14th February 2014

Attention:

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

Australian Government – Better Regulation and Governance, Enhanced Transparency and Improved Competition in Superannuation (Better Regulation) – Discussion Paper/28 November, 2013

1. Focus question

As long-term researchers within the Australian superannuation industry, we wish to take this opportunity to provide feedback and comments on **Focus Question One** which relates to Regulatory Impact Assessments (RIA).

The question reads: "The Government has committed to identifying (in dollar terms) measures that offset the cost impost to business of any new regulation. What suggestions do you have for how the regulatory compliance burden can be reduced?"

2. Complexity and regulatory capture

Our joint research has focused on attempting to explain the widespread view, explicit in the focus question, that there is too much regulation in the superannuation industry[1]. Evidence for this view arises from our survey of trustees, as well as widely reported views of the industry in addition to APRA's own surveys.[2]

Our explanation is that it arises, in important respects, from both the failure of regulators to fulfil their obligations and subtle forms of regulatory capture by vested interests in the industry. Academic theory of regulatory capture has not been particularly well developed, and recent research warns of unthinkingly applying blame to undoubtedly powerful business interests. David Carpenter[3] suggests that: '…to claim capture, an argument ought to:

[1] Taylor, Sue and Anthony Asher (2013) "Regulatory Capture and Overload in the Australian Superannuation Industry over the Last Decade: Trustees' Views and a Cost/Benefit Analysis" Presented to the 21st Annual Colloquium of Superannuation Researchers, Sydney, July.

[2] APRA Stakeholder Survey, (2013), Report of overall findings, July, Produced by Australian Survey Research, at pp. 8-9).

[3] D. Carpenter (2013), 'Detecting and Measuring Capture', in D Carpenter & D. Moss (eds.) (2013), Preventing Regulatory Capture: Special Interest Influence and How to Limit it', The Tobin Project, Harvard Law School, Cambridge University Press, at pp. 3-4.

- Provide a defeasible model of the public interest
- Show a policy shift away from the public interest and toward industry (special) interest
- Show action and intent by the industry (special interest) in pursuit of this policy shift sufficiently effective to have plausibly caused an appreciate part of the shift.

While our research is far from complete, there is evidence within the superannuation industry of a growing regulatory burden that has significantly benefitted larger players and the compliance industry (which may include some of the regulators themselves) at the expense of having significantly reduced the number of competing funds in the industry.[4]

We believe that the solution lies in the proper implementation of the Regulatory Impact Analysis (RIA) framework that has ostensibly had bipartisan political support for some decades. In order to fully appreciate the critical importance of the RIA process within the Australian superannuation industry however the reality faced by fund members must be appreciated. That is, their mandatory, occupational superannuation payments have been fully captured within an extremely complex, publicly mandated, but privately controlled superannuation system. This point was acknowledged within the June 2010, Cooper-led, Labor Government's 'Super System Review: Final Report – Part One: Overview and Recommendations' (CSSRR) (Para. 3.2.2), which highlighted that compulsory occupational superannuation payments were fully outsourced to a multitude of privately controlled schemes.

Within this context, our arguments go along the following lines – evidence and background for them can be found in related numbered sections within the Appendix.

1. Government policy intentions have clearly been for a detailed RIA, however both the Office of Best Practice Regulation's (OBPR) 2010 Best Regulation Handbook and the 2014 OBPR Interim Guidelines, in their implementation, offer a range of carve-outs, 'weak-form', potentially qualitative only, Regulation Impact Statements (RIS) and Ministerial exemptions. In addition, regulatory-based election promises have also been traditionally exempted from the RIA process.[5] As highlighted by the 2006 Banks Taskforce Report (at p. 18)[6], '…RIA compliance has also tended to be lowest for the more significant or controversial regulations, where good process is most needed.' Of great concern, and as highlighted in the OECD's 2010 Review Report[7], this low compliance level appears to be an orchestrated outcome given that:

   '…a fully implemented, quantitative based RIA has the capacity to prevent rent seeking and promote the highest social benefits in regulation, thus generating many potential opponents. For example…Departments may have an incentive to evade the requirements of RIA either because of resource demands or because it precludes a favoured use of regulatory power (OECD 2010, at p. 45).'

[4] For example, refer to Taylor, S. 2011, 'Captured Legislators and Their Twenty Billion Dollar Annual Cost Legacy', *Australian Accounting Review*, 21, 3: 266 – 281.
[5] As detailed by the Centre for International Economics, 10th May 2010, in their Submission to the Productivity Commission (PC) Review of Regulation Impact Analysis, at p. 7.
[6] The Taskforce on Reducing Regulatory Burdens on Business, Rethinking Regulation (January 2006) (Banks Taskforce Report), pp i and ii. <http://www.regulationtaskforce.gov.au/finalreport>.
[7] OECD, Government Capacity to Assure High-Quality Regulation in Australia (2010). <http://www.oecd.org/dataoecd/63/59/44529857.pdf>.

2. Within this context, the size and power of the financial services sector is significant. Dominated by the four large banking conglomerates, which account for half of its employment and whose market position continues to increase, the power of the financial services sector suggests that it may have disproportionate influence on superannuation regulation to the point of potentially capturing both legislative and agency policy-making processes. This point is made by Adair Turner, previous head of the UK Financial Services Authority, when he highlights that the sector has the power:

   '…to generate unnecessary demand for its own services…and attract to themselves unnecessarily high returns and create instability which harms the rest of society[8].'

