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Mr Shon Fletcher
Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Email: corporations.joint@aph.gov.au

Dear Mr Fletcher,

INQUIRY INTO THE SUPERANNUATION LEGISLATION AMENDMENT (MYSUPER CORE PROVISIONS) BILL 2011

The Association of Superannuation Funds of Australia (ASFA) would like to provide this submission in relation to the Committee's inquiry into the *Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2011* ("Bill").

About ASFA

ASFA is a non-profit, non-political national organisation whose mission is to protect, promote and advance the interests of Australia's superannuation funds, their trustees and their members. We focus on the issues that affect the entire superannuation industry. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90% of the 12 million Australians with superannuation.

Comments of the Bill

We have some comments on the timing of the implementation, which we have addressed in this letter, and on some technical aspects and drafting issues with the Bill which we have enclosed in an annexure.

1) Need for longer transitional period on obligation to pay default contributions into MySuper Offering

The Bill is scheduled to come into effect from 1 July 2013 to allow MySuper offerings to be made from that date. Of greater significance is that with effect from 1 October 2013 an employer making contributions with respect to the Superannuation Guarantee legislation ("SG") which are "default" contributions must make those contributions to a MySuper offering. ASFA strongly believes that the employer compliance date of 1 October 2013 must be extended to 1 July 2014.

While ASFA supports the Stronger Super reforms, it is important to note that compliance with these reforms will necessitate considerable changes being made to a mature and complex superannuation system. In addition the Future of Financial Advice reforms, which are due to commence during the same period, will also have a significant impact on the structures of some superannuation funds.

Some trustees will need a great deal of certainty in relation to the legalisation to be able to make the threshold decision as to whether or not to provide a MySuper offering. This is the case in particular where a relatively small percentage of contributions are default contributions.

Following the threshold decision there is a variety of strategic and tactical decisions which need to be made. As we are unlikely to see final legalisation in the first half of 2012 the time afforded to implement is greatly reduced.

Implementation of the legislative requirements will involve the identification of, and agreement upon the approach to, considerable and extensive alterations to IT systems; processes and procedures and fund documentation such as governing rules and product disclosure statements. Business requirement documents, let alone functional and technical specifications, cannot be agreed upon and signed off, nor most IT systems work commenced, until such time as there is a high degree of legislative certainty.

Change management on this kind of scale and degree of interrelatedness is not only expensive but, more importantly, making significant alterations to member databases and IT systems poses considerable risks of lost or corrupted data or functionality, which at worst can result in inaccurate or incomplete member records. The most effective means by which such a risk is mitigated is by utilising robust project management methodologies to determine timelines; identify interdependencies; produce a staged project plan; include sufficient time for regression and user acceptance testing, and then execute in accordance with the plan.

All of this takes time and resources.

Often there are capacity constraints, interdependencies and unintended consequences, especially when it comes to implementing system changes. Rushing to meet deadlines materially increases the risks to a project and can increase costs which are ultimately born by the member.

Any delays in, or changes to, any aspect of either the Stronger Super or FOFA legislation will significantly impact on some trustees' abilities to implement the required changes in an orderly and appropriately risk-managed fashion.

At this time only the first tranche of the MySuper legislation has been introduced into Parliament – the Bill – while the consultation period with respect to an exposure draft of the second tranche (trustee obligations and prudential standards) has only just closed. There are a number of issues to be addressed in the third tranche, which is yet to be released as an exposure draft, let alone introduced as a bill into Parliament. Similarly, APRA will not be releasing draft prudential standards until early to mid 2012, which will not be finalised until mid to late 2012. Many of these standards directly impact MySuper offerings.

It should be noted that the Regulation Impact Statement with respect to the Bill stated as follows (emphasis added): -

- "[t]he requirement that employers have to make default contributions to funds offering a MySuper product from **1 July 2014**" (Page 15);
- "It is expected most trustees will offer a MySuper product so they are able to accept default contributions from **1 July 2014**" (Page 17);
- " ... some MySuper products may not be licensed until close to **1 July 2014**" (Page 20)

We submit that – in order to mitigate the risks outline above – the three months from 1 July 2013 to 1 October 2013 is not an appropriate transitional period. While funds should be able to have MySuper offerings from 1 July 2013, the period from which default contributions must be made to a MySuper offering should not commence until 1 July 2014.

