14 August 2017

Retirement Income Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: superannuation@treasury.gov.au

Dear Mr Beckett

Treasury Legislation Amendment (Improving Accountability and Member Outcomes in Superannuation) Bill 2017

The Financial Services Council (FSC) welcomes the opportunity to provide a submission in relation to the Treasury Legislation Amendment (Improving Accountability and Member Outcomes in Superannuation) Bill 2017 (the Bill). The FSC supports the Bill and its objective of making the superannuation industry more transparent and accountable to consumers.

The FSC has over 100 members representing Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies. The industry is responsible for investing more than $2.7 trillion on behalf of 14 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world.

The FSC supports the policy objective of the Bill and its component parts. A more transparent superannuation system that is accountable to consumers is an important element of empowering consumers to choose between superannuation product providers.

Please contact me with any questions in relation to this submission on (02) 9299 3022.

Yours sincerely,

Blake Briggs
Senior Policy Manager

Introduction

The Financial Services Council (FSC) broadly supports the package of reforms that are designed to collectively increase the transparency of the superannuation system and the accountability of funds to consumers.

The FSC notes that the measures apply across default MySuper products as well as choice products. The FSC supports these reforms as a basis to enable to consumers to make informed decisions that will support further reforms to make the superannuation industry more competitive.

This submission primarily addresses technical design or implementation concerns that may arise as a result of the reforms.

Member Meetings

General meetings in the corporate sector are an important mechanism to promote transparency around how a business operates, however it is primarily a decision-making forum that allows company management and directors to be accountable to shareholders through resolutions and voting rights.

The FSC understands that the proposed reforms seek to adopt the transparency elements of a general meeting, by allowing consumers to ask questions of their fund executives and directors with regard to the management and operation of the fund and to ensure a meaningful response is provided in a timely manner. The FSC supports this objective, however some elements of the design of annual member meetings (AMMs) in the draft Bill undermine the effective achievement of this objective.

Prescriptive approach

The Bill takes a prescriptive approach to how member meetings are to be held, with key elements derived from the regulation of general meetings in the corporate sector. There are, however, important differences between general meetings and member meetings, such as the use of general meetings as a decision-making forum, whilst a member meeting is an inquisitive forum.

The FSC submits that the differences are important and, as the new regime is implemented, challenges will emerge that require flexibility in how member meetings are conducted. Some initial challenges that we foresee are outlined below.

Given the very different nature of AMMs and the sheer size of some funds, the FSC has identified significant issues with timing for implementation including notification to members (current and incoming) which can only occur once the design and approach has been determined.

While it is appreciated that an earlier deadline may appeal we have concerns that ill-managed and hastily conceived approaches could undermine the very intent behind the concept – that is the ability to more readily engage with the trustees and responsible officers on matters related to the management and operation of the fund could be compromised.

The preference is that the timeframe for the first AMM be no earlier than 6 months after the end of the entity's income year following the financial income year in which the Act receives Royal Assent – a maximum 18 months after assent. Further the regulator should have the ability to extend the timeframe where it is in the overall best interest of members in certain circumstances (for example, revocation of license/wind up of the fund, potentially a merger/successor fund situation).

The FSC also proposes that the Bill take a 'light touch' approach to the regulation of member meetings and that the administration of those meetings be implemented through regulations following further industry consultation. This will avoid the need for legislative amendments to solve for potential costly implementation issues that may arise in the future.

Trustee protection

The FSC recommends that the Bill provides that trustees are afforded protection for any AMM model that may be adopted to give effect to the core intent. No model will capture or suit all members.

The FSC's view is that members should have the capacity to pose questions to the responsible officers of the fund about its operations, management and overall condition, and that a trustee should have flexibility to choose the model that best suits its operations.

Online options or in person

The Bill provides that a member meeting may be online, but leaves this decision to the trustee. However this raises issues for a trustee and their obligations to act in the best interests of members if there may be members who are excluded by any given approach. This may be more so for MySuper members given requirements for equivalent rights and benefits. There will never be a universally inclusive approach for all members (of a large fund). .

We would also note that to date, we have not been able to identify an interactive and moderated online capability that would accommodate potentially several, if not tens of, thousand members.

The FSC supports the trustee being able to adopt either:

- Webcast responses to pre-registered questions with capacity to submit further questions online on the day for response within the stipulated period;
- Only online member meetings.

These approaches are likely to be the only viable models for very large entities and will reduce the cost of implementation and the administration of meetings that may involve several million consumers.

The FSC submits that the Bill (supported by regulations) should make it clear that member meetings are taken to satisfy the requirement to hold a meeting and meet the best interest test if they are held exclusively online or via a webcast in response to pre-registered questions (with ability to submit further questions following the webcast).

The regulations may provide that trustees are protected where they have taken reasonable steps to provide access and notices to members (which may be with "Annual Reports", but also potentially via the website, emails or other communication modes)- see further below. .

Questions of directors and managers

The Bill provides that all questions put to directors and management must be answered within 30 days, and that the question must be answered by the person to whom the question was put.

In some instances a question may be put to the director or manager, and the Bill should be sufficiently flexible to allow these questions to be allocated to the correct person.

