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Submission to the SENATE SELECT COMMITTEE ON FINANCIAL TECHNOLOGY AND REGULATORY TECHNOLOGY

Reforming financial advice – providing data

We attach our submission to the Committee's Second Issues Paper, thanking you for the extension.

In summary, the proposal is that the Australian public can be provided with vastly improved financial advice if government and private sectors collaborate to develop the infrastructure to provide people's financial data (assets and income) in an appropriate format for robo-advice. Such an initiative would involve the collation of relevant data held by government agencies and financial institutions, so that it could be used to automatically generate personal financial advice (specifically recommendations on contributions to superannuation and life insurance).

We thus address two questions raised in the Issues paper:

- "Ideas on how to best leverage the long term potential of the CDR, in combination with other data reforms, are welcomed by the committee."

- "The committee is interested in exploring the long term possibilities of how a single digital channel to government could streamline the interactions of businesses and individuals with government, and how it could be used to support novel applications."

1   Background

Our submission interest arises out of our membership of the Actuaries Institute's Retirement Incomes Retirement Incomes Working Group (RIWG). The objective of the RIWG has been to encourage the development of appropriate products and advice for retirees - by research and submissions to regulators and government. This submission develops the ideas on advice in our Dialogue paper, "Developing the retirement income framework"[1] published earlier in

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[1] https://actuaries.logicaldoc.cloud/download-ticket?ticketId=b6c596fe-d86e-4ed6-82b2-b9faeca533fd

the year. We have subsequently had informal discussions with informed parties in industry and government agencies, which have been very helpful in refining the proposal.

1.1 Defining advice

The Dialogue Paper was particularly concerned with "standard advice" [2] which would cover:

> *For those with most of their savings in superannuation accounts, there are effectively three decisions: how much to save, where to invest and when to retire. Buying a house comes into both of the first two. ...*

We accept that high income individuals and those with unusual financial arrangements do require a level of complex advice that would be impractical to automate. We also accept that there are those on lower incomes who will not want to save more than they are absolutely required to do. We estimate that over half the population are in the middle and would benefit from automated standard advice.

1.2 Advice model needs reform

We note that the current institutional arrangements for the provision of advice often mean that people in the middle make do without advice, with the consequence that they are left in the dark and vulnerable.

There is a view that the fault lies with complex regulations, with the current AFS licensing rules[3] make giving guidance or advice to individuals difficult and expensive. Recent media articles have highlight that only the wealthy can afford financial advice as the minimum fee is several thousand dollars. ASIC, however, takes the view[4] that it is not the regulatory requirements that are making it challenging for advisers to produce advice, but the conservative approach taken by compliance functions of licensees. More recently however, ASIC has indicated its willingness to work with the advice industry to identify and if possible overcome regulatory barriers to advice, and to that end has published Consultation Paper 332[5] seeking industry input.

It is likely however that there is also resistance to paying for any financial advice. The reasons probably include that it has historically been provided "free" – or rather funded by product providers. The resulting "conflicted commissions" have reduced trust in advisors, and provide another reason for people to avoid taking advice.

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[2] See Appendix.

[3] See s766B or ASIC RG 36.4 and 36.97.

[4] https://www.professionalplanner.com.au/2020/08/conservative-licensees-making-scaled-difficult-asic/

[5] https://asic.gov.au/regulatory-resources/find-a-document/consultation-papers/cp-332-promoting-access-to-affordable-advice-for-consumers/

There is thus a need both to reduce costs, increase trust, and reach those people who are averse to taking advice. Our proposal addresses each of these issues.

1.3 Advice and the rate of SG

Research, much of it reported in the Retirement Income Review[6], has confirmed that no single rate of Superannuation Guarantee (SG) is appropriate for everyone, and most people would be better off if their contributions to superannuation could change over their working lifetime. But a proportion of the population may be expected to benefit from higher compulsory contributions. This highlights the need for bespoke calculations to determine contribution rates appropriate for each member.

Our proposal envisages all members being provided with a recommended contribution rate annually. For taxpayers, this would coincide with their income tax assessment. A further development could be that this recommended rate be provided to their employer, who might automatically adjust their personal contributions to superannuation unless the employee requests otherwise. Employees would obviously have to have easy access to inexpensive or "free" financial advice under such circumstances.

We believe that automatically provided advice can therefore contribute to the resolution of the debate about the level of SG. Specifically, we envisage that the base SG rate could remain at 9.5% as at present, but that the provision of advice would lead to many individuals (acting in accordance with that advice) opting to make additional concessional contributions (or even, perhaps, being defaulted to making additional contributions by the interaction between the advice provided and the superannuation schemes).