3. There are a significant number of examples of exemptions, carve-outs and 'weak' RIS that have been applied to the superannuation legislative reforms. In the last decade, these have included the introduction of the licensing regime, the APRA prudential standards and the Stronger Super reforms. However the problem of low compliance levels in terms of the RIA process can be traced back to the failure to generate either an appropriate RIS for the fundamental building block of Australia's superannuation system and that is the 1993 enactment of the *Superannuation Industry (Supervision) Act* or to ensure a timely post-implementation review process.

3. Recommendations to more closely align RIA principles with practices

As highlighted by the PC in their 2012 Report (at p. 195),[9] they believed that there is a:

> '…large gap that exists between principle and practice…[Thus]…improving RIS quality is unlikely to be achieved by simply providing more detailed guidance material or further strengthening analytical requirements. Based on the evidence examined, such an approach would likely only further widen the gap between principle and practice. In view of this, other approaches are needed.'

Our research within the superannuation industry supports this belief. For example, the Coalition Government's 2001 Issues Paper entitled 'Options for Improving the Safety of Superannuation' provided a detailed public interest rationale for the passage of the licensing, legislative enactments. Within this document, it is argued that legislative intervention was necessary given that '…superannuation is essentially a managed investment with special characteristics that collectively place an onus on Government to ensure proper governance frameworks.'[10] These special characteristics included: compulsion; restricted member access to their investments until retirement; limited choice and portability; and a range of information asymmetries related to superannuation investment risk.

In introducing the key licensing regime associated with this 'Safer Superannuation' rationale in 2004, the OBPR, however, exempted these legislative reforms from any form of RIS or from any post-implementation review process. Thus, the Federal Government in Australia failed to fulfil its own public interest objectives by not enforcing a detailed, quantitative analysis in relation to its regulatory reforms

8 Turner, A (2009) Mansion house speech
http://www.fsa.gov.uk/library/communication/speeches/2009/0922_at.shtml

9 Productivity Commission 2012, Regulatory Impact Analysis: Benchmarking, Research Report, Canberra.

10 Commonwealth of Australia 2001, 'Options for Improving the Safety of Superannuation', Canberra.

within the superannuation industry. Internationally, this is inconsistent with the current emphasis and direction of the Securities Exchange Commission which has placed a high priority on detailed, economic analysis in all its rule makings.[11] The absence of evidence-based analysis is also inconsistent with the OECD's Guiding Principles,[12] to which Australia is a signatory, which prioritise transparency and accountability in policy making.

Important mechanisms to more effectively blunt the force of capture are:

1: for both political parties and the OBPR to more clearly understand the nature of the industry within which the RIS are being prepared;

2: for the legislature to more clearly elaborate the critically important RIS threshold concepts such as 'minor or machinery in nature' and 'does not substantially alter existing arrangements'; and

3: to significantly restrict the carve-out and exemption provisions that are included within the Australian Government Regulation Impact Assessment process which is to be issued in 2014.

We recommend that such changes take into account the 2012 Independent Review Report's[13] recommendation (at p. 18) that where a prima facie case for regulatory reform has been established, a range of feasible policy options need to be identified and their relative merits rigorously assessed. This should include assessing the costs and benefits of regulatory alternatives, including quantifying compliance costs and undertaking risk assessments.

In addition, as highlighted by the Productivity Commission's 2012 Report (at p. 236)[14], of critical importance is that:

> '…RIS documents should not be delivered to the door of executive government to inform decisions and then disappear. RIA processes are less about giving a single answer, and more about framing problems, scoping solutions and uncovering unintended consequences of proposed regulatory measures. A RIS should not fade from the scene once a regulatory decision enters parliament, but should remain an important reference point in political negotiations in the parliament before final decisions are taken. In short, RIA processes should not only better inform executive government decisions; they should also better inform the decisions of Australian parliaments.'

Thank you for your time in reading this submission.

Dr Sue Taylor, School of Accountancy, QUT Business School, Brisbane, Australia, **Corresponding Author**.
Email: sm.taylor@qut.edu.au

Associate Professor Anthony Asher, Australian School of Business, University of New South Wales, Sydney, NSW, Australia. Email: Anthony Asher a.asher@unsw.edu.au

[11] Refer to Securities Exchange Commission 2012, 'Memorandum to Staff of the Rulewriting Divisions and Offices – Current Guidance on Economic analysis in SEC Rule Making', Securities Exchange Commission, New York; Securities and Exchange Commission, Memorandum: Use of the Current Guidance on Economic Analysis in SEC Rulemakings, June, 2013

[12] OECD (2005), Guiding Principles for Regulatory Governance and Performance, Paris.

[13] Borthwick, D. and Milliner, R. 2012, Independent Review of the Australian Government's Regulatory Impact Analysis Process, April.

[14] Productivity Commission 2012, Regulatory Impact Analysis: Benchmarking, Research Report, Canberra.

