

# Wallis Enquiry - Mercantile Mutual Submission

## Introduction

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Mercantile Mutual is an Australian based multi specialist financial services group and operates in the life insurance, superannuation, general insurance, banking, financial planning and unit trust markets of Australia. The Group manages assets in excess of \$ 11 billion.

Mercantile Mutual occupies a significant position in a number of these markets notably fifth in the life insurance market and 11th in the general insurance market.

Mercantile Mutual is part of the international financial services group ING (Internationale Nederlanden Group). The ING Group operates in 55 countries worldwide and manages assets in excess of \$ 330 billion. The ING Group holds third place in the world league of providers of integrated financial services. A copy of the ING Structure is attached (Appendix 1).

**SCOPE:** The focus of this submission will be on the following major points:

1. Regulation of Institutions
2. Regulation of Disclosure
3. Regulation of Distribution
4. Complaints handling
5. Impact Study

The issues covered under these headings will incorporate banking, life insurance, superannuation and general insurance.

## 1. Regulation of Institutions

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Mercantile Mutual is of the view that replacing the existing system of multiple regulators with a single regulator would improve efficiency and consistency. The reasons for this position are:

### ◆ **Enhanced efficiency -**

Customers believe that the Mercantile Mutual Group is a single entity and that their service is coming from one organisation. Current regulations create artificial barriers to expected customer service and creates inefficiencies for which the customer ultimately pays and, through differing capital requirements lead to different prices for essentially the same products.

The existence of a single regulator would facilitate the exchange of information between Companies within a Group so as to efficiently manage a customer relationship as opposed to a product relationship. Customers' financial services needs will be fulfilled by the wider range of products and choices made available by this model. Also by managing the full customer relationship economies of scale will be achieved largely due to the removal of duplicate information being communicated to customers. These cost efficiencies will flow on to the customer. Under existing arrangements, the provisions of the Privacy Act prohibits Companies within a Group sharing customer information. This is particularly so for Banks.

The ING has a philosophy of being a multi specialist integrated financial services group. This philosophy is built on a cornerstone of efficient service delivery to retail customers through the channel of their choice. The Group has developed business models for retail customers that have enabled an effective translation of the economies of scale mentioned above to these customers. This scenario strongly suggests that the existence of a single regulator for Companies within a Group will result in more efficient service delivery to the customer.

### ◆ **Consistency of decision making -**

Currently many business decisions have to be made at a Company level rather than a Group level due to the different regulatory regimes that apply. If Mercantile Mutual were to report to one regulator, it would enable the Group to introduce a complete product (rather than a series of individual products) to satisfy the needs of a target market such as small business. This would result in cost savings to the customer. For example, in the small business market it would be more convenient and more efficient from a customers' perspective if a product fulfilled the Superannuation Guarantee, Business insurance and Work Cover requirements. Currently this is not possible due to the differing regulatory requirements of each of the products.

Another example is the differing capital adequacy requirements between institutions which gives some institutions a competitive advantage in certain markets. Retirement Savings Accounts (RSA's) are an example where the same contract will be offered by different institutions with differing capital adequacy requirements. While the nature of liabilities under different financial services vary, there is no evidence that there has been an evaluation of the nature and degree of these differences and that differing capital requirements are justifiable. These requirements prevent the development of a level playing field. Differing capital adequacy requirements have an impact on ease of entry, the ability to operate profitably and on competition.

**◆ Lower cost of compliance -**

The Group would only have to comply with the requirements of one Regulator instead of the current arrangements where reporting has to be provided to the ASC, ISC (Superannuation, Life, General) and RBA.

**◆ Monitoring of systemic risk -**

There is a need for monitoring system and nexus and accumulation risks. Logically this would occur at the apex of the regulatory structure and in conjunction with the supervision of items like the payments system, which organises the movement of money through the system, and monetary policy, which is the price of money at its simplest interpretation.

Accumulation risks recognise that financial service providers often act in more than one market with the holding company being the ultimate provider of risk capital to the entities serving the various markets. Most financial service providers also look to repeat business from the same customer either in single markets or across the different markets they service. Throughout the above processes, risks can accumulate. Just as a financial services organisation needs to monitor such accumulations, there is potential that unharmonised regulatory models would not map the system effects of such accumulations.

System risks would include system implosion (systemic risk) as a result of gearing via derivatives or other means, other knock-on effects and events which might threaten the stability of the financial system as a whole or in part.

Mercantile Mutual's preferred option is a single regulator. Should this fail to win support our second option is for the Reserve Bank to implement and control monetary policy, for a second regulator to have prudential supervision of all financial services institutions including banks with a third regulator supervising product and service delivery. Financial services institutions offer a wide range of products. The plethora of legal entity requirements, prudential and consumer "protection" regulations create artificial barriers to entry and competition and add substantially to costs ultimately borne by the customer. Customers do not understand the existing differences and, in some cases, are misled by current differences in regulation.

## 2. Regulation of Distribution

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Mercantile Mutual is of the view that Distribution Companies should be licensed by the Regulator, providing them with the capacity to authorise advisors, agents, employed staff, financial planners and brokers to distribute any product provided certain minimum competencies are achieved. The reasons for this are:

**◆ Choice of distribution channel to customers -**

It enables a wider range of choice of distribution channel being available to customers. Polarisation of the distribution channels would lead to a substantial lessening of competition with no additional consumer protection.

**◆ Complete advice -**

It would also enable intermediaries to provide complete advice taking into account the full range of products available as opposed to only providing advice in relation to certain products which they are authorised to distribute. This would lead to a better quality of advice being provided to the customer ie. the advice would be better aligned to their comprehensive financial services needs.

