CHARTERED SECRETARIES AUSTRALIA

Leaders in governance

16 May 2012

Manager
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By email: strongersuper@treasury.gov.au

Dear Treasury

Exposure Draft – Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012

Chartered Secretaries Australia (CSA) is the peak body for over 7,000 governance and risk professionals. It is the leading independent authority on best practice in board and organisational governance and risk management. Our accredited and internationally recognised education and training offerings are focused on giving governance and risk practitioners the skills they need to improve their organisations' performance and are 'first-choice' options for those intent on pursuing a C-suite career.

CSA has unrivalled depth and expertise as an independent influencer and commentator on governance and risk management thinking and behaviour in Australia. Our members are all involved in governance, corporate administration, legal practice and compliance with the *Corporations Act 2001* (the Act) with their primary responsibility being the development and implementation of governance frameworks in public listed and public unlisted companies, private companies, and not-for-profit organisations.

CSA welcomes the opportunity to comment on the Exposure Draft – Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 (the exposure draft) and draws upon the experience of our Members in formulating our response.

Time frame for consultation

From the outset, CSA wishes to again raise its concerns about the period of time for consultation being wholly inappropriate for feedback on the exposure draft. CSA notes that the consultation period amounts to a mere 15 working days for consultation on the third tranche of legislation implementing the government's Stronger Super reforms. This is unacceptably short.

CSA again notes that these time frames do not accord with the recommendations of the Banks Report[1] and, in particular, the principle which requires effective consultations with stakeholders,

[1] Treasurer of Australia, *Report of the Taskforce on Reducing Regulatory Burdens on Business – Final Government Response*, Media Release, 15 August 2006.

or the government's own guidelines on consultation as found in Appendix C of the Department of Finance and Deregulation's *Best Practice Regulation Handbook* (June 2010), which recommends a consultation period of between six and 12 weeks, depending on the significance of the proposal, citing the United Kingdom Government's Code of Practice on Consultation which stipulates a minimum of 12 weeks for written consultation at least once during the policy development process.

The *Business Checklist for Commonwealth Regulatory Proposals* (the Checklist), which has endorsement from a number of leading professional associations representing diverse stakeholder interests, furthers the principle of effective consultation and recommends that consultation periods be at least 30 days and longer for more complex consultations.

Recently, however, CSA notes that there have been several consultations on different topics issued by the government which have not adhered to these guidelines. CSA is disappointed, therefore, that despite constant feedback on the inappropriateness of various consultation time frames, our comments in this regard have been neither acknowledged nor addressed.

Our concerns with inadequate time for consultations reside with the problems which arise from insufficient or inappropriate consultation. In the first instance, CSA notes that a short time frame provides insufficient time to canvass views and generate discussion among stakeholders and potential respondents. This is particularly difficult where there are multiple consultations about a diverse range of issues, all with similarly short timeframes. Stakeholders do not have sufficient time to review each of the proposals independently and then must prioritise those which require their attention. When stakeholders are faced with these competing demands, it cannot be said that effective consultation is taking place.

The second issue is that of unintended consequences attached to rushed drafting and insufficient time to provide input on the practical implications of the drafting. In relation to the exposure draft, this issue is particularly salient as the content of the document is largely technical in nature. Stakeholders, therefore, need to invest time in canvassing the issues and undertaking informed discussions, with a view to providing constructive feedback. The failure to address all the issues which arise from the drafting of the exposure draft might result in drafting errors, as occurred with the Corporations Amendment Bill consultation in late 2011, where a drafting error saw many shareholders disenfranchised of their voting rights. The drafting error, which the government still has not resolved, is one which required the time and effort, of our Members, legal advisers, the regulator, and other stakeholders, to address the negative consequences and ensure that companies were not in breach of their statutory obligation. CSA notes that this error could have been avoided if sufficient consultation time had been provided in the first instance, as the error was brought to light not long after the close of the consultation period.

For these reasons, CSA believes that the government needs to restate its commitment to ensuring that consultations are carried out appropriately and with due consideration to the timing and abilities of stakeholders to respond. It is important that consultation is genuinely designed to seek input on policy formulation, rather than as a 'box-ticking' exercise which has been undertaken after a policy decision has effectively been made. CSA notes that the government must ensure that it does not utilise consultation as a way of legitimising policy outcomes, when in fact insufficient consultation has occurred.

Building stronger governance for Stronger Super

CSA is broadly supportive of the third tranche of legislation implementing the government's MySuper and governance changes. CSA is in strong accord with the intentions of the Stronger Super reform package, particularly in light of the public interest in ensuring a more transparent superannuation system for Australia's ageing population. CSA believes that the focus on governance will help to address the traditional opacity of the superannuation industry.