APPENDIX

1. Government Intentions: 2014 OBPR Guidelines and Potential Regulatory Capture Mechanisms

The Office of Best Practice Regulation (OBPR) is seeking to address the regulatory compliance issues that have arisen from prior interventions through the January 2014 release of new guidelines for RIA in the form of the Interim Regulation Impact Statement Process Guidance Note (GN). These Interim Guidelines will then be replaced by a new comprehensive guide to the Australian Government Regulation Impact Assessment process which is to be issued in 2014 and will replace the 2013 Best Practice Regulation Handbook.

The requirements of this two-staged GN (the Options and Details Stages) serve to more closely align the Federal Government's RIS processes with those recommended by prior reviews including: the 2006 Banks Taskforce on Reducing the Regulatory Burden on Business (Rethinking Regulation)[15]; the 2010 OECD Report on the Australian Government's Capacity to Assure High-Quality Regulation[16]; the 2011 Productivity Commission (PC), Identifying and Evaluating Regulation Reforms Report;[17] the 2012 Independent Review of the Australian Government's Regulatory Impact Analysis Process[18]; and the 2012 Regulatory Impact Analysis Benchmarking Research Report by the Productivity Commission (PC) [19].

To facilitate the Government's objective of reducing regulatory compliance issues, the Office of Best Practice Regulation (OBPR) has been transferred from the Department of Finance to the Department of the Prime Minister and Cabinet. The Government has also strengthened the RIA framework, with a focus on costing impacts on business, community organisations and individuals as part of a broader goal to reduce the burden of regulation. The key changes to the RIS process include the requirements that a RIS is required for all Cabinet submissions, even if the proposal is of a minor or machinery nature or does not have a regulatory impact on business, community organisations or individuals. A RIS is also mandatory for all non-Cabinet decisions made by the Australian Government and its agencies that are likely to have a regulatory impact on business, community organisations or individuals. However, a RIS is not required for non-Cabinet decision-makers if the regulatory impact is of a minor or machinery nature and does not substantially alter existing arrangements.

Of concern is that the efficacy of these provisions rely on the appropriate use of words such as 'minor or machinery in nature' and 'does not substantially alter existing arrangements' and the available exemptions and carve-out mechanisms that remain within the RIA process as part of the OBPR's 2013 Best Regulation Handbook. For example, in terms of carve-outs, the OBPR is responsible for advising

---

[15] The Taskforce on Reducing Regulatory Burdens on Business, Rethinking Regulation (January 2006) (Banks Taskforce Report), pp i and ii. <http://www.regulationtaskforce.gov.au/finalreport>.

[16] OECD, Government Capacity to Assure High-Quality Regulation in Australia (2010), p 67. <http://www.oecd.org/dataoecd/63/59/44529857.pdf>.

[17] Productivity Commission, Identifying and Evaluating Regulation Reforms (2011), http://www.pc.gov.au/projects/study/regulation-reforms.

[18] Borthwick, D. and Milliner, R. 2012, Independent Review of the Australian Government's Regulatory Impact Analysis Process, April.

[19] Productivity Commission 2012, Regulatory Impact Analysis: Benchmarking, Research Report, Canberra. This latter Report undertook a detailed study designed to benchmark the efficiency and quality of Commonwealth, state and territory and Council of Australian Governments (COAG) Regulatory Impact Analysis (RIA) processes, as at January 2012.

government agencies on whether regulation impact statements are required.[20] To assist in improving the efficiency of this process, the OBPR often grants 'carve-outs'. A carve-out is a standing agreement between the OBPR and an agency that removes the need for a preliminary assessment to be sent to the OBPR for certain types of regulatory change. As highlighted in the OBPR's 2013, Best Regulation Handbook, a carve-out can be used for regulatory changes that occur on a regular basis, are minor or machinery in nature. Possible categories of carve-outs include indexation changes and routine administrative changes.

In relation to exemptions, Appendix C of the currently applicable, 2013, Best Regulation Handbook provides that exemptions from the RIS requirements for exceptional circumstances can be granted by the Prime Minister in writing. A minister wishing to obtain an exemption should write a letter to the Prime Minister, copied to the Treasurer and the Minister for Finance and Deregulation, addressing the criteria under which an exemption is required. Prime Minister's exemptions are only granted where: truly urgent and unforeseen events arise, requiring a decision before an adequate RIS can be undertaken; or where there is a matter of Budget or other sensitivity and premature announcement (even of options) could cause unintended market effects or lead to speculative behaviour which would not be in the national interest.

It is important to note that the existence of exemptions and carve-out provisions within the OBPR's Best Regulation Handbook and its focus on excluding, for example, non-Cabinet decision-makers if the regulatory impact is of a minor or machinery nature and does not substantially alter existing arrangements, can potentially facilitate regulatory capture of the RIA process by the regulated industries. This is particularly the case within the context of the Australian superannuation system given the size of the superannuation asset base and the related power of the Financial Services Sector as detailed below.