**◆ Increases competition -**

Competition amongst the distribution channels would increase. This would ultimately benefit the customer in terms of cost of advice being lowered.

The above would not interfere with the ability of financial planners for example to provide non product specific advice.

Mercantile Mutual believes it is essential that all existing distribution channels are maintained to promote customer choice. In particular the multi agent distribution channel has enabled customers access to a wider range of products compared with being offered the products of only one Company. In order to control the possible risk of default associated with advisors who are multi agents representing several companies, the existing arrangement of the Companies bearing the risk should be maintained. That is, if a multi agent provides misleading advice relating to the product of a Company, then that Company is responsible for remedying the situation. If general or non specific advice is provided, then all Companies that the particular multi agent represents are liable.

Mercantile Mutual believes there should be no barriers to a multi agent representing more than one licensee or product provider. Multi agents should not have to seek the permission of a licensee to represent other licensees as this may serve to lessen competition.

The Licenses should be issued at a Distribution Company level rather than individual representatives of that Company as we believe that the Distribution Company is in a better position and more likely to police its representatives than the Product Provider.

The above would make the role of the Regulator more efficient as the Regulator would then only deal with the Licensee rather than individual intermediaries.

Mercantile Mutual is of the view that distribution should be regulated rather than advice as this would also encompass the distribution of products where advice is not necessarily provided eg. If products are distributed via a direct distribution channel, the regulation of advice would leave a vacuum, whereas the regulation of distribution would still apply.

Also it should not be assumed that advice would continue to be in person as expert systems for example may replace the face to face advice situation. Regulation of distribution has the flexibility of incorporating these future distribution channels.

### 3. Regulation of Disclosure

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Mercantile Mutual believes that disclosure requirements should be consistent across products and should factor in the parameters that the product delivers rather than the institution providing the product. To enable concise and more meaningful communication the key features and benefits of a product should be limited to one page. The current system is inefficient for the following reasons:

◆ **Differing disclosure requirements -**

Similar products have different disclosure requirements eg. Unit trusts are subject to ASC disclosure requirements whereas superannuation products are subject to ISC requirements. This results in an overlap of disclosure requirements. For example, a customer has to compare a Customer Information Brochure (CIB) with a Prospectus making the decision process more difficult and confusing.

◆ **Certain products exempt from disclosure requirements -**

Deposit style savings accounts offered by banks are exempt from disclosure requirements whereas a superannuation account is subject to strict disclosure requirements (For example, the method used to calculate interest must be disclosed for these products whereas this is not the case for a bank product). This results in a lack of a level playing field and makes comparison of product performance more difficult for a customer.

◆ **Cost of disclosure -**

The regulation of disclosure should be such that a test of reasonable disclosure rather than absolute disclosure should apply. Currently under the Trade Practices Act the responsibilities of Directors are so onerous that the length of the disclosure documents is impacted. This results in increased costs of production and reduction in clarity of communication.

### 4. Complaints Handling

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Mercantile Mutual is of the view that a central complaints handling body should handle all complaints from banking, life insurance, superannuation and general insurance customers. The current system of complaints handling is inefficient. For example, a superannuation complaint can be referred to either the ISC, the Life Insurance Complaints Board, the Superannuation Complaints Tribunal or the internal dispute resolution mechanism that Trustees are compelled to have in place. In some cases bodies such as the Australian Competition and Consumer Commission may also be involved. Apart from being inefficient the current system is also open to duplication and exploitation. For example, a customer can raise their complaint via the various bodies mentioned above until such time as a favourable ruling is obtained. Our alternative position is to allow a separate complaint system for general insurance.

We believe that customers should be encouraged to complain in cases where there is a genuine grievance such as misleading advice. However, the current Nil cost system also encourages customers to complain on non material issues resulting in the potential for the system to become overloaded. To ensure that only genuine complaints are lodged, the current Nil cost system should be converted to a low cost system, that is , customers should be obliged to pay a deposit of say \$ 50 when lodging a complaint. This money would be refunded in the event that the complaint is settled in favour of the customer. Where a complaint is not settled in favour of the customer, the money can be retained by the complaints body to cover the cost of handling the complaint.

## 5. Impact Study

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Regulators and Agencies should be required to produce impact studies for all regulations (and changes with regulation type effects) when they are tabled in cases where the industry can provide reasonable justification as to why an impact study is required. Currently bodies outside the formal regulators can have regulatory-like effects (eg. ATO, DSS). This can result in a lack of co-ordination of Government policy across all agencies. Agencies who have a narrow perception of their brief, for example protection of revenue, do not always consider the effects their actions have on industry or products.

Even within formal regulators, decisions are insufficiently tested prior to promulgation and implementation and often produce “unintended consequences”. As well as “unintended consequences”, new regulations often fail to fully target the abuses and may cause substantial increases in compliance costs.

In some cases (such as the introduction of Reasonable Benefit Limits regulations in 1990) the Government’s approach to rectifying “unintended consequences” is to introduce transitional arrangements. This results in the system becoming increasingly more complicated and costly.

## Overview

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The structure and impact of regulation has a significant influence on the efficient delivery of financial services. The regulatory environment should be such that it enables the promotion of savings and investment within Australia. The cost and impact of regulations on Australia’s international competitiveness should be considered, that is the impact of regulations on the ability of Australian Institutions to compete overseas and with others competing here via (say) the Internet. Regulation should ensure that Australians save and invest in Australia and not offshore for reasons of cost and efficiency .

In focusing attention on consistency and efficiency of regulation, the impact of varying tax regimes should not be overlooked. A consistent tax structure and the provision of appropriate incentives to save will promote a savings culture in Australia.

## Contact Persons

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