Stronger governance and competition needed in the super system

*by Andrew Bragg

The G20 leader's summit on 15 November, will provide a rare perspective on the challenges we share with other nations.

Managing the cost of an ageing population is a common thread between many G20 nations. It represents one of the most significant policy challenges for the current generation of world leaders.

Many G20 members such as China are implementing private pension schemes as their primary policy response to an ageing society.

These policy responses must be strong enough to face the test of time.

To be effective, private pension systems must be transparent, efficient, strongly governed and subject to competitive market forces. These are the features that will maximise retirement incomes and community confidence.

Our superannuation system has many of these traits. It is a world-leading policy designed to address an ageing population. And, it is well on the way to achieving its goal to provide an adequate retirement for Australians.

But there are key design features which have been overlooked as the growth of superannuation has eclipsed the capitalisation of the ASX.

Better corporate governance and open market competition are essential to ensure the retirement savings of Australians are protected and that the best returns are achieved.

These factors were overlooked when the original legislation was introduced In 1992 by the visionary Keating Government. At the time there were good reasons. These are no longer valid.

In 21 years, Australia has developed the world's fourth largest private pension system. Today it is $1.8 trillion. This will grow to more than $6 trillion over the next 20 years.
We must ensure the superannuation system maintains community confidence.

To achieve this, superannuation funds must have independent directors and operate in a truly competitive marketplace.

The interrelated issues of low standards of corporate governance in the superannuation industry and conflicted and anti-competitive relationships between industry funds' boards and the default superannuation laws must be addressed by the Parliament.

Let us consider both issues.

First, the superannuation industry is a laggard when it comes to corporate governance.

It is hard to imagine that an industry of such magnitude is not required to have independent directors.

Listed companies are required to have a majority of independent directors on their boards as a check and balance to protect shareholders. The superannuation system is larger than both GDP and the ASX, but there is no requirement of to have a single independent director.

Evidence presented to the ongoing Royal Commission into trade unions showed that some superannuation funds are being used by unions and employer groups as playthings.

There have been allegations of unions and employer groups using their board positions on industry superannuation funds to promote their own interests with scant regard for the members of the super fund.

Unions and employer groups typically own industry superannuation funds. This is a by-product of the 1992 superannuation legislation where unions and employer groups own and occupy all directorships on industry superfund boards.

This is not a new problem.

In 2010, the Cooper review into the superannuation system questioned the sustainability of governance standards that did not meet community expectations.

Jeremy Cooper recommended that the Government legislate to mandate independent directors.

While Cooper's recommendations on this issue are yet to be enacted, because we recognised and acted on a need for independence, retail funds have taken the initiative to self-regulate via a FSC Standard which requires a majority of independent directors and an independent chair.

In the four years since the Cooper review, there have been many examples of union and employer group nominated directors acting in the sponsoring organisation’s interests – at the expense of members’ interests.

It is now time to address the issue before community concerns escalate regarding the superannuation system operating for the benefit of unions and employer groups. Independent directors would provide a check on their power.

The second issue is that the default superannuation market is anti-competitive. Competition in this market is restricted at the workplace and the individual level.

Union officials and employer organisations can use their positions as directors of industry superannuation funds to restrict competition.

They do this to prevent employers and employees from choosing their desired fund.

The Fair Work Commission is central to this conflict. It has the power to give the final tick of approval to default fund recommendations.

The legislation is drafted to allow only the unions and employers who sit on the boards of industry superannuation funds to recommend a default fund. Every other entity is cut out of the process.

This is a howling conflict at the heart of the super system. The only way to stop this racket is through legislation.

Receiving default fund status in a Modern Award is a tremendous fillip for a superannuation fund. It provides over $9 billion in guaranteed contributions from employers who *must* pay all default contributions to the industry fund named in the award.

Last Saturday, the Royal Commission provided examples of how individuals had been denied the right to choose their own superannuation fund − a fundamental right for any working Australian.

To this day, the law allows unions and employer groups to deny choice of fund to union members and non-union members alike.

The Fair Work Commission prevents Australians from moving to a better performing or lower fee super fund.

Whilst this racket continues, super funds have no incentive to lower their fees and improve their performance to compete for business.

Now is the time to adopt reforms to address these gaps in our super system.

Better governance and competition will maximise retirement savings and help deliver on the objectives of the system as our population ages. And, legislation must be drafted so that all Australians and their workplaces can select any APRA approved default fund without restriction.

Australia was an early mover on superannuation. As other countries move to adopt similar schemes, we should remind them that governance, transparency, competition and avoidance of conflict must be paramount.

[ENDS]

*Andrew Bragg is the Director of Policy at the Financial Services Council