2 The Relevance of the Size and Power of the Financial Services Sector to the Achievement of RIA Process Objectives

Our prior research[21] has highlighted the regulatory compliance burdens that currently exist within the superannuation industry in Australia which have resulted from the particular, partisan approaches that were originally adopted by both the Labor (Hawke/Keating) and Coalition (Howard) Governments throughout the last three decades in particular, as they instigated the largest legislative expansion in Australia's history.[22] These regulatory reforms transformed Australia's occupational superannuation which, until 1980, had played only a peripheral role in securing retirement savings for the workforce at large with less than 40% of all employees at this time contributing to superannuation schemes with the key plank of retirement incomes policies of both political parties resting on the universal (but means-tested) old-age pension. By the time the twenty-first century began, however, 91% of all Australian employees and 81% of all workers at this time were covered by superannuation.

[20] OBPR External Guidance Note – Carve-outs, December 2012, Australian Government, Department of Finance and Deregulation, Office of Best Practice Regulation, at p.1.
[21] For example, refer to Taylor, Sue and Anthony Asher (2013) "Regulatory Capture and Overload in the Australian Superannuation Industry over the Last Decade: Trustees' Views and a Cost/Benefit Analysis" Presented to the 21st Annual Colloquium of Superannuation Researchers, Sydney, July.
[22] Berg, C. 2008. 'The Growth of Australia's Regulatory State', Institute of Public Affairs, Melbourne, Australia, at p. 15.

By the end of September 2013, superannuation assets had reached $1.75 trillion, covering 94% of all Australians while total contributions for the year to this date totalled $90.3 billion.[23] The total superannuation market is then expected to grow to $3.353 trillion dollars (measured in 2013 dollar terms) by 2018[24] and, to $7.6 trillion by 2033, or in real terms, to approximately 180% of GDP over the next 20 years.[25]

In turn, the largest 20 superannuation funds measured by assets within the industry accounted for 57.3% of these assets and 52.5% of members of Australian Prudential Regulation Authority (APRA) funds with more than four members[26] and the industry held 21% of total financial institutions assets, putting its share second only to that of banks.[27] This current pool of funds is equivalent to approximately 100% of Australia's annual GDP, significantly higher than the weighted OECD average, and 120% of the Australian share market capitalisation, where they are the dominant investors holding some half the value of all listed shares.[28]

As at June, 2013, an estimated 40.1% of these superannuation assets were under management by investment managers making the Australian managed fund industry the fourth largest in the world.[29] In 2013-14, IBISWorld forecasts that this industry will generate revenue of $12.7 billion from an estimated $703.2 billion in superannuation assets under management. This represents revenue growth of 15.1% from the previous year.[30]

As John Brogden, the Chief Executive of the Investment and Financial Services Association, the main lobby group in the financial services industry, has highlighted, financial services is the largest single sector of the Australian economy which invests $1.9 trillion on behalf of working Australians.[31] In 2013, this sector accounted for '… more than ten per cent of the total value added, up from five per cent in the mid 'eighties, and closer to two per cent in the years immediately following World War Two… [and] is also large relative to many other countries such as the United States, Canada, the Euro area and Japan.' [32] The Australian Bureau of Statistics data on Australia's National Accounts, released in June 2013, also highlighted that the Finance and Insurance Sector has been growing at well over double the pace of the rest of the economy since deregulation.[33]

The size and power of the Financial Services Sector is, then, a key factor that needs to be taken into account in any review of the RIA process related to the superannuation industry. This is particularly the

---

[23] APRA (2013b), Statistics - Quarterly Superannuation Performance (interim edition), September 2013 (issued 21 November 2013), p. 6.
24 Rice Warner Media Release, 18th December, 2013, 'World class, more change coming - Rice Warner releases updated retirement savings projection scorecard', at p. 1.
25 Deloittes (2013), Dynamics of the Australian Superannuation System: The next 20 years: 2013 – 2033, at p. 4.
26 APRA (2013b), Statistics - Quarterly Superannuation Performance (interim edition), September 2013 (issued 21 November 2013), p. 6.
27 KPMG (2012). Evolving Superannuation Industry Trends; Shorten 2013 at p.1; APRA 2012 (a) at p. 9.
28 KPMG (2012), at p. 9.
29 Superannuation Funds Management Services in Australia: Market Research Report, October 2013, IBISWorld, accessed on the 23rd December, 2013 at http://www.ibisworld.com.au/industry/default.aspx?indid=1890.
30 Superannuation Funds Management Services in Australia: Market Research Report, October 2013, IBISWorld, accessed on the 23rd December, 2013 at http://www.ibisworld.com.au/industry/default.aspx?indid=1890
31 Financial Services Council (2013), 2013-14 Federal Budget Submission, at p. 3.
[32] Rodney Maddock (2013), Is the Australian financial sector too big?, , Monash University and Victoria, University, at p. 3. http://www.australiancentre.com.au/sites/default/files/NewsDocs/D1P1%20-%20Is%20the%20financial%20sector%20too%20big%20%20RMaddock.pdf
[33], Australia's Financial Sector Continues to Dominate the Economy', article, September, 2013, MacroBusiness, http://macrobusiness.com.au/2013/09/australia-on-fire-once-again.

case given that a RIA process is expected to provide relevant information to decision makers and stakeholders about the expected consequences of proposed superannuation-based regulation. By providing a '…better informed, objective, evidentiary basis for making regulations, RIA seeks to ensure that the policy development process consistently delivers regulations (or other policy solutions) that provide the greatest benefit to the community, relative to the overall costs imposed (Productivity Commission 2012, p. 3).' This public interest-based objective can be placed at significant risk from potentially conflicting, private interests in the form of legislative, agency and corrosive capture[34] mechanisms utilised by the financial services sector in Australia which is seeking to protect/control the government mandated, but privately controlled, trillion dollar, superannuation asset base.