CSA recognises the focus on increasing disclosure and access to information for the public, which is at the heart of the current reform package, particularly elements such as the details of

director and executive pay; the details of assets in which the fund has invested; and the inclusion of the 'product dashboard', setting out information about the performance of funds. However, CSA believes that the exposure draft does not go far enough in terms of disclosure requirements.

CSA supports the widely held view that superannuation funds are far less transparent to members than companies are to shareholders. CSA has previously advocated for the superannuation disclosure regime to mirror the reporting requirements of listed entities under the Australian Securities Exchange (ASX) Corporate Governance Council's *Corporate Governance Principles and Recommendations* (the Principles and Recommendations). This framework is one which offers a model for good practice against which corporate reporting takes place. All listed companies must report against the Principles and Recommendations on an 'if not, why not' basis, and they provide a consistent structure for those stakeholders wishing to understand the governance of companies listed on the ASX. The Principles and Recommendations offer a flexible framework for the corporate governance of listed companies, irrespective of their size or industry, providing transparency and accountability to their investors, the wider market and the Australian community.

CSA Members firmly support a principles-based approach to corporate governance, rather than a rules-based approach, as there is no 'one-size-fits-all' approach to many governance issues facing companies. A principles-based approach provides insight into board decision-making, allowing companies to meet the 'spirit' of the Principles and Recommendations through whatever means they believe are most appropriate to their business, provided they explain their approach. CSA believes that it is for shareholders to test directors' thinking and behaviour through shareholder engagement and for boards to be accountable to justify their decisions to shareholders.

However, CSA is of the view that the current superannuation model does not provide this opportunity to the vast number of Australians who have become indirect shareholders through the investment of their superannuation savings and contributions.

While CSA recognises that the model of superannuation governance needs to include a strong legislative regime which recognises the unique circumstances of compulsory superannuation, we believe it also needs to allow superannuation funds the freedom to organise themselves and respond effectively to the needs of their members. A 'one-size-fits-all' approach is not an appropriate approach to corporate governance, or member investment needs, and CSA strongly believes that transparency as to decision-making is paramount to the reform process.

CSA, therefore, advocates that alongside the changes to disclosure set out in the exposure draft, namely; the reporting of remuneration provided to the trustees/directors and CEO; and the reporting of performance of the fund's investments through the product dashboard, the following disclosures should also be mandatory for superannuation funds:

- the fund managers to whom the trustee outsources the management and investment of the superannuation fund
- any adverse findings issued by the Australian Prudential Regulation Authority (APRA) against the superannuation scheme
- the names of all trustees or directors where it is a corporate trustee and the period of office held by each trustee or director in office at the date of the annual report
- the number of trustee or board meetings held during the year and the number attended by each trustee/director
- whether performance evaluations of the trustees, or board and its committees have taken place in the reporting period.

CSA is in accord with the requirement in the exposure draft that these disclosures are made publicly available, ideally by posting them to the superannuation fund's website in a clearly marked governance section. CSA also recognises that not all members will access the fund's website, and we recommend, therefore, that these disclosures also be made in the fund's annual report, which is sent to all members.

Fees, costs and intra-fund advice

CSA acknowledges the importance of establishing protocols for the charging of financial advice, including intra-fund advice, and the general fee rules that will apply to regulated superannuation funds and approved deposit funds. All Australians have risks associated with superannuation as a result of the investment of superannuation funds and it is a matter of public policy that disclosures provide meaningful information to the public. CSA is cognisant that the current structure of the superannuation industry does not provide clear advice about the derivation and operation of fees.

It is important, therefore, that the legislation provides clear guidance around the disclosure of fee structures, so as to promote transparent and accountable conduct on the part of investment managers. However, while CSA is supportive of the inclusion of criteria in the formulation of assessing fees and charges, CSA is also aware that there needs to be a balance struck between legal regulation and the role of the board and CEO in determining matters of remuneration for managers.

CSA notes that clause 1.21 stipulates the five criteria which must be contained in the terms of the arrangement the fund has with an investment manager if there is a fee that is determined, in whole or in part, by reference to the performance of the investment made by the investment manager on behalf of the trustee or trustees of the fund. In particular, CSA notes that the third criterion (detailed in clause 1.29) requires that the performance of the investment must be measured by comparison with the performance of investments of a similar kind.

CSA is concerned that this criterion interferes with the business objectives of superannuation funds in determining their own levels of remuneration. While CSA acknowledges the benefit of comparability of funds in assessing performance and the interest in aligning the interests of fund managers with beneficiaries in determining rewards for performance, CSA believes that there may be instances where the board and CEO determine that investment in longer term assets, or ones which appreciate more slowly than comparable funds may be appropriate. In the same way in which corporations no longer pay a dividend purely on profit, but instead look to the overall solvency of the corporation, CSA notes that comparative fund assessment must also be placed in the context of the overall financial performance of the superannuation fund.

