



17 February 2014

Manager
Superannuation Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: superannuationconsultation@treasury.gov.au

Dear Sir/Madam,

Better regulation and governance, enhanced transparency and improved competition in superannuation

The Institute of Chartered Accountants Australia (the Institute) would like to take this opportunity to make the following comments in relation to the discussion paper on better regulation and governance, enhanced transparency and improved competition in superannuation.

The Institute is the professional body for Chartered Accountants in Australia and members operating throughout the world.

Representing more than 73,000 current and future professionals and business leaders, the Institute has a pivotal role in upholding financial integrity in society. Members strive to uphold the profession's commitment to ethics and quality in everything they do, alongside an unwavering dedication to act in the public interest.

Chartered Accountants hold diverse positions across the business community, as well as in professional services, government, not-for-profit, education and academia. The leadership and business acumen of members underpin the Institute's deep knowledge base in a broad range of policy areas impacting the Australian economy and domestic and international capital markets.

The Institute of Chartered Accountants Australia was established by Royal Charter in 1928 and today has more than 61,000 members and 12,000 talented graduates working and undertaking the Chartered Accountants Program.

The Institute is a founding member of both the Global Accounting Alliance (GAA), which is an international coalition of accounting bodies and an 800,000-strong network of professionals and leaders worldwide; and Chartered Accountants Worldwide, which brings together leading Institutes of Chartered Accountants in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support, develop and promote over 320,000 Chartered Accountants in more than 180 countries around the world.

charteredaccountants.com.au

If you have any questions regarding our submission, please do not hesitate to contact me on 02 9290 5704 or via email on liz.westover@charteredaccountants.com.au.

Yours sincerely,

Liz Westover
Head of Superannuation

Customer Service Centre
1300 137 322

NSW
33 Erskine Street
Sydney NSW 2000

GPO Box 9985
Sydney NSW 2001

Phone 61 2 9290 1344
Fax 61 2 9262 1512

ACT
L10, 60 Marcus Clarke Street
Canberra ACT 2601

GPO Box 9985
Canberra ACT 2601

Phone 61 2 6122 6100
Fax 61 2 6122 6122

Qld
L32, Central Plaza One,
345 Queen Street,
Brisbane Qld 4000

GPO Box 9985
Brisbane Qld 4001

Phone 61 7 3233 6500
Fax 61 7 3233 6555

SA / NT
L29, 91 King William Street
Adelaide SA 5000

GPO Box 9985
Adelaide SA 5001

Phone 61 8 8113 5500
Fax 61 8 8231 1982

Vic / Tas
L3, 600 Bourke Street
Melbourne Vic 3000

GPO Box 9985
Melbourne Vic 3001

Phone 61 3 9641 7400
Fax 61 3 9670 3143

WA
L11, 2 Mill Street
Perth WA 6000

GPO Box 9985
Perth WA 6848

Phone 61 8 9420 0400
Fax 61 8 9321 5141

General comments

The current size and projected growth of the pool of assets contained in the superannuation environment necessitate the need for a governance structure that is robust enough to appropriately take responsibility for the retirement savings of the Australian people now and in future years.

One of the key pillars of the super system is the compulsory contribution regime. A government that requires the forgoing of salary and wages now to put money into a superannuation account, potentially for decades, needs to ensure the appropriate governance framework exists for the system that will house these monies. Such a framework should be free from conflicts of interest to ensure savings will be guarded by those, and only those that will act in the best interests of their members.

While some governance arrangements to date may have served a useful purpose, good governance dictates continual monitoring to ensure that systems remain appropriate or are adjusted to meet the maturing and changing needs of the super system. There is no doubt that Australia's super system has changed in recent times; super funds have consolidated, grown and transformed into something quite different from years gone by. Many industry funds have become public offer funds, the growth of the self-managed super fund sector has been significant and the volume of funds under management now exceeds \$1.7 trillion.

The Institute supports the government's current initiative to assess the regulation and governance of the superannuation system. We note however that the results of many recommendations arising from the Cooper Review into Australia's superannuation system and the Stronger Super reforms are yet to be seen. We encourage the government to allow those measures to be given time to prove themselves before more potentially unnecessary regulation is introduced.

Reference to APRA Prudential Standards

APRA have addressed and issued prudential standards on many of the issues canvassed in this discussion paper. Notwithstanding specific recommendations contained in this submission, we would encourage, where appropriate, that reference be made to those prudential standards. In the interests of limiting compliance costs and reduction of red tape, consistency where possible is encouraged.

We note however that any gaps in the application of APRA prudential standards to certain types of superannuation funds would need to be addressed.