As highlighted by Novak[35]:

> '…there is simply no older theme in the Western legal and political tradition than the one highlighted by capture. In Plato's Republic, Socrates noted that "our aim in founding the State was not the disproportionate happiness of any one class, but the greatest happiness of the whole." And he bemoaned "the corruption of society" whereby "the guardians of the laws and of the government are only seemingly and not real guardians" who "turn the State upside down" and ultimately destroy it. Aristotle's Politics also decried the corrupting effects of private interest and private vice on the commonwealth noting that 'the true forms of government, therefore, are those in which the one, or the few, or the many, govern with a view to the common interest; but governments which rule with a view to the private interest, whether of the one, the few, or the many, are perversions.'

The concept of corrosive capture is particularly relevant in terms of the RIA process currently operating within the superannuation industry given that and as detailed by Carpenter (2013, p.3)[36]:

> '…special interests and regulated industries can shape policies in different ways, and they can push policies in several directions. The Stiglerian account of capture predicts that captured regulation will be stronger in the sense of more rigid and less permeable entry barriers to the market. If the industry is using regulation to form a cartel and restrict supply and/or entry, then captured regulation will be more effective for these aims to the extent that it is more effective in terms of achieving its stated aims, that is, to the extent that the entry barriers are strong. If physicians seek to limit the supply of their services and thereby raise their pay, then licensing needs to present higher hurdles to qualification and entry for prospective doctors. Corrosive capture, on the other hand, occurs if clearly organized firms push the regulatory process in a "weaker" direction.'

---

[34] D. Carpenter (2013), 'Detecting and Measuring Capture', in D Carpenter & D. Moss (eds.) (2013), Preventing Regulatory Capture: Special Interest Influence and How to Limit it', The Tobin Project, Harvard Law School, Cambridge University Press; and D. Carpenter (2013), 'Corrosive Capture? The Dueling Forces of Autonomy and Industry Influence in FDA Pharmaceutical Regulation', in D Carpenter & D. Moss (eds.) (2013), Preventing Regulatory Capture: Special Interest Influence and How to Limit it', The Tobin Project, Harvard Law School, Cambridge University Press. Daniel Carpenter is the Free Professor of Government, Harvard University.

[35] W. Novak (2013), 'A Revisionist History of Regulatory Capture', in D Carpenter & D. Moss (eds.) (2013), Preventing Regulatory Capture: Special Interest Influence and How to Limit it', The Tobin Project, Harvard Law School, Cambridge University Press, at p. 3. Novak's quote refers to comments in: Plato, The Republic: The Complete and Unabridged Jowett Translation (New York, 1991), Book IV, 129-130, and Aristotle, The Politics and The Constitution of Athens (Cambridge, 1996), Book III, 71

[36] Daniel Carpenter (2013), 'Corrosive Capture? The Dueling Forces of Autonomy and Industry Influence in FDA Pharmaceutical Regulation in in D Carpenter & D. Moss (eds.) (2013), Preventing Regulatory Capture: Special Interest Influence and How to Limit it', The Tobin Project, Harvard Law School, Cambridge University Press, at pp. 2-3.

In this case, the interests of the Financial Services Sector are best served by a 'weakly' applied RIA process which facilitates the introduction of industry desired legislation without scrutiny, such as the 2004 Registrable Superannuation Entity (licensing) reforms and the 2012 APRA-based Prudential Standards. These regulatory reforms simultaneously generate significant barriers to entry and survival through increasing compliance costs which benefit the larger, existing retail funds within the industry. These issues will be elaborated with particular examples in the following section.

3 Examples of Exemptions, Carve-Outs and 'Weak' RIS Applied to Superannuation Legislative Reforms

In order to effectively reduce the regulatory compliance burden within the superannuation industry, the examples provided of the range of carve-outs, 'weak-form' RIS and exemptions that have characterised the superannuation regulatory reform process to this point need to be carefully considered. These examples clearly highlight that greater attention needs to be paid to both the carve-out and exemption provisions that should be in place and the quality of RIS that are provided. Of particular importance is to ensure the independence of the decision-making processes of the OBPR in terms of both its development of policy and the implementation process.

In its 2011 Report, the PC observed:[37]

> 'Regulation has grown at an unprecedented pace in Australia over recent decades. As in other advanced countries, the increase in the stock of regulation has been a response to the new needs and demands of an increasingly affluent and risk adverse society and an increasingly complex global economy. This regulatory accretion has brought economic, social and environmental benefits. But, it has also brought substantial costs. Some costs have been the unavoidable by-product of pursuing legitimate policy objectives. But, a significant proportion has not. And in some cases the costs have exceeded the benefits. Moreover, regulations have not always been effective in addressing the objectives for which they were designed, including regulations designed to reduce risk.'