2 Collating and processing the data

An initial practical step towards reducing the cost of advice would be to define what data are required and consider how it could be collated inexpensively. The inputs into standard advice that are available would be (ideally, as argued in detail by Asher et al[7]):

- Demographic information on age and household composition.

  o This is perhaps best obtained from Medicare.

- Historical income that can be used to project future income.

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[6] https://treasury.gov.au/sites/default/files/2020-11/p2020-100554-complete-report.pdf

[7] Asher, A, Adam Butt, Gaurav Khemka and Ujwal Kayande (2015) Formulating Appropriate Utility Functions and Personal Financial Plans, Presented to the Actuaries Institute, Sydney (April); http://www.actuaries.asn.au/Library/Events/SUM/2015/ButtEtAlUtilityFunctionsPaper.pdf and the International Actuarial Association, Oslo (June) http://www.actuaries.org/oslo2015/papers/PBSS-Asher.pdf

- o Taxable income is available from the ATO, while the income of those below the tax thresholds are kept by Services Australia (previously Centrelink).

- The historical development of assets (including superannuation, property and bank balances).

  - o The ATO and Services Australia have access to almost all this data,[8] although the ATO only collects a full set of data from just over half of the adult population who report a taxable income[9] (but and who are most in need of superannuation advice), but data on the other half is likely to be collected by Services Australia.

  - o A particular gap is that the ATO does not appear to collect bank balances (and mortgages) – although Services Australia does, so may be in a position to fill the gap.

  - o While personal household furnishings are not collected (for those not receiving welfare payments), the Personal Property Securities Register has information on vehicles, boats, caravans and farming equipment and materials.

- Significant expenses that are not uniform over the lifetime. The largest and most common are buying a house and the costs associated with children including day-care and school fees. Existing homes and mortgage debts can be obtained from the state registers and banks, but it is probably not possible to obtain school fees unless it becomes a future candidate for the CDR. There will therefore be a residue of data requirements that will require personal input.

- While data from the past can allow for calculators[10] to be prepopulated with the most likely projections, people's future plans in areas such as housing, family formation, schooling and other significant planned expenses will also require inputs. While such inputs can be made on-line, our research suggests that most people will want to talk to an expert for explanation and assurance that they understand the consequences. On-line calculators can be developed to allow for these inputs to be made and the consequences illustrated in real time. We envisage such calculators being provided by financial advisors and superannuation funds.

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[8] The ATO collects information about taxpayers. About you! The ATO collects your data from…

- your employers,
- your bank and other financial institutions (now including banks overseas),
- health insurance funds,
- BAS Statements,
- Superannuation accounts,
- and the property information your state may have. (https://www.etax.com.au/ato-data-matching/)

[9] See Biddle, N., Breunig, R., Markham, F., & Wokker, C. (2019). Introducing the Longitudinal Multi-Agency Data Integration Project and Its Role in Understanding Income Dynamics in Australia. *Australian Economic Review,* 52(4), 476-495.

[10] Such as the one developed by Asher et al at www.draftfinplancalc.com – see note 7 above.

The Financial Systems Inquiry thought the ATO could collect and provide some of the data necessary to give financial advice.[11] While the ATO has no statutory power to provide data for financial advice, under Australian Privacy Principle 12 – Access to personal information, an "entity that holds personal information about an individual" has the obligation "to give the individual access to that information on request."[12] Such a request could be channelled through myGov, which could inform people when it was available. It could then be made available (subject of course to appropriate privacy protection and the necessary release authority from the relevant individual) to financial advisors to interpret, supplement and convert into appropriate financial advice. Bank balances and spending patterns could be collected at the same time using Consumer Data Right (CDR) powers.[13]

An alternative model would be to extend the CDR to all cover all private and public institutions that hold relevant data. This would clearly be more expensive. More importantly, the data aggregators would not have a direct route to a market for their services, potentially leaving many people without advice. Employed members could of course be provided with the advice by their funds if they approached the aggregators, but those without a formal employment relationship would not be addressed.

A further alternative model is private sector management of a common resource. An example is the Integrated Public Number Database (IPND)[14], managed by Telstra but regulated by the Independent Telecommunications Adjudicator[15] to ensure all parties obtain the same outcomes. Access for the advisors to their market would remain an issue.