2) Impact of absence of Capital Gains Tax roll-over relief

The absence of Capital Gains Tax ("CGT") roll-over relief and the fact that many funds are carrying deferred tax assets may necessitate many trustees (who may otherwise have considered entering into a successor fund transfer arrangement to merge their fund with another) to expend considerable time and resources creating a MySuper offering which would otherwise not have needed to have been created.

We note that CGT relief may be granted where APRA forces a fund to merge after the MySuper legislation is in place. In our view this is inadequate as for this to happen the fund would have to establish its MySuper offering first which would be a waste of resources.

We strongly urge that if permanent CGT relief is not provided then as a minimum it should be provided from now until 1 July 2014. There is a clear precedent for this as similar relief was provided during the last APRA licensing transition period. It was also a clear recommendation from the Cooper Panel that such relief be provided in recognition of the extent of the transformation of the industry that stronger super will drive.

The absence of CGT roll-over relief creates a significant barrier to fund mergers.

In determining whether to merge with another fund, trustees of superannuation funds are under a trust law duty required to act in the best interests of members. Accordingly, any threshold decision as to whether or not to merge, as well as the specific decisions as to the other fund, the timing, the benefit design and cost allocation, are all made taking into consideration the various benefits and costs to members of the proposed merger.

The impact of the CGT tax represents a significant consideration when determining the costs of a proposed merger and may well be a critical, threshold, determining factor as to whether or not a merger is considered, negotiated or proceeds.

Currently some funds are carrying deferred tax assets equivalent to 1.5% or more of member account balances, which given the volatility of the market may well increase. The benefit of these assets is lost if a merger were to go ahead without CGT relief. For a member with an average account balance of approximately $70,000 this could represent a reduction in the value of their superannuation account of approximately $1,050.

Accordingly, the absence of CGT roll-over relief may cause the costs to members, through the extinguishment of deferred tax assets, to outweigh the benefits of any proposed merger.

In ASFA's view there is strong argument as to why permanent CGT relief can be provided. When it comes to CGT it is important to note that there is a distinction between where both the legal and beneficial ownership of an assets changes (a "total" change of ownership) and where only the legal ownership is transferred to another, leaving the beneficial ownership unchanged (a "legal" change of ownership).

From the outset the CGT regime has allowed rollover relief in circumstances where asset ownership changes were associated with business reorganisations, where no change occurred in the underlying beneficial ownership of the asset concerned or where the underlying assets against which the CGT taxpayer had a claim did not change.

We submit that the roll-over of CGT gains \ losses on successor fund transfers - where only the legal, and not the beneficial, ownership of the assets has changed - is entirely consistent with the business reorganisation rule which has been in place since 1985.

Accordingly, we submit that the CGT legislation should be amended to allow the roll-over of CGT gains\losses on successor fund transfers on the same basis as it is permitted under the business reorganisation rule.

3) Amendment of Trust Deeds

We also ask that, in lieu of the need for extensive amendments to be made to governing rules, that consideration be given to the Bill deeming the relevant provisions to be included in trust deeds in a fashion similar to that employed with respect to sub-section 52(1) of the SIS Act.

4) Branding and multiple MySupers

We acknowledge the public policy reasons for having a limited number of MySuper offerings in a single superannuation fund. In ASFA's view, however, the current wording does not facilitate legitimate alternate MySuper offerings within a fund, including multiple brands.

For example it is unclear why – in order for there to be two MySuper offerings in the same fund - the benefits of members and beneficiaries must be transferred in from another regulated superannuation fund and cannot, for example, be in an existing sub-plan of the same superannuation fund.

There are a number of funds which have a variety of different sub-plans. They exist because of the economies of scale which can be achieved by sub-plans coming together under a master trust or similar arrangement. These economies of scale will be lost if the trustee is forced to create a different fund for each of the sub-plans.

In addition, a trustee should be able to "white label" a MySuper offering for different groups. Each "white label" offering would have identical fees and benefits, however, the name and the "look and feel" would be able to be tailored for the different groups. This could be as little as producing PDSs and member statements incorporating different logos, colours and \ or themes.

