



Submission to Treasury with respect to the April 2013 Discussion Paper on Financial Industry Supervisory Levy Methodology

30 April 2013

The Association of Superannuation Funds of Australia Limited – ABN 29 002 786 290
ASFA Secretariat
PO Box 1485, Sydney NSW 2001
T 02 9264 9300 (1800 812 798 outside Sydney)
F 1300 926 484
W www.superannuation.asn.au

* * * *

About ASFA

ASFA is the peak policy, research and advocacy body for Australia's superannuation industry. It is a not-for-profit, sector-neutral, and non-party political national organisation whose aim is to advance effective retirement outcomes for members of funds through research, advocacy and the development of policy and industry best practice.

ASFA's focus is on whole of system issues and its core strategies are aimed at encouraging industry best practice, advocating for a system that plays a productive role in the Australian economy and ensuring the industry delivers on its primary purpose of delivering decent retirement incomes.

Our membership - which includes superannuation funds from the corporate, industry, retail and public sectors, and, through its service provider membership, self-managed and small APRA funds - represents over 90 per cent of Australians with superannuation.

* * * *

Should you have any queries regarding the contents of this submission, please do not hesitate to contact me on (03) 9225 - 4021 or 0431 490 240 or fgalbraith@superannuation.asn.au.

Yours sincerely



Fiona Galbraith
Director, Policy

Table of Contents

1.	Introduction	4
2.	Summary of ASFA's positions	5
3.	Ensuring costs incurred are justifiable	7
4.	Accountability \ transparency of determination of costs	9
5.	Financial industry supervisory levy methodology - discussion paper	12
6.	Financial assistance funding levy	22

1. INTRODUCTION

RSE licensees will pay over \$180 million this year in supervisory levies. This represents an increase of some \$134 million over the 2011 – 2012 levies.

Significantly, 67% of the 2012 – 2013 levy payable by superannuation fund members is attributable to the new SuperStream component of the levy.

Given that this is money which could otherwise have been attributed to member accounts, it is critical that all of the agencies who receive the levy are accountable for the costs and expenditure they incur.

In particular it is important that: -

1. the costs incurred are justifiable: -

- the nature, scope and timing of activities, and the method of performing these activities, are warranted by the likelihood and consequence of the risk being regulated \ supervised; and
- the costs are reasonable;

2. there is transparency and accountability with respect to the activities undertaken and the costs incurred; and

3. the supervisory levy methodology is appropriate: -

- the nature \ type of costs to be recovered from a particular industry are appropriate to be recovered by way of a levy, as opposed to being funded out of consolidated revenue;
- the costs are, directly or indirectly, with respect to the regulation and supervision of the relevant industry;
- the quantification of costs, and their allocation to the various industries, is done on an appropriate and reasonable basis, thereby ensuring that the maximum amount levied is at most equivalent to, but does not exceed, the reasonable costs incurred by the other who receive the levies with respect to the relevant industry; and
- the amount of the levy is determined on an equitable and reasonable basis after appropriate consultation.

While the “Financial industry supervisory levy methodology” discussion paper released by Minister Shorten and the Treasury Department in April 2013 (the “Discussion Paper”) is focussed on the third aspect – the supervisory levy methodology – this cannot be done in isolation from considerations with respect to whether the costs are justifiable and there is transparency and accountability with respect to these costs.

This submission will address the issues as to the incurring of costs and whether there is adequate transparency and accountability with respect to costs, before turning to address the Discussion Paper and the consultation issues asked therein.

2. SUMMARY OF ASFA POSITIONS

1. It is ASFA's view that the levy process should be as transparent as possible, through adequate disclosure and appropriate consultation (section 3.2).
2. APRA should publish a cost recovery policy as soon as possible (section 4.2.1.1).
3. ASFA supports the publication of a comprehensive CRIS by APRA with respect to the financial sector levies it receives (section 4.2.1.2).
4. ASFA supports the ANAO's comprehensive audit of APRA's activities, expenditure and its allocation of costs to industries and to the restricted \ unrestricted components of the levy calculations (section 4.2.1.2).
5. ASFA submits that consideration should be given to making the production of CRISs mandatory for agencies who receive more than \$5 million per annum through levies, with sanctions if the CRIS is not produced or is not sufficiently detailed (section 4.2.1.2).
6. ASFA supports the publication of a comprehensive CRIS by ASIC with respect to the financial sector levies it receives (section 4.2.2).
7. A CRIS produced by ASIC should ensure that functions performed with respect to:
 - regulated superannuation funds;
 - self-managed superannuation funds;
 - managed investment schemes; and
 - financial adviceare identified separately, with only the first category subject to a super levy (section 4.2.2).
8. The funding of the SCT should be separate from the funding provide to ASIC (section 4.2.2).
9. If the SCT is not to have separate funding, then at a minimum there should be full and transparent disclosure of the amounts allocated to the SCT and the basis on which it is determined (section 4.2.2).
10. ASFA submits that the ATO should undertake release its comprehensive costing of the SuperStream initiative (section 4.2.3).
11. ASFA submits that SuperStream should be subject to audit by the ANAO and ongoing review (section 4.2.3).
12. ASFA submits that the determination of direct salary costs attributable to each levy-paying industry should not be performed on the basis of time alone but actual salary costs incurred (section 5.1.1)
13. ASFA submits that consideration should be given to the appropriate method for allocating indirect costs. In ASFA's view a "head count" model may be appropriate (section 5.1.2).
14. ASFA agrees with the conceptual basis for imposing a minimum and maximum amount with respect to the restricted, supervisory component, as a number of the costs of prudential supervision are fixed and those which are variable are not in direct proportion to fund assets (section 5.3.1).
15. ASFA submits that consideration should be given to whether asset value continues to be the most appropriate basis for allocating the levies (section 5.3.1).