Further, there may be duplication of questions, or vexatious questions. The Regulations should allow flexibility in the administration of questions, so that material questions must be answered by the

fund, which duplicated questions need only be answered once, and vexatious questions screened out. This could be achieved by the 'moderator' of the questions having a responsibility to ensure legitimate questions reach responsible officers, to prevent a moderator from screening out genuine questions that may embarrass directors or managers.

The FSC also submits that the Bill should be amended to provide that in relation to the opportunity to ask questions at the AMM the following matters are excluded for questions:

1. Questions in relation to the *individual* situation of an RSE member – the forum for such matters is, in our view, outside a governance mechanism such as an AMM and properly the remit of liaison between the individual member and the RSE Licensee, and failing agreement, via dispute resolution mechanisms (Internal Dispute Resolution and External Dispute Resolution); and
2. Questions which may be brought via the dispute resolution procedures (including the Superannuation Complaints Tribunal) and which do not relate to the operation of the RSE as a whole. Essentially matters which are within the Terms of Reference of an external complaints resolution scheme (and not excluded by the Terms of Reference) or which are within the jurisdiction of the Superannuation Complaints Tribunal, should not be the subject of questions at the AMM. The Government has announced the establishment of the Australian Financial Complaints Authority (**AFCA**) – so similarly, matters not within AFCA's jurisdiction and which relate to the operation and management of the RSE should be within the remit of AMM questions, but matters within AFCA's jurisdiction should not be within the remit (for questions) of the members as a collective via the AMM.

Questions which are matters that are managed under existing frameworks (legislative provisions as also regulator standards) should be able to be managed via that framework. That is, this AMM process should not override or interfere with these processes. It will be important to ensure that 30 day response periods are not intended to circumvent, for example, dispute resolution timeframes and protocols. It should be sufficient to respond to such questions by providing the approach for managing the issue in response.

<u>Managing the answering of questions</u>

The Bill also does not make it clear how questions should be answered, except that they must be answered within 30 days. The FSC proposes that all answers should be made public, on the fund website, rather than the response being directed to the individual who asked the question. This would improve transparency, and also assist in the management of duplicate questions.

The FSC also proposes that consideration be given to requiring questions to be provided by the members prior to the AMM in order to construct the agenda, manage resources and reduce costs. This would make it simpler and potentially the AMM broadcast.

We note that some funds have upwards of 1.5 million members. Even if 10% were interested this would be more than 150,000 individuals. While we have not had the time to conduct sufficient research, at this juncture, we have not identified an interactive online provider with moderating capability with capability for this capacity (or potentially more).

<u>Notice requirements</u>

The Bill requires funds to issue a notice 21 days prior to the meeting, along with the 'Annual Report'.

This is very prescriptive and could add significantly to costs. There needs to be some more flexibility in the approach.

The Bill should also clarify what the 'Annual Report' is, as it is not defined in the SIS Act or Regulations. The FSC expects that this is a reference to fund information published under the banner of an 'Annual Report', but we note that this is not a defined concept under the SIS Act.

Funds currently have up to 6 months to issue their annual report, however under the Bill a member meeting must be held within 5 months of year end. Further, the notice must go out at least 21 days prior to that, with the Annual Report. As a result the 6 month publication timeframe has effectively been shortened to 4 months. The FSC submits that the timeframe should not be dealt with in the Bill, but Regulations, and the Regulations should extend this timeframe back to 6 months.

The FSC submits the Bill should ensure that:

- existing digital disclosure provisions in relation to the Corporations Act are replicated in the SIS Act and that the notice and report component can be online;
- A notice can be issued with information about where to access the Annual Report (or to request a copy).

To reduce cost, the Bill could also allow default notification to be emailed or provided via SMS link unless a consumer opts out or trustees do not hold the relevant details. In addition, the Corporations Act provisions for not having to send to lost or uncontactable members would need to be adopted.

<u>Minutes</u>

The Bill requires minutes to be kept for member meetings, but minutes traditionally record decisions, of which there will be none.

The FSC submits that instead of minutes, the regulations prescribe that funds be required to publish on their website, in a common and publicly accessible location:

1. The agenda for the general meeting;
2. The Annual Report;
3. A list of attendees from the fund who will be available to answer questions;
4. All the questions lodged with the fund (including those not answered); and
5. The answers that were provided to questions.

The FSC submits that this will provide a more meaningful outline and recount of the meeting that will be useful to consumers.

<u>Attendance Requirements</u>

The bill currently requires all directors and senior managers to attend the member meeting and be available to answer questions. The FSC broadly supports the intent of this requirement, but submits that some flexibility is required to operationalise this requirement.

The onus should be on the attendance of the trustee directors, the CEO, and the auditor, as the principle decision-makers. Other senior managers, such as heads of business should be encouraged to attend on a 'best endeavor' basis, in recognition that it is not always feasible to have an entire executive team available on a common date. This would also help funds ameliorate the cost of meetings.

MySuper Outcomes Test and related APRA Powers

The FSC supports concept behind the new MySuper Outcomes Test as an important mechanism to ensure trustees act even more diligently in respect of members who may have defaulted their decisions to the trustee and, where beneficial, to drive consolidation of the superannuation industry.