Finally it is unclear as to what is meant by "material goodwill" in the current draft legislation.

We take it that the material goodwill is in the intellectual property rights in a particular brand and the inherent commercial value to the trustee as a consequence of the awareness of that brand. If so then why is this a necessary criteria (i.e. essential that it be demonstrated in all cases), as opposed to merely being a sufficient criteria (i.e. existence of criteria is sufficient to warrant exemption in that instance but does not preclude other cases)? Why cannot other criteria be taken into consideration in determining whether an exemption should apply? A "one size fits all" approach to the superannuation industry does not work due to the vastly different structures of providers.

Finally, it is of concern that, in addition to the trustee formulating an opinion, APRA must also be satisfied as to the existence and maintenance of material goodwill. In our view it is not within the role of a prudential regulator such legal and commercial assessments. This is the duty of the trustee as fiduciary.

5) Large Employer exemption – definition of 500 employees

If a numerical measure of 500 is to be employed we suggest that the measure be aligned with the prescribed class in regulation 3.01 of the *Superannuation Industry (Supervision) Regulations 1994* ("SIS regs"), which is the class of members, other than standard employer members, which non public offer funds are allowed to have without having to become public offer. This includes former employees, or relatives and dependants (generally spouses) of employees and former employees, of the employer - and its associates.

Further, with respect to the requirement that "any" employee may become a member - there may be instances where, owing to the industrial relations circumstances of the employer, it may not be possible for this to be the case.

Finally, it is unclear whether the trustee must make a separate application with respect to each large employer MySuper offering or can simply make one application with respect to being able to offer one or more large employer MySuper offerings. If it is the former then it is unclear as to why this should be the case, given that the only additional criteria are relatively narrow and capable of being determined "objectively" as a question of fact.

To compel the trustee to make a series of separate applications to APRA would prove an extremely inefficient process, consuming considerable resources and creating significant delays for little or no benefit. As a prudential regulator APRA has the power to assess large employer offerings as part of their regular reviews of funds.

6) Lifecycle investment option – investment fees

It is unclear whether a fund which offers a lifecycle investment offering will only be able to charge a single investment fee.

Each investment cohort will have a differently constructed portfolio of investments. This will directly affect the level of investment costs with respect to each portfolio.

If trustees are compelled to charge the same investment fee to all cohorts of members this will result in members who are in a more conservatively invested portfolio (generally older members) cross-subsidising those whose portfolio is invested more aggressively (generally younger member).

Given that one of the overarching principles of MySuper is that investment fees should be borne by members on a "cost recovery" basis it would appear anomalous that this should occur.

Accordingly, we submit that a trustee should be able to recover a different quantum of investment fees with respect to each portfolio. Importantly, once these cohorts are defined, all members within the same cohort of age and other similar characteristics, who are invested in the same portfolio, will have the same investment fee.

7) Pension

Given the attempt to move from the short-termism of focussing on the accumulation phase to a "whole of life" approach, it is disappointing that a MySuper offering is prohibited from paying a pension. While we appreciate there may have been insufficient time to develop rules around MySuper pensions, we recommend this be undertaken as a matter of urgency.

8) Prescriptive nature of drafting

Some of the drafting of the Bill - rather than being principles based – is too prescriptive and detailed. This can drive behaviour around avoiding the legislative intent and produce adverse outcomes, especially with respect to fees.

We are also concerned that the Bill contains a level of detail that may create an environment where inadvertent compliance breaches increase dramatically.

In relation to prescription, the Bill has introduced definitions which do not reflect current or future practices. The definition of "investment fees" in particular has ignored the importance of global standards which have been developed, such as the Global Investment Performance Standards, the ongoing development of outcomes reporting standards and the existence of industry standards. Whilst we agree that comparison of fees is essential, definitions should be developed between the industry and the regulator to ensure they continually reflect current practice and structures.

Adopting a prescriptive approach to drafting means the Bill cannot reflect the different products offered and the variety of decisions trustees make and there is a significant risk that it will stifle innovation.