These past reviews also agreed that there were significant shortcomings in system design and a considerable gap between agreed RIA principles and what happens in practice which had served to reduce the efficacy of RIA processes. At the heart of these implementation failings were a range of issues which included[38]: the number of proposals with highly significant impacts that were either exempted from RIA processes or were not rigorously analysed; the fact that public consultation on policy development was often perfunctory or occurred only after development of draft legislation; and, while RIA processes had brought some isolated but significant improvements from more thorough consideration of policy options and their impacts, the primary benefits of RIA have been forfeited through a lack of ministerial and agency commitment.

Thus it is not surprising that, in 2007, the then Honourable Kevin Rudd, highlighted that 'despite the long history of regulatory reform initiatives, these efforts had not been sufficient to deliver a material reduction in the regulatory burden on business.' In turn, the Labor Party renewed its commitment to a rigorous RIA process to protect businesses from new, unnecessary regulation. However this renewed commitment to reduce the regulatory burden on business, which has been consistently shared by the

[37] Ibid, p XI.

[38] 2012 Regulatory Impact Analysis Benchmarking Research Report by the Productivity Commission at p. 2.

Coalition Government, has not been achieved based on the data provided to the 2012 Independent Review cited above. That is, for the period 1 December 2007 to 31 December 2011 (at p. 110):

- 15,942 Commonwealth Acts and legislative instruments have been introduced; and
- 5,792 Commonwealth Acts and legislative instruments have been repealed,

as against approximately 3,295 Preliminary Assessments (PAs)[39] and 239 RISs required.

Thus, the data provided to the Independent Review clearly highlights that, of the regulatory measures undertaken by the Commonwealth, relatively few are subject to a RIS. Also of concern was the trend in the data given that (2012, p. 111):

> '…the Government's 2010 modifications to the RIA Framework [were designed] to extend the scope of regulatory reviews to all regulatory proposals, other than those of a minor or machinery nature; and to remove the ability of agencies to self-assess whether a RIS is required, leaving this decision instead to OBPR, would intuitively suggest an increase in the number of RISs. However, the data does not show any appreciable increase in the number of RISs undertaken…which seemingly was one of the likely outcomes, if not intentions, of the 2010 reforms.

As highlighted by the 2012 Regulatory Impact Analysis Benchmarking Report by the Productivity Commission (pp. 62-63), a number of stakeholders identified regulatory proposals with significant impacts that were bypassing RIA:

> '…There are a number of explanations for proposals with significant impacts not having a RIS or escaping RIA altogether, including that: the agency and/or oversight body do not adequately consult with stakeholders to correctly gauge the importance of a regulatory proposal; the responsible Minister chooses to take the proposal to Cabinet notwithstanding its non-compliance with RIA requirements; or an exemption is granted. Of greatest concern, however, is the perception that in some jurisdictions proposals (often politically contentious) with highly significant impacts are more likely not to be subjected to adequate RIA than other less significant proposals, either because: they are more likely to be granted an exemption from the process by the Prime Minister, Premier, Treasurer or relevant delegated officer, or, where no exemption is granted, it is more likely that a RIS will nevertheless not be prepared at all for proposals with highly significant impacts or that the analysis in the RIS will be assessed as inadequate.'

The concerns raised by the Productivity Commission had previously been identified in the 2006 Banks Taskforce Report[40] which stated that (Appendix C):

> '…RIA compliance has tended to be lowest for more significant or controversial regulations, where good process is most needed. It also noted that in many cases, RISs appear to have been an afterthought, merely justifying decisions already taken. It concluded that RIS requirements needed to be strengthened to reflect the analytical and consultation requirements.'

3.1 The Licensing Regime and Carve-Outs from Any Form of RIS

Of great concern, is that the key legislative provisions introduced into the superannuation industry have been the subject of a series of carve-outs, perfunctory, qualitative only, regulatory impact statements

[39] After agencies inform OBPR about regulatory proposals, OBPR determines whether a RIS is required in accordance with the Handbook. This is usually done through a preliminary assessment form which identifies the key features of the regulatory proposal.

[40] The Taskforce on Reducing Regulatory Burdens on Business, Rethinking Regulation (January 2006) (Banks Taskforce Report), pp i and ii. <http://www.regulationtaskforce.gov.au/finalreport>.

and Ministerial exemptions. Firstly, the carve-out provisions set out in the OBPR's External Guidance Note – Carve-outs (December 2012) define carve-outs as "…a standing agreement between the OBPR and a department or agency that removes the need for a preliminary assessment to be sent to the OBPR for a type of regulatory change – generally minor or machinery changes that occur on a regular basis."

A carve-out is only meant to be used when there are regulatory changes that occur on a regular basis and are minor or machinery in nature. A change is minor where it does not substantially alter the existing regulatory arrangements for businesses or not-for-profit organisations. Machinery refers to changes which are consequential to, and required as a result of, a substantiative regulatory decision, and for which there is limited discretion available to the decision maker. Examples of acceptable carve outs include: routine indexation that uses a well-established formula, such as the Consumer Price Index (CPI); routine indexation of aged care subsidies in line with increases in the CPI; and regularly updating of the listing and price of medicines available under the Pharmaceutical Benefits Scheme.

These carve-out provisions were however applied in relation to the introduction of the *Superannuation Industry (Supervision) Amendment Regulations (200*4), No. 113 which established the key licensing provisions for the superannuation industry, eliminating the necessity for any form of RIS.

