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Mr. Jonathan Rollings
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Financial System Division
The Treasury
Langton Crescent
Parkes, ACT, 2600

Recommendation 2.1 – office of "trustee director", codification of statutory directors' duties and enhanced duties for directors and trustees

Dear Jonathan,

I refer to the first meeting of the Governance Working Group when we discussed Recommendation 2.1, in particular the creation of the office of trustee director. At the conclusion of that meeting you asked the group to provide practical examples of problems associated with this recommendation.

Notwithstanding that it would appear that Treasury seems to be moving away from supporting the creation of the new office this issue remains of concern to a number of our members. In this letter we reiterate some of our member's concerns and provide some practical issues associated with the recommendation. We support the working group's view that the duty of directors of APRA regulated superannuation funds should be enhanced to ensure they:

- give priority to the rights of members above all else; and
- exercise the degree of care skill and diligences as an ordinary prudent person of business….

Office of "trustee-director" and the associated duties

ASFA supports the policy objective of increasing the accountability of superannuation trustees and the directors of corporate trustees. However, we are not convinced that increased accountability will be achieved in any meaningful sense by creating a distinct new office of "trustee director" with all statutory duties to be set out in the SIS Act. Instead, ASFA suggests that efforts to increase accountability would be better served by focusing attention on the effective enforcement of existing legal duties.

The idea of directors owing fiduciary obligations directly to fund members contradicts the basic principle that a director's primary obligation is to the company. The reasons why a generalised director/beneficiary fiduciary relationship is not appropriate were canvassed in the well-known decision of Justice Finn in *ASC v AS Nominees* [1995]. Specifically, Justice Finn queried whether the imposition of a direct fiduciary obligation irrespective of the facts was "*desirable or necessary*". He thought members could be protected "*by other quite orthodox means and in a more extensive way*".

The more conventional approach to the design of directors' duties was recently supported by Dr Pamela Hanrahan, formerly a noted academic in this area and now an ASIC Regional Commissioner. Speaking at the 2011 Law Council Superannuation Committee

conference, Dr Hanrahan identified 6 ways in which a superannuation trustee director is already potentially personally liable to members:

- duty of care under section 52(8) of SIS;
- financial services misconduct under CA Pt 7.10 and ASICA Pt 2;
- trust law proscriptions;
- knowing receipt;
- knowing assistance; and
- involvement in a contravention of SIS, CA or ASIC Act.

ASFA submits that it is highly questionable whether adding a seventh way in which a director could be personally liable to members will increase accountability in any meaningful sense.

On the other hand supporters of the Review's proposal may point to section 601FD(1)(c) of the Corporations Act, under which a director of a responsible entity must act in the best interests of scheme members. In other words, there is a generalised director/beneficiary fiduciary relationship (imposed by statute) of the kind not favoured by Justice Finn.

ASFA suggests that while section 601FD(1)(c) may provide a precedent for what is proposed in the superannuation context, it is not a good precedent. Section 601FD(1)(c) has not saved scheme members from the consequences of the actions (or inaction) of RE directors. ASFA is not aware of any reported case where the outcome has turned on the operation of section 601FD(1)(c), in the sense of that section being the difference between a scheme member obtaining and not obtaining legal redress.

We have identified the following potential practical issues associated with the recommendation:

- D&O insurance premiums may be reviewed (upwards) in light of this change (should it proceed), as there is a potential for "claims" to be made against individual directors and for the directors to be indemnified (where permitted by the general law). If covered, notification obligations arising under standard form clauses may need to be considered closely.
- Given that what is proposed are new statutory obligation(s) operating at an individual director level, we can foresee situations where boards facing difficult/contentious decisions may need to contend with the scenario that individual directors will require independent (and separate) legal advice on the potential consequences of their participation in the decision (in light of this new obligation). This could produce a series of unintended consequences (in terms of timing, costs, ineffective decision making etc).
- Further to the previous point, the proposed regime may lead to directors being reluctant to take the risks necessary to achieve above average returns. In other words, ineffective decision making could lead to a downturn in returns.
- There may be increased litigation for individual member complaints.
- It may be more difficult to attract talented directors as they will be more likely to take up positions in banks and life companies without personal liability.

ASFA makes these further brief comments in regards to recommendations 2.1(a), 2.1(c) and 2.1(e):

- It is proposed that directors be required to act solely for the benefit of members.

  However, there are a number of problems with this proposed duty:
  - the "best interests" formulation has a well-established meaning while the proposed requirement does not;

    - a requirement to act "solely" for the benefit of members is, ASFA submits, unworkable in practice and has the potential to put many directors, such as those who are paid directors' fees and those who take into account the long-term impact of their decisions on "the community" (being something they would all be required to do - see below), in breach from day 1; and
    - why just act solely for the benefit of members and not also for the benefit of beneficiaries?
- the proposed requirement for a director to exercise "independent judgment" sounds reasonable but, practically, how does a director *prove* that they did?
- the proposed requirement to consider the long term consequences of the decision again sounds reasonable, but what is "the community" and how does this square with the requirement to act "solely" for the benefit of members and further, how does it sit with the sole purpose test?

We thank you for providing us the opportunity to make these further submissions and more generally for the opportunity to participate in the Treasury consultation process

Yours sincerely

David Graus
General Manager, Policy & Industry Practice