

# ASFA Submission to the Cooper Super System Review

## Phase One: Governance

### Covering Letter

October 2009

Association of Superannuation Funds of Australia

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## ASFA Submission - Super System Review – Phase One: Governance

The Association of Superannuation Funds of Australia is pleased to provide this submission in response to Phase One – Governance, of the Review by the Australian Government into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (the Review).

ASFA is a non-profit, non-political national organisation whose mission is to advance effective retirement outcomes for members of superannuation funds through research and advocacy. We focus on the issues that affect the entire superannuation industry. Our membership, which includes corporate, public sector, industry and retail superannuation funds, has as members over 90% of the approximately 12 million Australians with superannuation.

Our Constitution requires that we promote and protect the interests of superannuation funds, their trustees and their members. As such we conduct extensive research, engage our membership in debate and offer what we believe is sound public policy which rises above vested interests.

### Superannuation Fund Governance Report Card: "good, but could improve"

ASFA contends that, in general, Australian superannuation funds are well governed by their trustees, with the assistance and support of the trust structure, a strong regulatory framework and effective regulators.

ASFA promotes best practice in governance and operation of superannuation funds through our series of Best Practice Papers. The wide use of these Best Practice Papers amongst superannuation funds demonstrates that the industry takes its governance responsibilities very seriously. ASFA also promotes good governance through a range of training courses such as "TrusteeKnowHow" and the "ASFA AIF" investment fiduciary course (which gives trustees an internationally recognised designation as an investment fiduciary).

We believe the current superannuation governance model is working very effectively and there is no evidence to suggest it is broken. This was demonstrated by the fact that Australia's superannuation funds have weathered the storm of the recent Global Financial Crisis (GFC). Whilst there have been some significant reduction in value of the accounts of individual fund members, those members who remained invested have already experienced a substantial recovery in their account balances. The key point is that no APRA-regulated superannuation fund has failed during the most severe financial crisis in eighty years, although some funds had to restrict withdrawals from some investment options due to liquidity concerns caused by the freezing of underlying managed investment schemes. This is in contrast to the situation overseas where many pension funds (including some national schemes) are in severe financial stress.

Whilst superannuation is generally well governed, there are some areas where we recognise that improvements can be made. Our response to the consultation questions are set out in Appendix 1 in which we highlight these particular areas and provide recommendations for improvement.

By way of a summary, we provide a brief discussion below in respect of 10 key governance areas:

- 1. Minimum competency standards:** Whilst we recognise that each trustee brings to the board their own set of skills (eg. general business skills, accounting, investments etc), it is important to ensure there are minimum competency standards and expertise for all trustees/directors (particularly in relation to governance) for the protection of not only fund members, but also the personal protection of trustees/directors. Therefore, a minimum competency standard and ongoing CPD requirements should be introduced for trustees (including SMSF trustees, but at a different level);
- 2. Policy on trustee composition, selection, removal, tenure and succession planning:** Trustees should implement a governance policy which considers board composition (including age and gender balance issues), maximum tenure on boards (possibly by way of fixed renewable terms), together with appropriate selection, removal and succession planning processes;
- 3. Independent directors:** There should be no requirement for trustee boards to have independent trustees, however boards should have the option of appointing them if they wish. Any impediments regarding the appointment of independent trustees should be removed, including the requirement for APRA approval to have more than one independent trustee on a board.