3   Feasibility

The CDR project embodies the principle that providing data to customers is appropriate because people should have the right to see what data institutions are keeping on them. It also shows that it is feasible to provide such data by setting standards for APIs (Application Programming Interfaces) and privacy protection. The CDR applies to the private sector, but the principles are also being applied to public sector through Data Sharing and Release legislation and other initiatives.

It has already been demonstrated that government agencies are able to successfully link records from different agencies. The Longitudinal Multi-Agency Data Integration Project (LMDIP) [16] combines data from the ATO, Medicare, Social Security and the Census. Over 93% of tax and social security records utilised for that Project were successfully matched to Medicare records. Sharing the agency records with the people involved and correcting errors

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[11] https://treasury.gov.au/sites/default/files/2019-03/p2014-FSI-01Final-Report.pdf p267

[12] https://www.oaic.gov.au/privacy/australian-privacy-principles-guidelines/chapter-12-app-12-access-to-personal-information/

[13] https://www.accc.gov.au/focus-areas/consumer-data-right-cdr-0

[14] https://www.telstra.com.au/consumer-advice/ipnd

[15] https://www.theita.com.au/

[16] See Note 9 above.

should be a relatively small exercise that will lead to an even greater degree of accuracy over time.

4   Other proponents of similar ideas

The advice industry is grappling with the possibilities offered by "fintech and regtech", with Ben Marshan of the FPA suggesting that enhanced technology could reduce costs by two thirds.[17] He is supportive of standardisation and industry collaboration, and agrees that further savings could be achieved by automatically provided data.[18]

Administration company Sargon suggests that applying the CDR project to superannuation assets only would have "nigh-immeasurable potential for transforming the state of the superannuation market".[19]

Similarly, Fintech Australia[20] argues that the financial services sector should be a priority in the roll out of CDR, suggesting that it would allow "innovative FinTech companies to create a more holistic view of a Consumer's financial position, working with them directly or via their Accountants and Financial Advisors to improve their financial literacy and long-term financial well-being."

We have had responses to the Dialogue paper from the UK, where there is interest in the British and European consequences of CDR legislation and confirmation that there is strong interest in the idea from participants in the financial services industry from around the world.

The Productivity Commission's *Data Availability and Use* report[21] explored some of the benefits of making such data available, but it referred to the value of the data to assist forward looking budgeting, not highlighting the possibilities of determining superannuation contributions and life insurance needs, or more general financial planning needs.

There are no doubt other proponents of the concept of public provision of data for personal financial planning processes of whom we are not aware.

5   Possible arguments against

One argument would be that providing this data goes beyond the role of government; that it should be best organised by the private sector, and the CDR project will eventually lead to all the data being available. The first counter to this argument is that the private sector does not have the complete records of income and some assets back to 1980 that are kept by the ATO and Services Australia. The second is that the CDR requires a level of collaboration by the private sector that would be considered anti-competitive if it were not regulated by the

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[17] https://fpa.com.au/wp-content/uploads/2020/01/2019_12_23_FPA_Submission_Senate-SCFTRT.pdf

[18] Private communication

[19] Senate Select Committee on Financial Technology & Regulatory Technology - Submission from Sargon, December 2019 https://www.aph.gov.au/DocumentStore.ashx?id=ee685f81-e576-4ec9-9f15-22e33e62a116&subId=675225

[20] https://treasury.gov.au/sites/default/files/2019-03/t247313-FintechAustralia.pdf

[21] https://www.pc.gov.au/inquiries/completed/data-access/report/data-access.pdf

ACCC, so some government involvement is necessary. The third counter is that the provision of this data is equivalent to the provision of infrastructure that facilitates the development of new markets. Even though we agree with Fintech Australia that its members could potentially create better and less expensive financial advice, we see no obvious route for them to that part of the market that is currently not served by financial advisors. Given the complexity of the CDR project, we would think it will be a decade or more before it will be possible to give holistic advice on the level of savings required to smooth income over the lifetime.

Moreover, we suggest that provision of the data would serve an educational as well as an infrastructural role, and this justifies government initiative. We also suggest that the Fintech companies are best placed to supplement government data as necessary, and create software to interpret the data for financial planning programmes once the data are made available in a standardised format.

A potential second objection is that people cannot really understand comprehensive advice, and that there is more value in permitting the wider use of partial and intra-fund advice to improve people's financial outcomes. The standard advice we are considering does however have to be comprehensive in that, without a full picture of lifetime income and expenses, we believe that it is impossible to make appropriate recommendations as to savings, investment and when to retire.

