and, we submit, an appropriate outcome.

A pooled superannuation trust (PST) is an investment structure for superannuation-related assets, it is not a superannuation 'fund' in the traditional sense. The range of possible investors in a PST, as prescribed by legislation[63], comprises regulated superannuation funds, approved deposit funds, other PSTs and life insurance companies (using certain superannuation related assets only). It is not possible for a consumer to invest directly in or be a member of a PST, and PSTs do not receive contributions or rollovers. To the extent that a consumer who is a member of an APRA-regulated fund has indirect exposure to a PST, through an investment in that PST by the trustee of the fund of which the consumer is a member, and the trustee incurs a loss due to fraud or theft involving that PST, that may be an 'eligible loss' for the purposes of Part 23.

Self-managed superannuation funds (SMSFs) are also excluded from coverage under Part 23. This was a matter of conscious design. As noted by the Treasury during a 2003 review of Part 23:

[61] Richard St John, *Compensation arrangements for consumers of financial services*, April 2012, piii-iv
[62] EDR Review Interim Report, p167
[63] Sub-regulation 1.04(5) of the *Superannuation Industry (Supervision) Regulations 1994*

> As the SMSF trustees are also members, it is assumed that the trustee(s) will act in their own best interests, and that members do not need the full range of statutory measures to protect them in relation to the conduct of the trustee. Accordingly, SMSFs are exempted from some provisions in the SIS Act, including the financial assistance provisions of Part 23 of the SIS Act. This is in accordance with a recommendation of the Financial Sector (Wallis) Inquiry.[64]

Similarly, Richard St John, in his 2010-12 inquiry into the merits of a compensation scheme of last resort, noted that:

> Part 23 specifically excludes self-managed superannuation funds (SMSF) from being able to apply for financial assistance under Part 23. This is on the basis that SMSF members, as trustees of their SMSF, have direct control over their superannuation savings and are in a position to protect their own interests. The trustees of an SMSF, in circumstances where they qualify as retail clients under the Corporations Act, have rights to compensation in line with other retail clients.[65]

SMSFs are not subject to the extensive and onerous prudential regulation faced by APRA-regulated funds, and are exempt from many stringent requirements under the *SIS Act 1993* and the *SIS Regulations 1994* that apply to APRA-regulated funds. SMSFs pay a modest supervisory levy to the ATO, reflecting this reduced level of regulation, but are exempt from the levies raised from the APRA-regulated superannuation sector to recoup the financial assistance awarded under Part 23. The regulatory regime recognises the heightened level of responsibility assumed by the members (who are also trustees) for decisions – including investment related decisions – relating to the SMSF. As noted by Richard St John, the "degree of protection afforded … reflects the perceived intensity of the financial promises in question"[66]. Given this, ASFA considers it appropriate that SMSFs are excluded from coverage under Part 23.

2.8.2 APRA-regulated superannuation must be quarantined

ASFA does not support any proposed industry-wide compensation scheme that has the potential to involve cross-subsidisation by the APRA-regulated superannuation sector of losses incurred within any other sector.

In the event that the Government were to proceed to introduce a broader compensation scheme, ASFA considers it imperative that APRA-regulated superannuation monies are either:

- entirely excluded from the scheme, with any eligible losses continuing to be redressed via Part 23 of the *SIS Act 1993*; or
- included within the broader scheme, but explicitly and completely quarantined from any potential exposure to losses incurred outside the APRA-regulated superannuation sector.

In particular, ASFA takes the view it would be inappropriate for APRA-regulated superannuation monies to be levied as part of any compensation scheme, other than where misconduct has caused a superannuation fund to fail. This is on the basis that APRA-regulated funds:

- are prudentially supervised and regulated
- already pay a significant levy for that supervision, as well as other levies
- have had a relatively low incidence of failure and a negligible incidence of non-payment of SCT determinations

[64] The Australian Government, the Department of the Treasury, *Review into Part 23 of the Superannuation Industry (Supervision) Act 1993*, 3 June 2003, para 17
[65] St John, 2012, p161
[66] St John, 2012, p56

- typically contain superannuation guarantee contributions, effectively representing deferred salary and wages
- generally have to pass the cost of any levy through to members.

Similarly, it would be inappropriate for superannuation funds to have to pay any up-front, annual management levy to the scheme.

Development of an equitable compensation scheme would involve consideration of a number of complex and important design issues to ensure that moral hazard is appropriately addressed, including a need to ensure that any formula for determining a financial provider's contribution to the scheme adequately takes into account risk, and not merely funds under management/advice.