We submit that the Bill should be principles based and not prescriptive in its approach.

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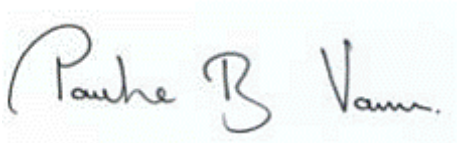
If you have any queries or comments regarding the contents of our submission, please contact me on (02) 8079 0805 or 0433 169 342 or by email pvamos@superannuation.asn.au.

Yours sincerely



Pauline Vamos
Chief Executive Officer

ANNEXURE

SUPERANNUATION LEGISLATION AMENDMENT (MYSUPER CORE PROVISIONS) BILL 2011

A) TECHNICAL ASPECTS

1) 29WA - Contributions in relation to which no election is made to be paid into MySuper

a) Elections as to choice products – historically given to employers not trustees

Under the SG legislation employers must give a "Choice of Fund" form to employees on commencement of employment which, inter alia, advises the employee of the "default" fund to which SG contributions will be made if the form is not returned. If an employee elects for SG contributions to be made to a fund other than the default fund they must return the Choice of Fund form to the employer, who must then make SG contributions for that employee into their "chosen" fund. Employees who are happy with the default fund do not need to return the form to the employer.

From a trustee's perspective, they frequently are unaware as to whether contributions are being made by an employer to a particular member's account because: -

- the fund has been chosen by the employer as their default fund and: -
  - the member is disengaged as to where contributions are made; or
  - the member is happy with contributions being made to that fund; or
- the member has exercised "choice of fund" to have contributions made to that fund (generally because they already are a member and on change of employment have decided to ask their new employer to contribute to their existing fund).

b) Proposed section 29WA – contributions for which no election to be paid into MySuper

Notwithstanding the above, section 29WA of the Bill creates a strict liability offence with respect to the following: -

> *"(1) This section applies if:*
> *(a) a person is a member of a regulated superannuation fund; and*
> *(b) a contribution to the fund is made for the benefit of the person; and*
> *(c) either:*
> *(i) the person has not given the trustee, or the trustees, of the fund* ***an election in writing that the contribution is to be paid*** *into a* ***specified choice product, or choice products****; or*
> *(ii) the person has given the trustee, or the trustees, of the fund* ***an election in writing to have some of the contribution paid into a specified choice product, or choice products****, but no such election has been made in relation to the remainder of the contribution" (emphasis added).*

c) Issues with section 29WA

(i) "Must treat any contribution"

Due to the complexities of administration systems ASFA submits that, in lieu of the obligation to ensure "any contribution" is paid into a MySuper offering, the requirement should instead be that "the trustee has processes in place to ensure that" such contributions are paid into a MySuper offering.

There should be recognition a process which provides that, upon identification of a contribution inadvertently paid into a choice product in error: -

- the transaction is reversed
- earnings are adjusted;
- fees are reimbursed; and
- the member is reinstated into the position in which they would have been had the error not occurred

is a process which satisfies this obligation.

(ii) "The" contribution

Proposed new paragraph 29WA(1)(c) makes reference to "*an election in writing that … **the contribution*** (i.e. the specific contribution – singular) *is to be paid into a specified choice product"* (emphasis added).

Accordingly, ASFA submits that, as a minimum, the Bill should be amended to make it clear that such an election covers "any" contributions in the future.

(iii) When election made

The need for an election in writing is onerous even if it were a "one-off" election "going forward", however, if a "back capture" of existing choice members is required this would be unduly onerous and would pose a considerable legal and commercial risk to trustees and to members. It is essential that funds be able to rely on existing instructions from members to determine that future contributions are to be placed in a choice offering.

Furthermore, diversion of contributions from a previously selected choice offering into a MySuper offering may put at risk insurance cover which is contingent on the receipt of contributions into the choice offering.

As such, the Bill should clarify that a valid election is one which may have been made either before or after the commencement of the MySuper provisions.

This would enable the trustee - when they receive a contribution for member who are in a choice offering – to be able to employ a "decision rule" to allocate contributions to that choice offering in accordance with the previous, standing, instructions from the member, irrespective of how long ago, or in what form, those instructions were received.