CSA believes that it is a matter for the trustees of each superannuation fund to measure and report on their performance. CSA does not believe that a ‘one-size-fits-all’ approach to measurement of performance, such as return on investment, will be of benefit to all members, in all circumstances. CSA notes that a trustee will appoint fund managers with different styles to accommodate the different investment choices that members will wish to make, as members will choose a different investment strategy according to the circumstances of their needs at the time. For example, younger members may wish to choose higher-risk, higher-growth investment strategies, while members closer to retirement may wish to make lower-risk, lower-growth investment strategies. CSA notes that the exposure draft does not allow for the market risk involved in investment decision making.

For these reasons, CSA believes that the key element in relation to performance of the investment must be disclosure by funds to their members how their investment structure is linked to the investment policy. This will ensure that there is transparency as to decision-making and members will be able to make informed investment decisions. CSA believes that good governance can also be demonstrated where boards report to members on factors such as whether the board met during the year and whether the trustee board monitored performance of all aspects of the fund, alongside their obligations to report on specific investment performance. Where disclosure of the performance of the investment and information about fees and charges provided to fund managers is disclosed, members have the ability to peer into the longer term investment strategy of the superannuation fund and to determine if it aligns with their interests.

Collection and disclosure of information

CSA supports the belief that there is no standardised methodology for calculating and disclosing relevant fund or investment option information [clause 3.2]. CSA recognises that there is no 'one-size-fits-all' approach to investment governance which is appropriate in all circumstances. Instead, CSA believes that it is preferable that the legislation adopt a broad, overarching, and principles-based approach to disclosure as discussed above.

CSA notes the requirements spelt out in clauses 3.8-3.12 to publish a product dashboard and other information, including the remuneration of directors and executive officers. While CSA strongly supports the emphasis on the disclosure of relevant information, we also retain some concerns with the prescriptive nature of the product dashboard and the relative ambiguity of the terms of remuneration which will be reported.

CSA recognises that the aim of the product dashboard is to establish fund comparability, through requiring consistency in how information is calculated, as detailed in clause 3.53. This will provide beneficiaries with up-to-date, accurate and complete information about investment returns. However, CSA notes that care needs to be taken in defining the specific elements that the dashboard will be required to display, as standardising any methodology for calculating and disclosing relevant fund or investment option information is a difficult process.

CSA believes that a more high-level approach could be adopted. The public policy benefit, CSA believes, is to provide information to members to allow them to make informed investment decisions. As expressed in the exposure draft, the purpose of the dashboard would not necessarily be clear to beneficiaries. For example, CSA notes that clause 3.8 of the explanatory memorandum requires the product dashboard to contain information on:

> The investment return target and the number of times the target has been achieved, level of investment risk, a statement about the liquidity of the product and a measure of the average amount of fees charged in relation to the product on a per member basis.

While this information is certainly pertinent to an investment decision, the disclosure process should emphasise quality, not quantity. CSA is concerned that where numerous disclosures are required, the volume of disclosure may not assist members to obtain clarity as to investment policy and how it is aligned with the interests of beneficiaries. Disclosure of multiple facts does not of itself promote transparency. Moreover, CSA is also concerned that some superannuation funds may be adversely impacted by the proposed legal requirements. CSA notes, for example, that the numerous disclosure obligations will increase the fund's administrative burden, thereby requiring an increase in member fees to support additional staff. Without clarity as to why quantity rather than quality of disclosures achieves the public policy benefit of providing transparency into investment decision making, such additional costs, that in turn are costs to members of the superannuation fund, are difficult to justify. CSA notes that the exposure draft and explanatory memorandum contain no costing analysis of the additional compliance and the effect this will have on fees payable by members. CSA is also concerned that a possible unintended consequence could be the rolling over of company superannuation funds into industry superannuation funds due to the increased compliance costs. CSA is of the view that this is not the intent of the legislative reform process, and would be very concerned if this was the outcome.

CSA strongly emphasises that the alternative is not a reduction in disclosure obligations, but rather to make disclosure about the operation, remuneration and performance of superannuation funds more meaningful. CSA believes that the terms of disclosure, therefore, need to be based on principles and not be prescriptive or granular as they currently are in the exposure draft. CSA strongly recommends that the governance statements should be expressed as simply as possible, given that the range of people affected by superannuation is very varied.

As noted earlier, the exposure draft does not include all of the matters which CSA believes are important to disclose. For example, CSA notes that without higher level principles which elaborate on the purpose of disclosures of remuneration, the exposure draft does little to tackle issues such

as related-party transactions and material personal benefits. CSA notes further that remuneration may be paid by either a director or executive's fund, or a related third party, and that the current provisions do not capture remuneration from associated organisations.