- 4. Clear Conflict of Interest rules:** Trustees should have a clear and transparent policy in place to manage actual and perceived conflicts, and to avoid situations where conflicts of interest or conflicts of duty are so great that they cannot in practice be managed. The policy should include general principles to be used in managing different types of conflict which may arise from time to time. We believe the relevant tests which trustees should apply should include, “how would members perceive such a conflict?”, “does it compromise open discussion at the board table?” and “does it impact on the directors’ duty to act in the best interest of the fund’s members?”.
- 5. No regulatory direction or prescription on investments:** ASFA does not support restrictions being imposed to enforce more diversification to other asset classes, nor any directed investments – i.e. Government directions to invest or not invest in certain classes of assets (such as venture capital, infrastructure, regional development, research and development, housing, forestry and small business). It should be left up to each trustee to formulate and give effect to appropriate investment strategies under section 52 of SIS, and there should not be any regulatory direction or prescription in relation to investment matters;
- 6. Consolidation of the industry:** Provided that trustees satisfy themselves that the current size and structure of their fund meets their members’ needs, then the “size” of the fund should not matter. However, trustees should be assessing the suitability, efficiency and sustainability of their fund on an ongoing basis. Compulsion in this regard is not required. Competition and regulation, as well as APRA licensing, has done much to encourage consolidation. There will always be a place for niche providers (such as small defined benefit funds). Further consolidation will occur naturally as a result of continued competition within the industry;
- 7. Rationalisation of legacy products:** There are impediments which can make product rationalisation a lengthy, complex, risky and expensive process, such as legal constraints and the potential adverse tax consequences for investors (eg. exposure to Stamp Duty). Legislative change is required in order to remove these impediments without diluting consumer rights, such as the introduction of a single legislative mechanism to enable financial product rationalisation and the amendment of State Stamp Duty laws, to provide tax neutrality where product rationalisation has been undertaken;
- 8. CGT relief extension:** In order to facilitate the cost effective merger of funds, and protect the interests of fund members, capital gains tax and loss relief on all fund mergers should be made permanent;
- 9. Trust model for super:** It can be argued that the trust structure is still appropriate for the super industry. However, there is an overriding issue in that the current SIS legislation is inflexible. That is, SIS does not provide the flexibility to cater for sub-trusts. Neither does it provide the flexibility to cater for different categories of members, such as accumulation phase and retirement phase members, a situation which occurs in many superannuation funds and will be a growing issue as more funds offer retirement products. The SIS legislation should be amended to reflect the different duties that trustees may have in relation to different sub-trusts or groups of members. These different duties may be at odds with the common law fundamentals of a fiduciary which expect the trustee to treat all members equally. We recognise that this is a complex area of law and further investigation would be required.
- 10. Regulatory Governance:** An issue which has been vigorously debated by ASFA’s membership is whether or not there should be a single regulator for superannuation, with many arguments elicited both for and against the single regulator proposition. However, there are strong views that, given the presence of financial conglomerates, if there was to be a single regulator, that single regulator should regulate the entire financial services industry (not just superannuation). ASFA believes that the current arrangements of ATO, APRA and ASIC are being tested, particularly in relation to criminal activities such as “illegal early release”. We also note there is duplication of activities, as well as risks that issues may fall between the gaps and that dialogue and referrals between the regulators may not always be consistent. There is also the question as to whether superannuation legislation, which is fragmented, should be consolidated in one cohesive instrument. One centralised piece of legislation which is specifically tailored for, and addresses the particular nuances of, superannuation could be a more effective way to regulate the industry. However, whether it is constitutionally possible to incorporate multiple pieces of legislation into one Act for superannuation is questionable.

The abridged responses to the consultation questions, together with discussions on the other issues which ASFA feels are important for the Review, can be found at Appendix 1.

#### **A principles based, not a prescriptive approach**

Many of the questions in the consultation paper are of a very detailed nature and suggest that the Review Panel is considering a more prescriptive approach to governance - that is, that trustees should have less discretion to exercise their judgement.

The current regulatory regime for superannuation uses a principles based approach, rather than a prescriptive approach,

and we believe that this approach should continue.

ASFA encourages the Review Panel to make recommendations which ensure:

1. there is a strong framework in place for effective governance (including removal of any impediments to effective governance);
2. trustees have the skills and competencies to discharge their fiduciary duty; and
3. the Regulators are able to properly supervise the system.

Once these three elements are in place, there is no need for an overly prescriptive approach and superannuation fund trustees should be left free to exercise their fiduciary duty under trust law to act in the best interest of their fund's members.

ASFA will continue to develop our range of training courses, CPD opportunities and Best Practice Papers to support trustees in performing their duties.

### ASFA Superannuation Fund Governance Framework

Governance theory and methodology used in the superannuation industry has been adopted from material developed for other industries.

ASFA has been working over recent months to develop the ASFA Superannuation Fund Governance Framework which sets out what ASFA expects as minimum foundations for good governance for the superannuation industry to ensure that the governance structure is comprehensive and robust.