As set out in the Explanatory Memorandum for these Regulations:

> "…The Office of Regulation Review has advised that a Regulation Impact Statement (RIS) is not required for the proposed Regulations, as the measures contained in the proposed Regulations have either been adequately addressed in the RIS for the Superannuation Safety Amendment Act (SSAA) or are of a minor or machinery of government nature."

In addition, given the wording of the exemption stated above, the carve-out provisions also allowed the licensing regime to be exempted from any form of post-implementation review.

This treatment of the RSE licensing regime reforms as minor or machinery or as having been adequately addressed within the original RIS related to the introduction of the SSAA legislative enactments stands in stark contrast to the statistical reality of the actual impacts of RSE licensing. That is, these amended regulations related to the Howard Coalition Government licensing of funds reforms which were designed to provide fund members with a safer, more competitive and best practice investment environment and were part of the reforms included in the 2004 *Superannuation Safety Amendment Act* (C'th). The core concept of this enactment was the formal licensing of both trustees and superannuation funds as part of the Registrable Superannuation Entity reforms (RSE reforms) with the licensing of APRA-regulated trustees also being recommended by the Productivity Commission in its April 2002 report on the SIS Act and other superannuation legislation[41].

This licensing regime, which was described 'as the catalyst for far-reaching change',[42] was set out in the initial 'Issues Paper Options for Improving the Safety of Superannuation'[43] which was released by the Federal Coalition Government on the 2nd October, 2001. A Superannuation Working Group (SWG) was put in place by the Federal Government to consider the proposals within this Issues Paper related to the supervision and governance of superannuation entities. This SWG comprised representatives from the

[41] APRA Insight, Issue Two, 'A Recent History of Superannuation in Australia', 2007 at p. 9.
[42] M. Taylor, 'Trustee Licensing – The Big Issue', Super Review, 10th January, 2006.
[43] APRA Insight, Issue Two, 2007, Special Edition, 'A Recent History of Superannuation in Australia' p.8.

Treasury, APRA and ASIC under the chairmanship of a retired senior executive from the financial services sector.

The introduction of RSE licensing for all superannuation funds regulated by APRA, was implemented by 2006 and included ''…substantial additional requirements for RSE licensees, including specific licence conditions relating to the governance and risk management of the RSE licensee's business operations (APRA 2012, at p. 3)." APRA viewed these licensing requirements as necessary however given that:

> '…the compulsory nature of superannuation means that the failure of the market to deliver optimal outcomes for superannuation impacts on almost all superannuation fund members. In a system of mandatory retirement savings where members must be part of the system, RSE licensees and superannuation regulators have an increasing obligation to ensure that confidence in the system is maintained (2012, at p. 3)'.

As highlighted by Clare (2005, at p. 6), licensing ''...will undoubtedly impact on individuals in those [exiting] funds, and, in some instances, force well run funds to exit and reduce the diversity within the industry." This prediction was then supported by the statistics which highlighted that, primarily as a result of the licensing requirements[44], the number of funds has decreased by 91 per cent from 3,720 in June 2001 to 325 funds in December, 2012 (APRA 2013, at p. 11). The number of RSE licensees fell from 225 to 209 over 2011/12, and have fallen further to 199 as at 31 December 2012.[45]

It is therefore also quite clear that the nature of the RSE licensing process regulatory reforms and their potential impacts do not fall within the acceptable carve outs provided by the OBPR which include, as previously highlighted: routine indexation that uses a well-established formula, such as the Consumer Price Index (CPI); routine indexation of aged care subsidies in line with increases in the CPI; and regularly updating of the listing and price of medicines available under the Pharmaceutical Benefits Scheme.

Of further concern is that the initial Regulatory Impact Statement generated for the *Superannuation Safety Amendment Bill* in 2003 which was meant to address the issues relating to licensing, and as detailed in the relevant Explanatory Memorandum, (Circulated by authority of the Minister for Revenue and Assistant Treasurer, Senator the Hon Helen Coonan), restricted the RIA to the two key issues set out in the Government's 2001 Issues Paper which can be summarised as:

- whether the prudential and legislative framework was outdated, inhibiting APRA's ability to identify and respond quickly and effectively to perceived difficulties in superannuation entities; and
- the adequacy of governance, particularly trustee competence, risk management systems and disclosure.

In addition, the options of the RIS were limited to two: Option 1 — Amend the superannuation prudential framework; and Option 2 — No specific action. These options were then based on qualitative assessments only of the costs and benefits of each option for stakeholders such as: APRA; ASIC; ATO; superannuation entity trustees; superannuation entity members; and employer-sponsors with Option One then selected. For example, the costs to fund members were evaluated as:

> '…improved trustee competence and fund governance may be offset by increased compliance costs, which may be passed on to members. The impact on members will vary depending upon the

[44] M. Taylor, 'RSE Licensing Cut Could Be as Low as 310', *Super Review*, 4th July, 2006.
[45] APRA Insight, Issue One, Superannuation Industry Overview, 2013 at p. 10.

size of the entity, and how well it is managed. Trustees who already follow best practice could be expected to face a lower compliance burden to meet the new requirements. Anecdotal evidence from APRA is that trustees of small employer-sponsored funds will need to devote the greatest level of attention to implement new processes, and trustees of these entities are likely to pass on comparatively higher costs to their members, which may impact on members' benefits.'