For example, CSA notes that clause 3.51 states that the regulations will codify the requirements for a superannuation fund to publish the name and a brief biography of each director or trustee, or person involved in the trusteeship of the fund, but that this clause stops short of requiring the director or trustee to disclose other appointments. Such a disclosure requirement is the means by which material personal interests, ability to commit sufficient time to the trusteeship of the fund, or potential conflicts of interest can be identified.

In a similar manner, while CSA supports the requirement for funds to publish the remuneration of directors and executive officers, CSA is also of the view that the disclosure of the remuneration of directors and executive officers of the superannuation fund will not of itself provide transparency. Rather, CSA believes that the issues that go to the heart of transparency and accountability with respect to remuneration are:

- disclosing the remuneration provided to service providers, where conflicts of interest may arise, and
- disclosing the remuneration of the investment managers who make the investment decisions, and how these decisions are aligned with the risks to the organisation.

CSA believes that these are the types of matters that disclosure for the superannuation industry needs to address and that unless a high-level, principles-based approach is adopted; the legislation will fail to achieve its intended outcomes.

CSA points to the framework for disclosure in the *Corporations Act 2001* (the Act) as a model for the disclosure of both remuneration and conflicts of interest. For example, the operation of s 191 of the Act provides for a standing item of directors being required to disclose conflicts of interest.

CSA believes there is merit in legislation governing the superannuation industry to set out similar high-level duties to act in good faith, avoid and/or disclose to the board real or apparent conflicts of interest and not seek personal profit. CSA notes that any such codification of duties should contain explicit provisions enabling trustees to override deeds that require the trustee to invest or outsource within the corporate group, and that this would assist in reducing apparent or real conflicts of interest.

Establishing these high level principles, as codified in law, will provide the requisite guiding values for disclosures by superannuation funds and any such codification would largely act as an education tool rather than changing responsibilities, as those responsibilities already exist in trustee law. CSA, therefore, notes that codification of these duties would not be an unreasonable imposition on the superannuation industry.

However, CSA also realises that the Act provides only a framework for reference in application to the superannuation industry. It would not be advantageous to try and subject superannuation funds to the current requirements of the Act. For example, CSA notes that in dealing with conflicts of interest, if the trustees cannot form a view that a commercial transaction is in the best interests of the members, the decision whether to proceed should not go to members, as it would under the corporations law.

Instead, CSA recommends that the principles governing related party transactions for superannuation funds should be based on the trustees forming a decision, subject to the following:

- if the transaction is material and non-commercial, it cannot proceed
- if the transaction is not material and non-commercial, the trustees may form a view that it can proceed
- any person or trustee with a material interest should not participate in discussion or voting on the matter

- if a quorum of disinterested trustees / directors is unable to be formed, the matter should not proceed.

Subject to carve-outs for matters such as D&O insurance and trustee/directors' fees, where all trustees have an interest in the matter, CSA notes that the high level principle, that is, the duty of acting in good faith and not for personal benefit, is maintained.

CSA reiterates that the structure of the superannuation industry is not conducive to a replication of the current corporations legislation. However, the establishment of a framework which mirrors the current corporate regime is preferable to implementing a legislative regime for the superannuation industry that differs substantially from the corporations law and applies different definitions to identical issues.

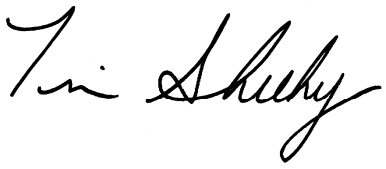
Conclusion

Establishing a disclosure regime for superannuation funds needs to take into account the complexity of the superannuation industry and the need to provide transparency in relation to the governance and operation of funds, which has been largely obscure when viewed in comparison to corporations. CSA strongly recommends that the governance of funds needs to be based on a high-level, principles-based approach which ensures that the disclosures made to members provide the right information for them to make informed investment decisions.

The operation of the Act in terms of setting out high-level duties, and the flexibility provided by the ASX Corporate Governance Council's Principles and Recommendations provide a foundation for an approach to governance disclosures that will best serve the interests of members. The superannuation industry requires its own model, unique to its own circumstances, but CSA is of the view that a high-level, principles-based approach is more likely to provide members with the window into director and trustee decision making than a prescriptive approach. The principles-based approach has been shown to engender cultural change in corporations, with the governance of Australian listed companies among the best in the world. A prescriptive approach, as has been evidenced in other jurisdictions, tends to a view of governance as a set of compliance obligations rather than an opportunity to engage with members on performance and conformance. CSA strongly believes that more can be done to ensure that the superannuation industry also undergoes the change in culture required to achieve better governance outcomes.

CSA would welcome the opportunity to discuss any of our views in greater detail.

Yours sincerely



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