The actual governance model for a particular fund depends on its individual circumstances, and each superannuation fund would use and modify our Governance Framework tool, to suit its needs and circumstances, ensuring in the process that the basis of the governance framework and its minimum requirements are followed.

Our preliminary ASFA Superannuation Fund Governance Framework is as set out in the following two diagrams and is further explained in Appendix 2.

Diagram 1

### ASFA GOVERNANCE MAP

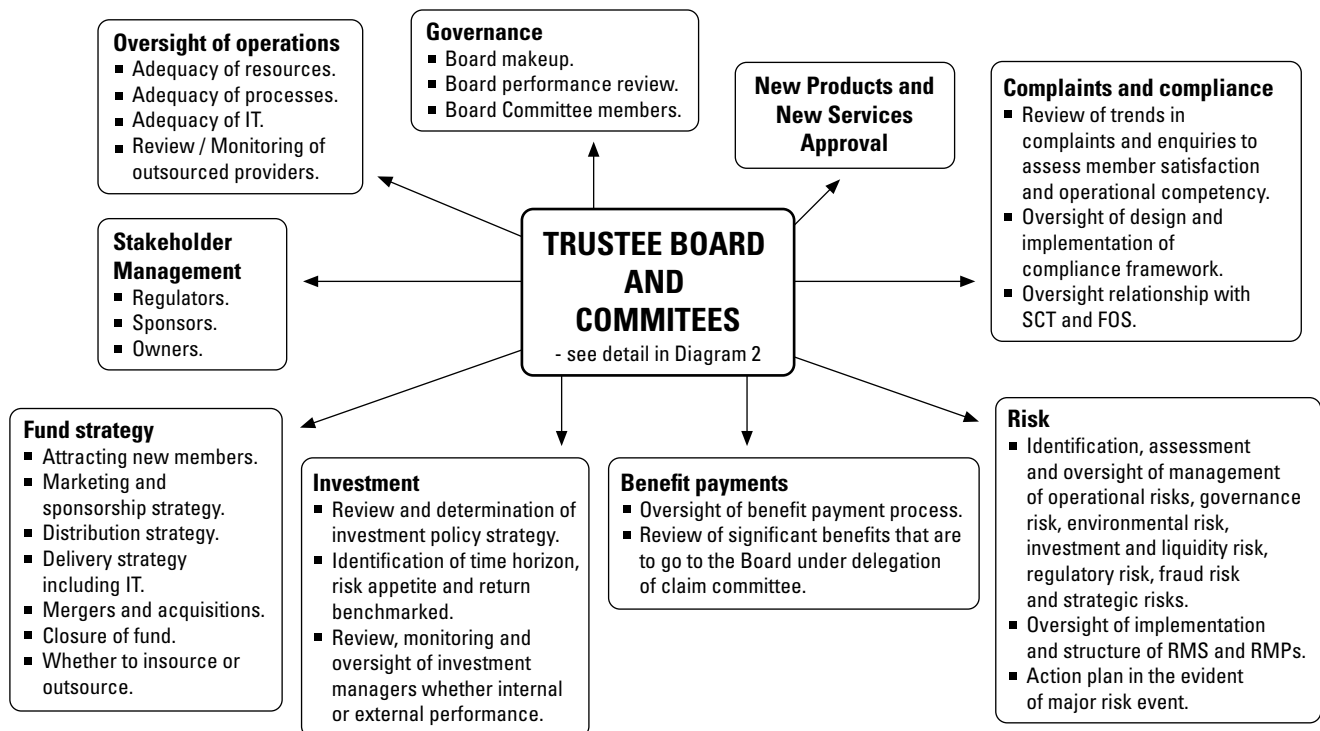
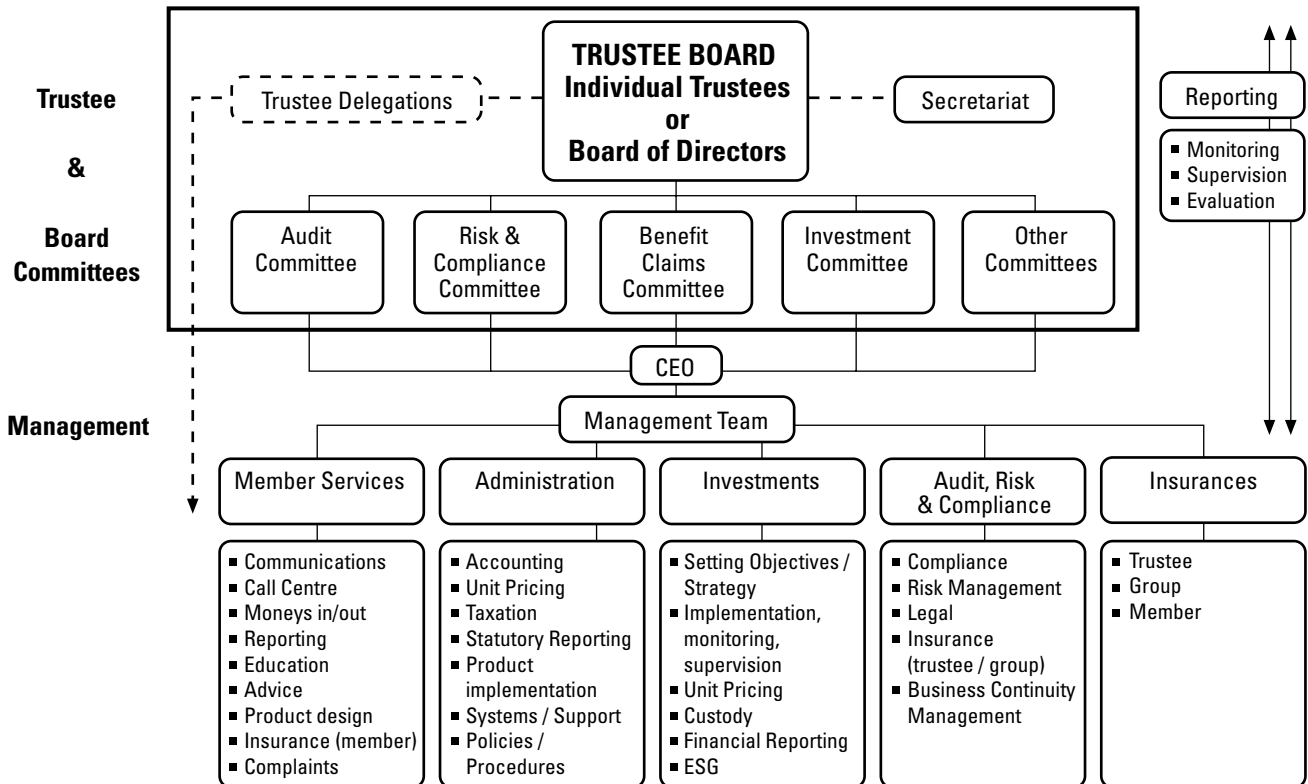