16. ASFA submits that care must be taken to ensure that the minimum and maximum are determined on an appropriate and equitable basis. Accordingly, there needs to be a methodology underpinning the basis upon which the minimum and maximum amounts are set each year (section 5.3.1).
17. ASFA is of the view that the minimum and maximums should strive to reflect the actual minimum and maximum costs of supervising entities in the relevant industries (section 5.3.1).
18. ASFA submits that it is necessary for the methodology to make a distinction between superannuation funds and PSTs (section 5.3.1).
19. Where a PST is 100% “owned” by a superannuation fund it should be recognised that the PST will be supervised as part of the supervision of the fund and ideally the PST should not be subject to a separate levy or it should be a very small one (section 5.3.1).
20. PSTs which are invested in by multiple funds should attract a specific PST levy – at a rate significantly lower than superannuation funds (section 5.3.1).
21. ASFA supports that the costing of the LMR function should take place and suggest that it be subject to continual audit and review, to ensure that the LMR function is performed as efficiently as possible (section 5.4.1.1).
22. ASFA welcomes the DHS \ APRA review of the early release activities and the intention to create efficiencies and thereby reduce costs and future levies (section 5.4.1.3).
23. ASFA submits that consideration should be given to levying the SuperStream component on a per capita basis, as opposed to a levy based on assets (section 5.4.1.4).
24. ASFA submits that a detailed analysis be undertaken to ascertain who will benefit from SuperStream, prior to determining the extent to which costs should be recovered from superannuation funds and the most equitable method of apportioning the costs between them (section 5.4.1.4).
25. ASFA submits that in 2012 – 2013 the SuperStream levy should have been allocated to the unrestricted component (section 5.4.2).
26. ASFA submits that consideration should be given to increasing the maximum amount by a factor reflecting the percentage increase in supervision costs in the past year (section 5.4.3.1).
27. ASFA submits that a maximum amount of the unrestricted component of \$2 million in 2012 – 2013 is unsupportable as an amount representing the costs of supervision, which is in direct contravention of the principles underpinning the concept of cost recovery (section 4.5.3.1).
28. ASFA submits that, with respect to the financial assistance levy, that the most equitable method to apportion the costs of financial assistance is either to apply a:
 - percentage across the assets of funds, with no minimum \ maximum; or
 - fixed dollar amount with respect to each member of the fund (section 6).

Overall conclusion

Given the lack of transparency about the process and the length of time since the initial parameters were set, that a thorough review of the levy determination process be performed. One possibility may be that the Productivity Commission review the basis on which the levies are determined, including the underlying methodology utilised.

3. ENSURING COSTS INCURRED ARE JUSTIFIABLE

3.1. Moral Hazard

The most significant aspect of agencies being primarily funded by levies is that it represents a form of moral hazard, in that the party which is providing the funding (industry) has no control over the resourcing decisions made by the agencies. This extends to the type, and in particular the scope, of activities engaged in by the agency and the quantum, and nature, of the resources used.

Good practice with respect to funding has a rigour about it, which necessitates having to perform a cost \ benefit analysis and prepare a business case, which thereby imposes a fiscal discipline on the parties concerned. If costs can simply be recovered by the imposition of a levy the agencies are relatively unconstrained as to the approach they can take, the scope and size of any project \ activity they undergo and, accordingly, the costs they incur.

3.2. The Supervisory Levy Imposition Bills

The Explanatory Memorandum to the various Supervisory Levy Imposition Bills in 1998, in the Regulatory Impact Statement in Chapter 3, stated as follows (emphasis added): -

“3.4 The aim is to establish an administratively simple and uniform funding scheme, reflecting the principles of equity, efficiency and competitive neutrality, that is the scheme will not create a relative cost disadvantage to any one category of institution covered.

3.5 The FSI recommended that regulatory agencies’ charges should reflect their costs ... and advised that, in the interests of equity and efficiency, the costs of financial regulation should be borne by those who benefit from it and that the agencies should not overcharge.

.....

*3.7 Furthermore, [not imposing a charge on financial institutions] would be a basic departure from the approach adopted to date and **would not satisfy the principle of efficiency since there is no link between the intensity of supervision and the cost of providing it.** Other considerations include that it **might reduce the incentive for the industry to seek to have supervision carried out in a cost effective manner**, and would subject the agency to the uncertainty associated with direct funding from the Commonwealth budget.*

.....