6   Cost benefit analysis

A rough cost benefit analysis suggests that there would be significant social benefits. We have approached half a dozen actuaries who work in or have knowledge of the financial planning process and asked them for their estimates of the potential cost savings (within the existing full-service personal advice model) if comprehensive, reliable and up-to-date data were available from a central source. Their estimates varied widely but we would attach greater likelihood to the central range of responses, which suggested that savings might be in the vicinity of 10% to 20%. Considering savings in the cost of advice only, total annual advice costs are over $2bn, so a reduction in costs of 10% would be at least $200m annually. Just 1% of that, $2 million p.a. should pay for any IT work quite quickly. The PC report[22] cited a UK report that estimated the total cost of an API project at about £1 million.

While cost savings in the advice industry would make for fewer jobs, greater use of financial advice would lead to more people working at giving advice. There are some 22,000 advisors in Australia, with the numbers falling given new qualification requirements[23], so the net impact on employment would be relatively small either way.

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[22] See footnote 21, page 222

[23] https://www.rainmaker.com.au/media-release/financial-adviser-numbers-decline, /

The automation of advice would however make it easier to monitor the quality. Our Dialogue paper identified some of the pitfalls of current advice,[24] most of which could be addressed by developing and monitoring appropriate templates for comprehensive advice.

Given the economic pressures created by COVID[25], there also needs to be a justification for making this project a priority. It is likely that part of any economic recovery is going to involve convincing people with significant assets to spend more of those assets. Proper advice – and the wider take-up of annuities, which we see as one consequence of good advice – would encourage and enable retirees to increase their superannuation drawdowns and spending. Every 1% increase in spending is about $600m annually, which alone would also justify the initiative. Australian Government Actuary calculations suggest that 65-year old retirees with annuities can increase their spending by 15% to 30%.[26] While one cannot expect everyone to utilise annuities, the corresponding proportional increase in spending would be more for retirees over 65, so the overall increase in spending by the retired population could well be in the range mentioned by the Government Actuary.

There is also the possibility that the Early Release from Superannuation will be repeated and ideally, inexpensive advice should be available to support individuals making decisions as to whether to withdraw from their account balances.

7   Next steps

We would like to suggest a few points to consideration by the Senate Committee in making its recommendations.

- There would appear to be few regulatory obstacles to starting a project that extended the data available through MyGov. Such a project could proceed on the understanding that it might be supplemented by private initiatives in due course.

- The Committee would probably want input from Treasury, ASIC, the ATO, the Digital Transformation Agency and Services Australia with their role in MyGov, and possibly the Office of the National Data Commissioner. If considered worthwhile, a further round of public consultation might be worthwhile, given this idea has not previously been specifically canvassed.

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[24] These pitfalls include: recommending higher risk investments in order to meet unreasonably high targets; a failure to understand life insurance is primarily required to cover lost income rather than debt; and recommending superannuation contributions that will lead to a much lower standard of living before retirement than after.

[25] With the Mid-Year Economic and Fiscal Outlook 2020-21 projecting unemployment to remain above 6% until 2023. https://budget.gov.au/2020-21/content/myefo/download/02_part_2.docx p18.

[26] https://treasury.gov.au/sites/default/files/2019-03/p2014-FSI-01Final-Report.pdf. See footnotes on page 26, 92 and 123.

- The Digital Identity project has a budget of $256.6 million over two years from 2020-21 for development and expansion, and some of this might well be spent on further investigation of the feasibility of the project.

Development of appropriate calculators could perhaps be left to the private sector to develop models and communication strategies that best communicate the results.

Appendix

Standard advice before retirement

For those with most of their savings in superannuation accounts, there are effectively three decisions: how much to save, where to invest and when to retire. Buying a house comes into both of the first two.

1.1 How much to save

This question can be addressed automatically – see www.draftfinplancalc.com or www.10E24.com. Such advice needs to consider future cash flow issues including the additional costs of raising children and buying a house – as well as weighing up standards of living before and after retirement. This calculation should include the repayment of debt, accumulation of a buffer for unforeseen costs and provision for bequests. If people cannot use a calculator like this, then they will know they need personalised help from an adviser. We expect that almost everyone will at least require initial explanations of the output of such a calculator.

1.2 Where to invest

There should be a strong default to well-designed lifecycle options here. Most modelling shows that retaining equity exposure until relatively late ages is likely to give better risk adjusted long term outcomes than using defensive assets. Given that mistakes that can be made, there is perhaps a place for relatively detailed regulation on this matter.

1.3 When to retire

This needs to include the possibility of phased retirement (working part time) and cover both members of a couple.