Diagram 2



**ASFA Framework for Superannuation Fund Governance**

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**ASFA Best Practice Paper 7- Superannuation Fund Governance**

ASFA deals with issues around Superannuation Fund Governance in our range of Best Practice Papers. The overarching paper on governance is Best Practice Paper 7 entitled "Superannuation Fund Governance: Understanding the framework, addressing the issues".

The paper was first developed by the ASFA Policy and Industry Practice team in May 2000, and has been updated in 2004, 2007, and 2008 to reflect the increased expectations of superannuation fund trustees by fund members, legislators and regulators. It provides superannuation-specific recommendations based upon the ASX's governance principles together with practical suggestions to assist trustees to implement the recommendations. Where applicable trustees are referred to other ASFA Best Practice Papers for more detailed information on particular governance issues. As detailed below, this paper is currently undergoing a major review.

**ASFA Review of Best Practice Paper 7**

As a result of the development of the new ASFA Superannuation Fund Governance Framework, ASFA has commenced a review of Best Practice Paper 7. The review is being run by ASFA's Regulatory Affairs subcommittee in consultation with representatives and governance experts from within the superannuation industry. The aim of the review is to align the material in the paper with the newly-developed framework, and address any areas in the framework that are not currently covered in the paper.

I trust that the information contained in this submission is of value. We would be please to meet with you to discuss our submission.

Yours sincerely

Melinda Howes  
Director of Policy & Industry Practice

*Enclosures*

- Appendix 1: Abridged responses to the consultation questions
- Appendix 2: ASFA Superannuation Fund Governance Framework