*3.10 ... “Levy on financial institution] may also tend to **encourage the institutions paying the levy to act as a constraint on empire building or other excessive cost increases on the part of the regulator**”.*

The corollaries to the first two highlighted statements are that: -

- imposing a charge on financial institutions would satisfy the principle of efficiency since there would be a link between the intensity of supervision and the cost of providing it; and
- imposing a levy might increase the incentive for the industry to seek to have supervision carried out in a cost effective manner;

while the third statement is that: -

- a levy on a financial institution may also tend to encourage the institutions paying the levy to act as a constraint on empire building or other excessive cost increases on the part of the regulator.

It can be argued that the extent to which the industry is able to: -

- affect \ influence the intensity of supervision (given that it is prudential supervision);
- seek to have supervision carried out in a cost effective manner; or
- act as a constraint on empire building or other excessive cost increases on the part of the regulator

realistically may be relatively limited in practice.

Notwithstanding this, it is ASFA's view the levy process should aspire to make this as achievable as possible through adequate disclosure and appropriate consultation.

3.2 It is ASFA's view that the levy process should be as transparent as possible, through adequate disclosure and appropriate consultation.

There needs to be effective oversight, checks and balances and controls to ensure that the activities performed, the resourcing utilised and the resultant costs incurred are appropriate and reasonable. Currently there is little in the way of transparency and accountability.

As such, the industry holds concerns about the absence of information with respect to the costs being recovered by the levies.

4. ACCOUNTABILITY \ TRANSPARENCY OF DETERMINATION OF COSTS

4.1. Department of Finance and Deregulation Guidelines

The Government first established a formal cost recovery policy in December 2002 to improve the consistency, transparency and accountability of cost recovery arrangements and promote the efficient use of resources. To this end, the Government reissued the Australian Government Cost Recovery Guidelines (“Guidelines”), administered by the Department of Finance and Deregulation (“DFD”), in July 2005 and we note that the DFD is currently reviewing the guidelines.

These Guidelines, amongst other things, stipulate that entities which receive at least some of their funding by means of the imposition of “cost recovery” levies, in excess of \$5 million per annum, should: -

- develop and publish policies with respect to cost recovery; and
- periodically publish a “Cost Recovery Impact Statement” (CRIS).

4.2. Compliance with DFD Guidelines in practice

4.2.1. APRA

4.2.1.1. Publication of policy with respect to cost recovery

It does not appear as though APRA has published a policy with respect to cost recovery. Given that APRA is primarily funded through levies, and has been for some years, this is a concern.

4.2.1.1 APRA should publish a cost recovery policy as soon as possible.

4.2.1.2. CRIS

The Treasury undated document “Proposed Financial Industry Levies for 2012 – 13” (“Consultation Paper”) stated that in 2012 – 2013 APRA would merge its current levy review process with the development of what would be its initial CRIS and would continue to consult with industry on the development of the CRIS.

Despite the fact that: -

- the guidelines commenced over a decade ago;
- they indicate that a CRIS should be published whenever a review is performed, arrangements change or there is a new arrangement; and
- APRA is primarily funded through levies

it appears as though the only CRIS which APRA may have produced is with respect to assessing applications by entities to be authorised to provide one or more financial services.

This is of concern, especially as it is members of superannuation funds who ultimately fund the payment of these levies. Given that superannuation is legislatively mandated, and not discretionary, APRA’s failure to produce a CRIS with respect to financial levies (other than applications) is less than ideal.

4.2.1.2 (a) ASFA supports the publication of a comprehensive CRIS by APRA with respect to the financial sector levies it receives.

4.2.1.2 (b) ASFA supports the ANAO’s comprehensive audit of APRA’s activities, expenditure and its allocation of costs to industries and to the restricted \ unrestricted components of the levy calculations.

4.2.1.2 (c) ASFA submits that consideration should be given to making the production of CRISs mandatory for agencies who receive more than \$5 million per annum through levies, with sanctions if the CRIS is not produced or is not sufficiently detailed.

4.2.2. ASIC's compliance with the Guidelines

ASIC has published cost recovery FAQs and a CRIS with respect to its 1 January 2012 to 30 June 2013 market supervision function. It does not appear to have published a CRIS with respect to its functions other than market supervision, such as consumer protection, regulatory and enforcements activities.

Of particular importance with respect to ASIC is that: -

- functionally within ASIC, superannuation is combined with managed investments – it is critical to ensure that superannuation funds only pay levies with respect to consumer protection within superannuation and not with respect to managed investments;
- similarly, it is important to distinguish between activities with respect to: -
 - self-managed super funds; and
 - financial advisers \ financial plannersas neither of these pay levies and activities with respect to them should not be funded by levies paid by regulated superannuation funds;
- there is complete transparency with respect to the funding of the Superannuation Complaints Tribunal (“SCT”). As the SCT is an independent Tribunal, best practice would dictate that its funding should be entirely separate from the funding provide to ASIC. If the SCT is not to have separate funding, then at a minimum there should be full and transparent disclosure of the amounts allocated to the SCT and the basis on which it is determined.

4.2.2 (a) ASFA supports the publication of a comprehensive CRIS by ASIC with respect to the financial sector levies it receives.