Better governance

Fundamentally, the Institute is supportive of a trustee board model that allows for the establishment of a talent pool of professionals. The role and responsibility of superannuation fund trustees is critical to the overall governance and operation of the Australian superannuation system. It is imperative that Boards have the flexibility to identify and recruit the right skill sets for trustees to ensure they have the best Board to look after their members best interests. While the equal representation model may have been useful in prior years, we do not believe that it remains the best model for the superannuation industry into the future. Employer and employee representation should not be required nor aspired to as a default or best practice scenario.

We note that as per Principle 2 of the ASX Corporate Governance Principles, all directors, whether independent or not, should bring an independent judgement to bear on board decisions. This is clearly aligned with acting in members' best interests and conflicts with the notion of employer and employee appointments. If independent judgement is required, as it should be, then these types of appointments potentially undermine that thinking.

Best practice would dictate a system in which a talent pool of professionals from a range of background dominates superannuation boards to bring more appropriate types and levels of skills and knowledge to the mix. The

Better regulation and governance, enhanced transparency and improved competition in superannuation

decisions of the right skill set for the Board as a whole should remain with the existing Board, acting in the best interests of the members and not be layered by a requirement that a position be filled by an employer or employee representative. Even if the Board were to request a certain skill set be met by an employer/employee appointment, this added layer undermines the best possible candidate filling the position.

Independent trustees

The difficulty of mandating independence for all members of a trustee board is that the Board may lose the ability to utilise the services of experienced and knowledgeable people due to their affiliation with an organisation. It does not make sense to limit a Board's ability to optimise the potential of the Board in this way. However, it must be clear that any board appointment is not due to a person's affiliation but because of their individual skill set.

From time to time, it may be desirable to appoint a person *because* of their affiliation with an organisation so the Board can access that particular experience. Again, a requirement for all 'independent' trustees may deprive the Board of the ability to access that skill set. Any potential conflicts of interest in these circumstances would need to be declared and managed, as appropriate.

Fundamentally however, we believe the best interests of members would be served by a board with a majority of independent trustees.

The Institute recommends that trustee Boards should, at a minimum, comprise a majority of independent trustees but be able to retain the ability to appoint trustees with an employer/employee affiliation if it is deemed to be appropriate. Any requirements for mandatory employer and employee representation should be removed.

Independent Chair

In line with ASX Corporate Governance Principles, the Institute is supportive of the role of Chair of trustee boards being an independent trustee. Regardless of the makeup of a trustee board, the best interests of members will be best served by the Board being directed by an independent Chair.

Definition of independent

The definition of independent is a subjective matter. In the context of the superannuation industry, the knowledge and experience that would prove invaluable to a Board is generally obtained having come from a certain sector, affiliation, fund type or background, which by its very nature may impinge on independence.

The accounting profession has dealt with the notion of independence with a principles based approach. APES 110 issued by the Accounting Professional and Ethical Standards Board is the Code of Ethics for Professional Accountants and extensively deals with actual and perceived independence along with risks and safeguards. Where threats to independence can be identified, appropriate safeguards must be put in place to mitigate those risks to an acceptable level. If those risks cannot be reduced to an acceptable level through safeguards, then the accountant, particularly auditors, would need to remove themselves from, or not accept, an engagement. We would encourage a similar approach to be used for superannuation trustee boards.

With this in mind, there are clear circumstances in which no appropriate safeguards could be put in place and in the superannuation context, these could be identified as clear rules or guidelines which may need to be adhered to in the first instance. For example, by reference to the ASX Corporate Governance Principles in which an independent director is a "non-executive director who is not a member of management.....". Other rules and/or guidelines may address current employment or affiliations.

Hard coding a definition of independence in legislation runs the risk of a "tick the box" mentality about what independence actually looks like and this can be vastly different for any individual. It is near impossible to identify every possible scenario that could affect the independence of every person. Being overly prescriptive in defining

Better regulation and governance, enhanced transparency and improved competition in superannuation

independence may allow people to satisfy set independence requirements when any reasonable person could see they were not independent at all.

The Institute recommends a principles based approach to independence accompanied by clear guidelines on applying these principles.

Appointment of directors

All trustee boards should establish a nominations committee. This committee would be responsible for making recommendations to the Board regarding the desired skill sets for the Board, gaps that may exist as well as developing processes for the appointment of directors. As per ASX Corporate Governance Guidelines, this could also include processes for performance evaluation of individual trustees and the means by which underperforming members will be dealt with.

Boards and nominations committees must be transparent about their processes and be held accountable for adherence to agreed processes.

The Institute recommends the establishment of a Nominations Committee for every trustee board. Guidelines similar to the ASX Corporate Governance Guidelines should be developed that require transparency around processes and adherence to best practice.

Management of conflicts of interest

While the Institute is supportive of frameworks and policies around management of conflicts of interest including registers and disclosures, it is important that where breaches occur, boards deal with it in an appropriate way.

While disclosure of conflicts is useful, it does little to manage the conflict if there is no consequence attached to it. That is, following disclosure there needs to be clear processes for how the actual conflict is managed and the Board held accountable where conflicts are not managed appropriately.