This reflects the legal and commercial reality that the member has exercised choice previously - to become a member of a choice offering and \ or to participate in member investment choice – and that standing instruction should prevail. It is also consistent with the underlying principles behind the SuperStream reforms, which reflect the desire to achieve the efficiencies and accuracy delivered by "straight through processing" of money and data upon receipt by the fund.

(iv) "In writing"

Further, it should be noted that not all elections to invest in a "choice product", through participating in member investment choice, are made in writing, as some funds allow member to effect member investment choice over the 'phone.

ASFA also considers it appropriate that superannuation funds be able to receive, and members make, an election other than in writing. This will necessitate amendments to the Bill, including removing references to members making "*an election in writing that the contribution is to be paid into a specified choice product, or choice products"*.

In summary, the Bill should not refer to elections being: -

- into a "specified choice product or products" – which confines the election to having occurred after the MySuper \ Choice regime has come in. The election should have been able to have been made at any time;
- with respect to "the contribution" which is to be paid – this confines the "election" to a specific contribution;
- "in writing" – this precludes investment choice instructions being received over the 'phone.

(v) Strict Liability

Even in the best regulated environment inadvertent administrative and clerical errors and omissions do occur, both on the part of the employers and with respect to fund operations. As such, ASFA is concerned with a breach of section 29WA being a strict liability offence.

It is important to note that, even if an error were to occur, an inadvertent misdirection of a contribution into a choice offering as opposed to a MySuper offering is a matter which is readily rectified by reversing the transaction with effect from the date of the contribution allocation. Earnings can be adjusted. Fees can be reimbursed. The member can be reinstated into the position in which they would have been had the error not occurred.

Accordingly, we submit that proposed new section 29WA of the Bill not be a strict liability provision.

2) 29E(6A)(b) – ensure governing rules not contravened

Proposed new paragraph 29E(6A)(b) states that: -

> *"(b) the RSE licensee must ensure that the governing rules of the fund relating to that class of interest are not contravened".*

While trustees endeavour to ensure that the governing rules are not contravened it is a fact of life that inadvertent errors and immaterial breaches do occur. It should be borne in mind that there is increasing concern and unease among trustees and their insurers that their potential liability is being increased significantly.

We suggest that this be re-drafted to the effect of "*the RSE licensee must ensure that there are processes in place such that the governing rules of the fund relating to that class of interest are not contravened"*.

3) 29SB - Period for deciding applications for authority

Proposed new sub-section 29SB states: -

> *"(1) APRA must decide an application by an RSE licensee for authority to offer a class of beneficial interest in a regulated superannuation fund as a MySuper product:*
>
> *(a) within 60 days after receiving the application; or*
>
> *(b) if the applicant was requested to provide information under section 29SA - within 60 days after:*
>
> *(i) receiving from the RSE licensee all of the information the RSE licensee was requested to provide under that section; or*
>
> *(ii) all notices relating to that information being disposed of;*
>
> *unless APRA extends the period for deciding the application under subsection (2)".*

It is not clear why – instead of merely "stopping the clock" – a request to provide information under section 29SA should instead "re-start the clock", especially given that APRA has the discretion to extend the period under sub-section 29S(2) should circumstances warrant it.

4) 29TA - Offering in another fund in which there is already material goodwill

Proposed new section 29TA provides as follows: -

> "*This section is satisfied in relation to a class of beneficial interest in a regulated superannuation fund (the **proposed MySuper product**) if:*
>
> *(a) the benefits of members and beneficiaries in another regulated superannuation fund (the **original fund**) are to be transferred to the fund; and*
>
> *(b) APRA is satisfied that:*
>
> *(i) some or all of the persons whose benefits are to be transferred hold a class of interest in the original fund that is similar to the proposed MySuper product; and*
>
> *(ii) there is material goodwill in that class of interest in the original fund; and*
>
> *(iii) that goodwill could not be maintained unless the RSE licensee were authorised to offer the proposed MySuper product as an additional MySuper product in the fund; and*
>
> *(iv) it would be in the best interests of the members of the fund, and those persons whose benefits are to be transferred to the fund, to maintain the distinction between the proposed MySuper product and other MySuper products within the fund".*

a) Only available upon transfer after commencement

It is unclear why the benefits of members and beneficiaries must be in another regulated superannuation fund and cannot, for example, be in a sub-plan of the same superannuation fund. This exemption should not be confined to a successor fund transfers \ mergers.