4.2.2. (b) A CRIS produced by ASIC should ensure that functions performed with respect to: -

- * regulated superannuation funds;
- * self managed superannuation funds
- * managed investment schemes; and
- * financial advice

are identified separately, with only the first category subject to a superannuation levy.

4.2.2 (c) The funding of the SCT should be separate from the funding provide to ASIC.

4.2.2 (d) If the SCT is not to have separate funding, then at a minimum there should be full and transparent disclosure of the amounts allocated to the SCT and the basis on which it is determined.

4.2.3. ATO's compliance with the Guidelines

With respect to the SuperStream levy of \$467 million - little in the way of information or a break-down of costs has been published.

In particular, the imposition of the new SuperStream component in 2012 – 2013 represented a new arrangement, or a material amendment to an existing arrangement, and in either case would have necessitated a CRIS being prepared prior to the arrangement or change being introduced.

Given the sheer magnitude of this levy – especially in light of the fact that the DFD Guidelines have a \$5 million threshold - it is reasonable for the industry to expect detailed information with respect to the various activities being performed, the anticipated deliverables, the basis upon which expenditure has been incurred and a breakdown of past and anticipated costs. This has not been forthcoming.

There has been no consultation with the superannuation industry in relation to the proposed ATO expenditure on SuperStream and the precise nature and scope, and resourcing requirements, of the deliverables that the levies will be funding. Very little information has been published.

In particular, the imposition of the new SuperStream component would represent a new arrangement, or a material amendment to an existing arrangement, which in either case would necessitate a CRIS being prepared.

4.2.3 (a) ASFA submits that the ATO should undertake release its comprehensive costing of the SuperStream initiative.

4.2.3 (b) ASFA submits that SuperStream should be subject to audit by the ANAO and ongoing review.

4.2.4. DHS's compliance with the Guidelines

It does not appear as though the DHS levy has yet exceeded the \$5 million threshold necessitating the publication of cost recovery guidelines or a CRIS.

5. FINANCIAL INDUSTRY SUPERVISORY LEVY METHODOLOGY

It is critical to ensure that only appropriate \ relevant costs are recovered through levies and that they are recovered on an equitable basis.

5.1. General principles – quantification\attribution of costs to industries

In a cost recovery regime it is critical that costs are accurately quantified and allocated appropriately.

There are two main aspects to this: -

- capturing direct costs accurately; and
- allocating indirect costs on an appropriate basis.

5.1.1. Direct costs - the salary cost with respect to each industry

In our view this should be determined by: -

- ascertaining the time spent by each employee during the financial year on activities directly related to each of the levy paying industries;
- multiplying the time spent on each industry by the mean (for that year) of the total cost of employment for that employee.

Determination of direct salary costs should not be performed based on time alone and not the actual salary costs. The actual costs will vary depending on the relative seniority of the staff concerned and whether overtime is payable. Allocation based on time does not necessarily reflect costs incurred.

If overtime is payable then any direct salary cost calculation should utilise the total time spent on activities for a particular industry, loaded to reflect the applicable overtime rate. If overtime is not payable then any direct salary cost calculation should be determined based solely on the “standard” units of time (e.g. 7.5 hours per day) for which the employee is remunerated, irrespective of the time actually spent.

The direct salary cost of each employee with respect to each industry would then be totalled, to determine the total direct salary cost for each industry. This would represent the direct cost component to be borne by that industry.

5.1.1 ASFA submits that the determination of direct salary costs attributable to each levy-paying industry should not be performed based on time alone but actual salary costs incurred.

5.1.2. Indirect costs

ASFA’s view is that the indirect costs of regulating the superannuation industry could be determined by one of three possible methods: -

- allocating indirect costs on a pro-rata “per capita” basis (i.e. on the basis of “head count”)(“Head Count Model”);
- apportioning indirect costs on the basis of the proportion that the industry’s direct salary costs bears to the total agency’s relevant costs (“Salary Proportioning Model”); or
- full activity based costing.

5.1.2.1. Head Count Model

Under this model the indirect expenditure of the agency would be allocated based on the number of employees with respect to whom all, or the majority, of their time is spent with respect to each industry. Given the nature of indirect costs, allocating them on a “per capita” basis (ignoring, for example, if an employee is part-time or the salary of the employee) frequently produces an equitable outcome.

A number of indirect costs, such as HR \ Finance \ IT \ rental \ workspace etc, are more fixed in nature than variable. As such, these costs tend to relate more to the number of employees and not necessarily to the number of hours that each employee works or their salary level.

5.1.2.2. Salary Proportioning Model

Another possible costing model would allocated indirect costs based on applying the proportion represented by each industry’s total direct salary costs against the total relevant costs of that agency.

Firstly, the direct salary costs for each industry would be totalled and the relative proportion of each industry determined. The proportion of each industry’s direct salary costs would be applied against the total relevant agency cost to determine the quantum of costs to be borne by each industry.

5.1.2.3. Activity based costing

A final alternative would be activity based costing.