Board tenure

The Institute is supportive of limited tenure for trustee boards. However, the Board may need some flexibility around this to ensure continuity, consistency and experience is maintained on the Board at any given time. We believe a period of no more than five years would be appropriate. This would enable experience on a particular board to be achieved and maintained. This could be accompanied by a two year extension where the Board believes that the members' best interests would be served by an extended period. This may be because no appropriate replacement has yet been found, a particular skill set is warranted etc. Such extensions would need to be justified and validated by the Board and the independent Chair.

We believe that a period of less than five years may be counter-productive to a goal of a best talent trustee board.

Board appraisals

There is no doubt that best practice would dictate the need for the Board of any entity to be accountable for their actions and performance. Superannuation funds would be no exception particularly in light of the responsibilities they have for the growing pool of retirement savings of millions of Australians and includes monies that are placed in their custodianship under a compulsory superannuation contribution system.

Again, however, this must go beyond holding policies to appraise board performance. There must be procedures to be followed where trustees or the Board as a whole are not meeting expectations. This could be in the form of additional training, mentoring or ultimately, early termination of their appointment where underperformance cannot be managed.

Better regulation and governance, enhanced transparency and improved competition in superannuation

All board appointments should go through (or have already gone through) some form of education in directorships, superannuation and importantly the super fund itself. Ongoing education of boards should be encouraged and supported.

Appropriate transition

As with any changes to an organisation, particularly those that impact on the governance structure, appropriate transitional arrangements should accompany any changes in requirements. The Institute is aware that some trustee boards either have, or are moving towards independent trustee boards; others may struggle in the short term to adjust their current board model. Furthermore, it would not make sense for significant numbers of funds to all be “in the market” at the same time recruiting new trustees. This would run the risk of some funds being unable to meet their skill set requirements or not being able to recruit the best people.

Should a change in trustee governance models be introduced, we would strongly encourage consideration of an appropriate time frame in which superannuation funds can meet any new requirements. This may require anywhere between five and ten years for full implementation across all funds.

Enhancing Competition in the Default Superannuation Market

While employees in Australia continue to enjoy the ability to select their own super fund, many workers simply do not or cannot select their own fund and rely on their employer to do so for them. Employers therefore require a default fund to ensure they can meet their legal obligations to make superannuation contributions for their employees where no employee nomination is made.

Large organisations with greater resources may go through a due diligence process in selecting a default fund while others will have the default fund selected by the relevant award. Others use the services of advisers or simply select the industry fund aligned with their own particular industry. For smaller organisations, the choice may simply be deciding which fund already has the most employees in it. Notwithstanding that an employee’s contributions may initially be directed to a default fund, they retain the ability to select their own fund at any time for future contributions. In the context of choice of fund, the Institute believes that employer choice of default fund is the appropriate model for default fund selection.

The Institute has always believed that easy, standardised, comparable data from super funds will enable employer choice mechanisms for fund selection to improve. It is our view that with this type of data, flexibility for employers and employees can continue and this we believe, will be in the best interests of employees. Education and easily accessible guidance and information will be important. This type of support is becoming much more easily available and we would encourage continued supply by the regulators (for example, MoneySmart website by ASIC and content available on the ATO website)

The need and validity of default fund nomination within modern awards is questionable. Notwithstanding the mechanisms for choosing which funds are nominated in an award, a requirement to use one of these funds may in fact limit an employer’s ability to act in their employee’s best interests. That is, restrict their ability to nominate a fund they (or their advisers) believe to have a better or importantly, a more suitable offering for their employees.

We do not question that some employers will desire support and guidance in choosing a default fund while others may welcome not having to make a choice at all and simply defer to those funds nominated in an award. To this end, the inclusion of default funds in an award may be useful but should not be mandatory. Flexibility and freedom of choice should be key drivers of default fund selection.

While the Institute does not support mandating default funds within modern awards, should this practice continue, we would largely support the recommendations from the Productivity Commission report on default funds to greatly improve the selection processes for fund inclusion in an award. In particular, the processes of selection need to be

Better regulation and governance, enhanced transparency and improved competition in superannuation

clear and objective. Those participating in the processes must be free from conflicts and given the flexibility to create a list of funds that will be in the best interests of employees and members.

The current system of selection does not appear to be fair, equitable or in the best interests of members. The processes of selection for fund inclusion in an award are far from transparent with the potential for unacceptable conflicts of interest.

The introduction and development of MySuper products will standardise and enhance the default super offering for many Australians. We caution too much reliance on this at this stage as the means by which default funds are selected. The MySuper regime is new and still needs to demonstrate its success in not only providing some protection for Australians who are less engaged with their superannuation but also as a tool in assisting employers in selecting the right default super fund for their employees.