Many master trusts and industry funds have sub-plans, either for different participating employers that has brought its corporate fund into the master trust or on some other basis, such as offering different products. These sub-plans have differing benefit designs, often reflecting the previous corporate superannuation fund which may have been transferred into the master trust.

Accordingly, we submit that these divisions should be able to have a MySuper class separate from the MySuper class in other divisions of the master trust without there having to be a transfer after commencement of the legislation.

b) "Material Goodwill"

Similarly it is unclear as to what is meant by "material goodwill". We take it that the material goodwill is in the intellectual property rights in a particular brand and the inherent commercial value to the trustee as a consequence of the awareness of that brand?

c) Determination by APRA

It is of concern that – as well as the trustee determining whether or not paragraphs 29TA(b)(i) to 29TA(b)(iv) are satisfied, APRA must also be satisfied that these paragraphs are met.

In ASFA's view APRA - a prudential regulator - should not be making assessments as to similarity of interests; existence and maintenance of material goodwill; and best interests of members. These are matters which are more appropriate for the trustee alone to determine.

5) 29TB - MySuper offerings for large employers

a) Definition of large employer

Proposed new paragraph 29TB(1)(a) necessitates that the employer must be a "large employer" in relation to the fund. "Large employer" in relation to the fund is defined in proposed new sub-section 29TB(2) as being: -

> *"(2) An employer is a large employer in relation to a regulated superannuation fund if there are 500 or more members of the fund who are any of the following:*
>
> *(a) a member of the fund:*
>
> *(i) who is an employee of the employer; and*
>
> *(ii) in relation to whom the employer or an associate of the employer contributes to the fund or would, apart from a temporary cessation of contributions, contribute to the fund;*
>
> *(b) a member of the fund:*
>
> *(i) who is an employee of an associate of the employer; and*
>
> *(ii) in relation to whom either the employer or an associate of the employer contributes to the fund or would, apart from a temporary cessation of contributions, contribute to the fund".*

We query the use of an arbitrary threshold number measure as opposed to a criterion such as the employer's willingness to pay any additional costs which may arise from the "tailoring" of the offering. The use of a threshold number always creates issues with respect to the need for transitional provisions should the number fall below the threshold.

Further, we query why the measure of 500 is only applied against employees for whom contributions are being made and not all members of the Large Employer offering?

We suggest that the measure be simply that there be 500 members, including employees, former employees and relatives and dependants of the employer and its associates.

b) Requirement that "any" employee can be a member

Proposed new paragraph 29TB(1)(d) states that: -

> *"(d) under the governing rules of the fund:*
>
> *(i) where the large employer or an associate of the large employer contributes to the fund or would, apart from a temporary cessation of contributions, contribute to the fund for an employee of the large employer,* ***any*** *employee of the large employer may hold an interest of that class in the fund; and*
>
> *(ii) where the large employer or an associate of the large employer contributes to the fund or would, apart from a temporary cessation of contributions, contribute to the fund for an employee of an associate of the large employer,* ***any*** *employee of that associate may hold an interest of that class in the fund"* (emphasis added).

There is no particular reason why there should be a requirement that "any" employee "may" be a member. This is a matter which should be left to the discretion of the employer and the trustee.

Furthermore, there are instances where industrial instruments restrict the ability of an employer to nominate an employer chosen fund in respect of a class of employees. ASFA considers that in this circumstance, which may not be uncommon for large employers, should not prevent the employer from establishing a MySuper offering for any employees not otherwise covered by the industrial agreement.

c) Separate application for each Large Employer MySuper offering

Furthermore it appears as though the trustee must make a separate application with respect to each large employer MySuper offering. ASFA suggests that this be amended such that a trustee need only make a single full application to offer one or more large employer offerings and simply advise APRA of the details of each offering.