In addition to establishing the cost basis for levies, this method may have the further advantage of documenting both the types of activities engaged in, and the amount of time spent on, each activity. In that this could in turn facilitate analysis of the nature, scope and timing of the activities engaged in by the agency, such information could potentially assist both the government, the agency and the industry in assessing whether the agency was allocating and utilising resources efficiently and delivering on its public policy outcomes in an effective manner.

Having said that, given that: -

- the majority of APRA’s costs are salary and wages (we believe about 80%);
- the majority of APRA staff are allocated to a particular industry, with relatively few performing “corporate” functions;
- the demands of each industry on “corporate” services are likely to be broadly in proportion to the number of staff who in are engaged in regulating that industry; and
- the costs of developing, maintaining and utilising an activity based costing system can be considerable

it would appear that any benefits at the margins might be outweighed by the costs.

5.1.2 ASFA submits that consideration should be given to the appropriate method for allocating indirect costs. In ASFA’s view a “head count” model may be appropriate.

5.2. Last Review of financial sector levies in June 2009

A review of the financial sector levies was last performed in June 2009. The Review focussed largely on specific issues about the methodologies and some operational issues, as opposed to a performing a fundamental examination of the levy system.

Amongst other things the report recommended that: -

1. *That **(subject to the recommendations below)** the current framework for setting financial sector levies be maintained.*
2. *That the current reporting accountability of APRA in relation to the imposition and collection of levies generally should not be changed. ... However, as part of the annual consultation process, **APRA will provide more detailed information on the allocation of costs and levy recovery to improve the transparency of the levy arrangements.***
3. ***That the minimum and maximum restricted levy arrangements for each sector be maintained** - there is sufficient capacity within existing caps to fine tune the amounts imposed. The statutory upper limits (which cap the maximum restricted levy amount) should continue to automatically increase annually in line with the indexation factor specified within the imposition Acts.*
4. *That the recommendation of the 2004 review that the notional ratio of the unrestricted component of levy to the total levy be between 10 per cent and 30 per cent be removed in relation to the 2009-10 and subsequent years.*
5. *That the valuation date for ADIs, general insurers, life insurers and friendly societies and superannuation funds not be changed.*
6. a) *That the levy date for new starters should be redefined and a new starter return be introduced.*
7. *Total assets should remain the base for most financial sector levies, subject to Recommendation 9. ... The Review further recommends that a more extensive review of the valuation basis be carried out at the next review.*
8. ...
9. ***That the imposition legislation be amended to provide more flexibility so that a valuation basis other than assets can be used on a case by case basis in the annual determinations.***
10. ...
11. *That no change in levy structure should be made to the levies for regulated institutions within conglomerate groups.*
12. *That no change should be made to the levy structure for Pooled Superannuation Trusts (PSTs). ... **This levy category should be re-examined at the next methodological review.***
13. ***That a further review of the levies framework be carried out within four years.***

5.3. April 2013 Discussion Paper re methodology – consultation issues

In ASFA's view the basis for the determination of the amount of the levy should strive to achieve equity both between different industries and between entities of different sizes.

With respect to the financial industry supervisory levy, ASFA has some concerns with respect to both: -

- the legislative formula for the determination of the levy; and
- the basis upon which the levy percentages, minimum and maximum levy amounts have been determined in practice.

Turning to the specific consultation issues raised in the Discussion Paper: -

6.1 Is the current setting for restricted (supervisory) and unrestricted (systemic) levy amounts appropriate? Are the current minimum and maximum restricted levy parameters appropriate?

The levies framework consists of two components, based on: -

- cost of supervision (restricted component);
- system impact (unrestricted component).

5.3 (a) ASFA agrees with the conceptual basis for imposing a minimum and maximum amount with respect to the restricted, supervisory component, as a number of the costs of prudential supervision are fixed and those which are variable are not in direct proportion to fund assets.

Care must be taken, however, to ensure that costs are allocated appropriately and that the minimum and maximum for the restricted component and the rates for both components are determined on an equitable basis.

ASFA is concerned that, with respect to the 2012 – 2013 year, the special SuperStream amount of \$121.5 million (more than the amount of the APRA component of the levy) was included in the restricted component, notwithstanding that it is nothing to do with the cost of supervision and is instead properly characterised as being with respect to system impact.

Furthermore, ASFA is concerned that it appears as though the apportionment between the components is based on time alone and not salary costs. The actual costs will vary depending on the relative seniority of the staff concerned and whether overtime is payable.

Section 6.1 of the Discussion Paper refers to “the financial **costs** APRA incurs in undertaking supervisory work relating to the institutions being levied” (emphasis added). Allocation based on time does not necessarily reflect actual costs incurred.

The Discussion Paper at section 4.1 states that “[t]he levy allocation methodology is designed to fully recover the costs from each industry sector and minimise cross-subsidies across sectors”. There is nothing inherent in the methodology which ensures this – what is critical is the determination and allocation of costs on an appropriate basis.

The Discussion Paper goes on to state that “[t]he estimated asset value of each institution is used as a basis for allocating the quantum of the sectoral levy to each regulated institution”. While historically this was considered to be the most appropriate basis, recent thinking is that a mix of a percentage of assets and a per capita measure (i.e. number of members) may yield a more equitable outcome.