3.2 APRA Prudential Standards and Weak-Form RIS

The second feature of the superannuation regulatory interventions of concern relate to the recent amendments to the *SIS Act* that provided APRA with prudential standards making power for superannuation. In order to give effect to this Government mandate, APRA argued that they must determine at least four prudential standards (covering risk management, the operational risk financial requirement, conflicts of interest and defined benefit matters) and to ensure that there were no inadvertent gaps in the regulatory framework. However rather than implementing these four prudential standards, APRA implemented a suite of eleven (11) prudential standards for superannuation. The introduction of these additional seven standards were designed to more fully implement the Government's Stronger Super reforms and more effectively align the current requirements for RSE licensees with those that are in place for the banking, life insurance and general insurance industries regulated by APRA.

As highlighted in the RIS prepared by APRA (2012, at p. 17) for this suite of eleven prudential standards:

> "…the introduction of prudential standards for superannuation is aimed at improving the governance standards of a relative minority of RSE licensees. The standards of governance and compliance demonstrated by RSE licensees have improved significantly over the past few years, but there is still some capacity to make incremental improvements within many RSE licensee business operations. There are also a small number of RSE licensees that do not currently have in place governance arrangements that APRA considers to be good practice. APRA's view is that the requirements of the 11 prudential standards will allow APRA to establish and enforce standards within superannuation entities it regulates that will support the management of risks which are ultimately borne by superannuation fund members."

After emphasising that the prudential standard were designed to 'reign in' a small number of funds that did not have 'good practice' governance arrangements in place, in preparing the RIS, APRA felt unable to complete any quantitative analysis for either the costs or benefits associated with the implementation and operation of the standards. This absence of a clear cost/benefit impact existed in spite of APRA acknowledging that the implementation costs by RSE licensees of the prudential standards requirements would ultimately be borne by members of RSEs in the form of higher fees and/or lower investment returns. From APRA's perspective (APRA 2012, at p.9): "…overall, it is not clear how large this cost will be because the Stronger Super reforms are creating an environment with more transparency and comparability of fees and costs, and this competition may lower fees…for this reason, the costs of implementing the prudential standards are not quantified in this RIS."

In terms of benefits for RSE licensees from the introduction of prudential standards, APRA (2012: 7-8) highlights that "…prudential standards provide greater clarity of how the requirements of the SIS Act and SIS Regulations can be met and requirements in prudential standards can be set in a way that is flexible and principles-based which provides freedom for RSE licensees to interpret the requirements in line with the size and complexity of their business operations." APRA has also stated (2012: 10) that the prudential standards will be reviewed "…after their implementation and on an ongoing basis to ensure

they continue to reflect good practice and remain relevant and effective, for both APRA's prudential supervision purposes and for regulated institutions."

Of great concern then with these RIS processes and the lack of quantitative evidence to support either the introduction of the licensing regime or the prudential standards, is their inability to meet the stated objective for RIA. That is, as set out in the Business Council of Australia's (BCOA, 2012, at p. 2) statement:[46]

> '...governments come to power with an objective to improve the wellbeing of Australians and to set policies they consider to be in the national interest. They have to make difficult choices about how they tax, regulate and spend or invest funds on behalf of taxpayers in order to deliver economic, social and environmental outcomes that will improve the lives of citizens. Evidence is crucial to good government policy outcomes because it helps policymakers work out which policy options are likely to achieve the best results."

3.3 Granting of Exemptions to the Cooper Review

An additional aspect of concern relates to the granting of exemptions by Treasury for the Federal Government's Stronger Superannuation Reforms and in terms of the Federal Government's Response to the Super System (Cooper) Review as outlined in the 2012 Independent Review Report (at p. 99). The exemption granted for the Stronger Superannuation Reforms was provided by the Prime Minister and related to the removal of any requirements for a regulatory impact analysis in relation to the ability of funds to offer tailored MySuper products to employees with more than 500 employees.

3.4 The Absence of a Publicly-Available RIS for the Superannuation Industry (Supervision) Act 1993 (SIS Act) and an Eight Year Lag in a Post-Implementation Review Process

It is also important to note that the absence of any available data on any form of RIS that has been conducted on the key legislative reforms introduced as part of the *Superannuation Industry (Supervision) Act 1993*, which continues to form the basis of the regulatory framework for superannuation in Australia. In addition, while a national program of review and reform of existing legislation which potentially restricts competition was commenced in 1996 and which was required to be completed by 31 December 2000, the review of superannuation related legislation such as the *SIS Act*, did not take place until 2001. This represented an eight year delay in any form of post-implementation review process.[47] Further, the Federal Government did not respond to the PC's 2001 review comments until 2003 – a further two year delay in the post-implementation review process.

[46] Business Council of Australia (2012), 'Familiarisation of the cost benefit analysis framework', Deloitte Access Economics.

[47] Productivity Commission 2001, Review of the Superannuation Industry(Supervision) Act 1993 and Certain Other Superannuation Legislation, Report - No. 18, AusInfo, Canberra.