There is a well understood issue of underperforming, often sub-scale, superannuation funds and APRA should have the capacity to take action in relation to trustees that are unwilling, or unable, to act in the best interest of their members.

Outcomes test

There is benefit to allowing the trustee to assess its MySuper product in the context and circumstances of its fund and membership, while also ensuring that there is sufficient consistency in disclosure, and the basis of that disclosure, to avoid inappropriate industry distortion. Much of this will rely on the form of the regulations to be drafted (including the peer information on which an assessment is to be based) and, to that end, we would welcome appropriate consultation on the form of regulations.

The benchmarking of funds should, however, only be against similar funds (ie those funds it is possible to compete with) given many MySuper funds are corporate funds and not public offer.

Given the timing of the existing scale test is currently linked to the date a MySuper authorisation was granted, a transitional period of one year after the Bill receives Royal Assent is also required.

Further, the Bill does not currently prescribe the manner and place of disclosure (simply referring in proposed section 29VN(1)(b) to the determination being 'in writing'), and the matters included in section 29VN(4) do not contemplate regulations on those matters. Similarly, the draft EM refers to the disclosure being a public disclosure requirement, but that is not clear in the Bill. We support the disclosure being a public disclosure and suggest that the disclosure should be limited to a statement of the determination included in the Annual Report.

Finally, the Bill proposes to apply to annual determinations after the day of enactment, and the amendments will replace the current scale test. If the timing remains in its current form, there is a need to clarify whether an assessment is required at the time the next scale test was due to be performed (which may be shortly after enactment for some trustees), or whether the determination can be made within a year of the legislation coming into effect despite when the last scale test was completed.

Attestation

The FSC understands that the requirement for an attestation that the expenditure of the fund is directed towards achieving its objective is intended to be public, but that the methodology for determining that the attestation is accurate is only intended to be submitted to APRA.

The FSC supports this new requirement, on the basis that it will force subscale or inefficient funds to consider whether their strategy continues to be in the best interest of consumers.

The FSC questions whether an annual attestation is necessary, or whether this will result in it becoming an ongoing compliance exercise, rather than a more rigorous examination of the business. The FSC submits that the first attestation should occur no later than 18 months after royal assent of the bill, and then attestation should occur at least every three years thereafter.

APRA Directions Powers

The FSC agrees that APRA should have broad powers to manage the superannuation industry through periods of genuine crisis. The proposed powers, which mirror APRA's oversight of ADIs and life insurance companies, do not recognise there are important distinctions between those types of companies and superannuation funds.

ADIs and life insurers manage shareholder capital, and can become insolvent, putting at risk creditors and the financial system more broadly. Superannuation funds, however, could sustain investment losses, but generally the risk to creditors and members is very low. The powers APRA is afforded should reflect these differences and be tailored to the problem that the regulator may be called upon to solve.

The FSC submits that administrative merits review of the use of its directions powers is not an adequate check on the substantial power APRA will be granted under these reforms. Further, we note that judicial review of an APRA decision under the new regime will be available, however, the powers given to APRA are extremely broad as are the circumstances in which they can be exercised. We feel that further steps should be introduced into the process so unnecessary litigation can be avoided and an objective measure or test applied.

The FSC recommends that a proportionality requirement be introduced to APRA's directions powers in relation to superannuation funds. In effect, APRA should be required to show how the direction it is issuing is proportionate to the risk to the fund and its consumers that APRA has identified in the crisis scenario.

In practice, if APRA is not able to readily justify how its action is proportionate there would be a strong argument that APRA has not conducted a sufficiently thorough assessment of the issue and its response.

The FSC also submits that if APRA is deciding to implement direction that would have a material impact on the fund and its consumers, APRA should be requires to get Ministerial approval for such a direction. Given the very significant consequences of the issue by APRA of a direction, it is appropriate that such a step occur only with Ministerial approval.

<u>RSE protections</u>

The FSC submits that the protection from liability be amended to expressly apply to the RSE Licensee itself (a corporate RSE Licensee is not currently included in proposed section 131FC(1)(c)).

Given the consequence of not complying with a direction, and the current limitation to administrative merits review, we suggest that it is inappropriate to limit the protection to compliance with the direction being 'reasonable' (section 131FC(1)(b)) and recommend that the limitation on the protection be removed.

Reporting Standards

The FSC supports the amendments to the reporting requirements. This is a significant development in the transparency of the system and should ensure most participants in the public offer sector are operating under similar disclosure standards for analogous products and services.

The FSC submits that the Government and APRA provide sufficient time to implement the new reporting requirement, based on further consultation with the industry.

Transfer of Ownership

The FSC is broadly supportive of these provisions, by notes that 90 days is a long time in the context of takeovers. The FSC suggests ASX trading rules and timings needed to be taken into account.

Director Penalties

The FSC supports the extension of these penalties, but is concerned that the proposals seek to take the offences from s601FD of the Corporations Act without applying the defences of Part 2D.1. This is in spite of the FSI specifically referencing Part 2D.1 as part of Recommendation 13 in its final report.