5.3 (b) ASFA submits that consideration should be given to whether asset value continues to be the most appropriate basis for allocating the levies.

The Discussion Paper states at section 6.1 that “[a]ny changes to the existing levy model would have distributional consequences, potentially with different effects on different industries and different sized institutions”. While this is true, nevertheless the mere fact that there may be distributional changes as a result of changes to the levy model does not mean that, if they are warranted on equitable or other grounds, they should not be made.

The Discussion Paper goes on to state that “APRA’s activities **and the time spent on them** are broadly broken down into the cost of supervision (the restricted component) and the systemic impact (the unrestricted component). Each component is then apportioned across the different industries based on the **total resources** APRA expects to dedicate to each industry”. This appears to be inconsistent as the initial breakdown appears to be based on **time spent** while the apportionment is based on **resources used**. In ASFA’s view both should be done on the basis of resources used.

The Discussion Paper in section 6.1 goes on to states “[t]o ensure continued vertical equity in the levy applied to individual institutions within a sector, adjustments to the minimum and maximum parameters for the restricted levy component are made annually following industry consultation. These adjustments are designed to support an equitable sharing of the levy burden within each industry sector”.

The 2012 – 2103 Consultation Paper merely proposed increasing the maximum amount from \$260,000 to \$1 million to accommodate the separate SuperStream component (which should not have been allocated to the restricted component in any event). No basis was stated for this approach. Instead the Consultation Paper merely provided different scenarios and presented comparisons of the impact of funds of differing asset values. The determination of the maximum was on an apparently arbitrary basis, with no justification as to how the proposed \$1 million, or final \$2 million, was determined.

ASFA agrees that the introduction of the unrestricted levy component in 2005-06 sought to resolve issues regarding vertical equity. With no cap on the unrestricted levy component larger institutions are subject to a higher levy amount.

The Discussion Papers at section 6.1 asks “*whether the minimum and maximum caps are broadly equitable to entities within each industry sector*”. ASFA agrees with the conceptual basis for making the distinction between the two types of activities. A minimum and maximum with respect to the restricted component relating to supervision makes sense – a number of the costs of prudential supervision are fixed and those which are variable are not in direct proportion to fund assets.

Care must be taken, however, to ensure that the minimum and maximum are determined on an appropriate and equitable basis.

5.3 (c) ASFA submits that care must be taken to ensure that the minimum and maximum are determined on an appropriate and equitable basis. Accordingly, there needs to be a methodology underpinning the basis upon which the minimum and maximum amounts are set each year.

The Discussion Paper goes on to state that “*[i]deally, the band width between the minimum and maximum should be such that few institutions pay the minimum and few pay the maximum. In this manner, increases in funding requirements fall evenly across those paying the marginal levy rate. The minimum levy typically applies to either a new entrant or a comparatively dormant institution. The maximum levy typically applies to the largest institutions*”.

5.3 (d) ASFA is of the view that the minimum and maximums should strive to reflect the actual minimum and maximum costs of supervising the entities in the relevant industries.

6.2 *Is the current levy base appropriate for each industry sector?*

The Discussion Paper at section 6.2 states “[t]he current base used for the calculation of a levy is the asset value, as at 30th June ... of the regulated superannuation funds”.

ASFA has no concern with respect to the use of the 30 June date.

6.3 *Is the levy structure appropriate for regulated institutions within conglomerates?*

ASFA agrees with the conclusion of the 2008-09 financial industry supervisory levy review that “*the individual institutions that make up a conglomerate require supervision both jointly and individually with little reduction in the overall work of APRA*”.

6.4 *Does the current levy methodology provide adequate transparency and is it appropriate for industry sub sectors?*

The Discussion Paper states that “*Further transparency of the process is achieved by ... a Cost Recovery Impact Statement (CRIS), prepared following the outcome of this levy methodology review*”.

We are concerned that, despite the DFD Guidelines, it would appear that the entities which are receiving annual levies in excess of \$5 million have not produced a CRIS with respect to them.

6.5 Should the current levy methodology take into account reinsurance recoveries and the resultant impact on the levy calculation [based on asset value] for general insurers?’

Not applicable to the superannuation industry.

6.6 Is the current levy methodology appropriate for pooled superannuation trusts?

ASFA shares the concern of some trustees of PSTs with respect to the assets being used in calculating the levy for each of the investing funds including assets invested in a PST, which are used again in calculating the PSTs’ levy. To the extent that this occurs it represents double counting. This results in members of funds invested in PSTs paying the levy twice – one in respect of the assets being counted towards fund assets and again in respect of the assets in the PST.

ASFA disagrees with the conclusion of the 2008-09 financial industry supervisory levy review that “PSTs require supervision by APRA and adequate mechanisms are in place within the imposition Acts to address any special cases where waiving of the levy is justified”.

Sub-section 7(4A) of the *Superannuation Supervisory Levy Imposition Act 1998* (pursuant to which the annual Determination is made) provides that a determination may make different provision for different classes of superannuation entity.

The need for this is especially pronounced in the case where the levy is used to fund costs other than those of APRA – in particular the costs of other agencies i.e. ATO, ASIC and DHS. A PST is likely not to have retail investors (ASIC) and does not necessitate the involvement of the ATO (LMR and SuperStream) or the DHS (early release).

It should be noted in this context that PSTs are not “regulated superannuation funds” but are superannuation entities.

The 2012 – 2013 Consultation Paper referred to the temporary SuperStream levy – appropriately – only being applied to superannuation funds. This statement – that the levy would only be applied to fund - was relied upon by the industry.

The final *Superannuation Supervisory Levy Imposition Determination 2012*, however, applied to all superannuation entities, including PSTs. This produced a manifestly different – and inequitable - outcome to that outlined in the Consultation Paper – especially considering that PSTs will not benefit in any way from SuperStream.

5.3 (e) ASFA submits that it is necessary for the methodology to make a distinction between superannuation funds and PSTs.

5.3 (f) Where a PST is 100% “owned” by a superannuation fund it should be recognised that the PST will be supervised as part of the supervision of the fund and ideally the PST should not be subject to a separate levy or it should be a very small one.

5.3 (g) PSTs which are invested in by multiple funds should attract a specific PST levy – at a rate significantly lower than superannuation funds.

5.4. Methodology in practice - 2012 - 2013 Supervisory Levy Determination

5.4.1. Determination of agency components

5.4.1.1. ATO

Funding from levies collected from the superannuation industry included a component to cover the expenses of the ATO in administering the Superannuation Lost Member Register (“LMR”). We note that, partially in response to the ANAO’s 2011 report on the administration of the LMR, the ATO now undertakes costing of the LMR function.

5.4.1.1 ASFA supports that the costing of the LMR function should take place and suggest that it be subject to continual audit and review, to ensure that the LMR function is performed as efficiently as possible.

5.4.1.2. ASIC Component

A component of the levies is to cover ASIC expenditure with respect to consumer protection, regulatory and enforcement activities relating to financial products. ASIC funding currently includes the SCT.

In 2012 – 2013 the ASIC component includes an amount for the continuation of work supporting the Stronger Super – MySuper initiative.

Costs with respect to functions performed relating to: -

- regulated superannuation funds;
- the SCT;
- self-managed superannuation funds;
- managed investment schemes; and
- financial advice

were not separately identified.

5.4.1.3. DHS Component

A component of the levies was to fund the administration of application for the early release of benefits on compassionate grounds.

We note that Consultation Paper indicated that the DHS and APRA would conduct a review of the early release activities with the intention of leveraging off DHS’s operational scale and infrastructure to reduce future levies.

5.4.1.3 ASFA welcomes the DHS \ APRA review of the early release activities and the intention to create efficiencies and thereby reduce costs and future levies.

5.4.1.4. SuperStream Component

In 2012 – 2013 it was announced that the full costs of the SuperStream implementation, estimated to be some \$467 million in total, will be recovered through the superannuation industry levies from 2012 - 2013 to 2017 - 2018 inclusive.

The Consultation Paper chose to indicate that the cost of the levy in 2012 - 2013 as being roughly in the order of \$4 per account, a per capita concept, however, the levy was actually determined based on fund assets. With respect to SMSFs, SuperStream associated cost are being recovered based on a flat dollar amount per fund.

5.4.1.4 (a) ASFA submits that consideration should be given to levying the SuperStream component on a per capita basis, as opposed to a levy based on assets.

Little was provided in the way of detail as to the SuperStream costs, other than a break-down into four high level deliverables, broken down further into the IT and non - IT costs for each deliverable. While we acknowledge that assurances have been given that the internal government processes have been robust, more information is required.

Given the magnitude of the SuperStream component of the levy, the industry is concerned at the absence of consultation with industry with respect to whether the nature and extent of the costs incurred was appropriate in the first place. We are also concerned that, despite repeated requests, there has been a paucity of information disclosed to date.

ASFA submits that significantly more information with respect to SuperStream is necessary before any kind of meaningful analysis and assessment as to the reasonableness of the costs and their allocation to industry can be made. This is necessary to ensure that SuperStream is designed and implemented as efficiently as possible.

At least some of the benefits of implementing SuperStream will flow to employers, payroll providers, SuperStream gateway providers, clearing houses and hubs, SMSF funds and their providers and even to government. As such, it is unclear why all of the costs should be borne by superannuation fund members.

5.4.1.4 (c) ASFA submits that a detailed analysis be undertaken to ascertain who will benefit from SuperStream, prior to determining the extent to which costs should be recovered from superannuation funds and the most equitable method of apportioning the costs between them.

5.4.2. Allocation to components

In ASFA's view the basis for the determination of the amount of the levy should strive to achieve equity between industries and between entities of different sizes within those industries.

We have some concerns about the transparency of the underlying rationale and methodology employed to allocate amounts to components and to determine the minimum and maximum amounts in any given year.

A matter of general concern to ASFA with respect to the use of the components is that it appears as though the apportionment between the components may have been on the basis of time alone and may not reflect direct salary costs. The actual costs will vary depending on the relative seniority of the staff concerned and whether overtime is payable. We consider that the apportionment should occur based on costs incurred, not time spent.

More importantly, a significantly area of concern was the apparent apportionment of non-supervision costs into the restricted component. Given the underlying policy rationale for the two components, and the imposition of minimums and maximums on the restricted component, the inclusion of non-supervision costs in the restricted component was inappropriate and led to a distortion in the impact of the levy and inequitable outcomes.

Specifically with respect to the 2012 - 2013 year, ASFA is concerned that the SuperStream costs were allocated to the restricted component and the maximum cap on the restricted component was increased to accommodate the SuperStream levy. As the SuperStream levy in no way relates to supervision, it should have been allocated to the unrestricted component.

5.4.2 ASFA submits that in 2012 – 2013 the SuperStream levy should have been allocated to the unrestricted component.

5.4.3. Methodology \ Rationale

ASFA notes with concern that the Consultation Paper failed to provide any underlying rationale or details as to the methodology which was employed to determine the minimum \ maximum amounts and the percentage scales.

5.4.3.1. Determination of minimum and maximum amounts

Both the Consultation Paper and the undated final paper stated that – to ensure continued vertical equity – adjustments to the maximum parameters for the restricted levy component are made annually.

The Consultation Paper proposed increasing the maximum amount in 2012 – 2013 from \$260,000 to \$1 million to accommodate the separate SuperStream component but no basis was stated for this approach. The determination of the proposed \$1 million, or final \$2 million, was on an apparently arbitrary basis, with no justification as to how these amounts had been determined.

Instead, the Consultation Paper merely provided different scenarios as to how the minimum and maximum amounts could be increased and the levy rate adjusted and presented comparisons of the impact of funds of differing asset values.

It was not apparent why, for example, the approach was not adopted to: -

- allocate the SuperStream amount to the unrestricted component - as it has nothing to do with supervision; and
- increase the maximum amount by the same three percent indexation factor as was proposed for the other industries.

The basis upon which the original maximum, subsequently indexed to \$260,000, was initially determined is also not readily apparent.

The final paper states at Page 12 as follows: -

“Further adjustments are also made to ensure fair sharing of the levy burden in each industry by requiring those institutions that are nearing the maximum amount to continue contributing to the increased cost of supervision. The maximum amount for the superannuation levy has also increased to \$2.0 million in 2012 – 2013 to accommodate the separate SuperStream component”.

Taking the first sentence – from this it would appear that one possible approach to utilising the indexation factor in the various Imposition Acts may be to increase the maximum by the percentage increase in supervision costs.

5.4.3.1 (a) ASFA submits that consideration should be given to increasing the minimum and maximum amount by a factor reflecting the percentage increase in supervision costs in the past year.

The second sentence contains an error – the maximum amount is only with respect to the restricted component of the levy, not the total levy – and makes no reference either to: -

- why the SuperStream amount was attributed to the restricted component; or
- the basis upon which the figure of \$2 million for the new maximum was determined.

It should be noted that the approach adopted in the final paper – of increasing the maximum amount of the restricted component from \$260 to \$2 million - produced the somewhat anomalous outcome whereby: -

- funds of \$50 million and \$250 million had a levy increase of 33.9%, while
- a fund of \$5 billion only had an increase of 20.7% and
- a fund of \$20 billion had an increase of 35%.

Curiously, these figures are identical to the ones in the original Consultation Paper, despite the change in the maximum from \$1 million to \$2 million, which would appear to indicate that perhaps they had not been recalculated.

Most significantly of all, the increase in the maximum amount of the unrestricted component from \$260,000 to \$2 million is effectively tantamount to saying that the cost of supervising the largest superannuation funds is \$2 million. ASFA submits that this is an unsupportable proposition and is in direct contravention of any principles underpinning the concept of cost recovery.

4.5.3.1 (b) ASFA submits that a maximum amount of the unrestricted component of \$2 million in 2012 – 2013 is unsupportable as an amount representing the costs of supervision, which is in direct contravention of the principles underpinning the concept of cost recovery.

6. FINANCIAL ASSISTANCE FUNDING LEVY

ASFA also has concerns with respect the basis upon which the financial assistance levy is determined and, in particular, potential inequities resulting from the imposition of a minimum and maximum levy.

When the *Superannuation (Financial Assistance Funding) Levy Act 1993* (FAF Act) was originally enacted the levy was a flat percentage applied against the assets of the superannuation funds. As a matter of policy a method which utilises fund assets, or possibly the number of members, is consistent with the cost of the levy being borne as equitably as possible across the membership base of all funds.

In 2002, just prior to the first determination of a financial assistance, the FAF Act was amended to insert the ability for there to be declared a minimum and a maximum levy, purportedly to align the financial assistance funding levy with the supervisory levy.

A minimum and maximum with respect to the supervisory levy makes sense – a number of the costs of prudential supervision are fixed and those which are variable are not in direct proportion to fund assets.

6. ASFA submits that, with respect to the financial assistance levy, that the most equitable method to apportion the costs of financial assistance is either to apply a: -

- * percentage across the assets of funds, with no minimum \ maximum; or
- * fixed dollar amount with respect to each member of the fund.

+++++