The only criteria under sub-section 29TB(1) are "objective" and narrow, namely whether: -

- the only persons who may \ do hold the large employer MySuper offering are employees, former employees and their dependants and relatives;
- any employees may hold the large employer MySuper offering (assuming this is not amended); and
- the employer meets the definition of a large employer.

All of these criteria can be determined objectively, demonstrated clearly and assessed by APRA on review. As such, an application with respect to each large employer offering would not appear to be warranted.

In particular, it is unclear as to how the trustees who are responding to a "request for tender" with respect to an existing corporate fund or sub-plan, or a future "large employer MySuper offering", will need to proceed in future.

Prospective trustees should not be required to: -

- go to the effort and expense of amending their governing rules and making a "hypothetical" application to APRA on the off-chance that their response to tender is successful; or
- wait until the result of the tender response process is communicated to them, before commencing on amending the governing rules and making an application to APRA, which will delay the transfer of the fund \ sub-plan by weeks, if not months.

6) 29TC(1)(b) - characteristics of a MySuper offering – same options, benefits and facilities

Proposed new paragraph 29TC(1)(b) states that within a MySuper offering

> *"(b) all members who hold a beneficial interest of that class in the fund are entitled to access the same options, benefits and facilities".*

There may be some – limited – instances of options, benefits or facilities which it may be reasonable to make available only to a sub-set of members, such as educational seminars which are targeted at a particular age group (generally pre-retirees aged 55 or more) or employees at a particular workplace. Education seminars are one of the most effective means of educating members and driving behaviour but it appears as though, without an exception, funds may no longer be able to offer such seminars.

In particular, seminars which are cost-effective delivered to large groups of employees at a single workplace simply cannot be justified, on cost grounds, for delivery to smaller numbers in remote locations.

One possibility may be to allow such seminars provided, for example, the same educational content is available to all members online.

Furthermore, we submit that it may be necessary to clarify that the reference to "benefits" is not taken to include a reference to insurance benefits.

Of particular concern is existing insurance arrangements where levels of cover and premium charges vary according to employer group, risk categories, industrial award or statutory requirement. The legislation should allow this to continue.

7) 29TC(1)(d) - characteristics of a MySuper offering – fee subsidisation

Proposed new paragraph 29TC(1)(d) states: -

> *"(d) the same process is to be adopted in attributing amounts to members in relation to their beneficial interest of that class in the fund, except to the extent that a different process is necessary to allow for* ***fee subsidisation by employers****"* (emphasis added)

It is important to note in this context that lower fees may be charge to some members not as a result of fee subsidisation but because – due to efficiencies and economies of scale – the trustee and employer have agreed that a lower administration fee is appropriate. This does not amount to a fee subsidisation.

8) 29TC(1)(e) - characteristics of a MySuper offering – fee subsidisation by employers

Proposed new paragraph 29TC(1)(e) states that: -

> *"(e) if fee subsidisation by employers is permitted, that subsidisation does not favour one member who holds a beneficial interest of that class in the fund and is an employee of a subsidising employer over another such member who is an employee of that employer".*

We query why there cannot be fee differentials between different groups of employees? If this has, for example, been determined as part of the employer's industrial relations arrangements, why should MySuper override this?

Currently, there are circumstances where different employees receive different levels of fee subsidy from their employers. ASFA is concerned that the provision, as currently worded, does not cover such circumstances.

This may have come about as a result of grandfathering arrangements (e.g. all employees who were employees of a previous employer \ members of a former fund are provided with a certain level of subsidy whilst new employees receive less, or no, subsidy) or may be dependent upon the category of the employee. Such arrangements may also be included within workplace agreements or individual contracts or may have been a feature of the sub-plan \ category of the fund when the member joined.

Accordingly, it may be appropriate to allow the grandfathering of fee subsidy arrangements which were in place as at the commencement of MySuper.

We suggest that the legislation also confirm that employers are able to subsidise the insurance premiums payable and that this would not be considered to fall under this provision.

9) 29TC(1)(f) - no limitations on source or kind of contributions

Proposed new paragraph 29TC(1)(f) states: -

> *"(f) the only limitations imposed on the source or kind of contributions made by or on behalf of persons who hold a beneficial interest of that class in the fund are those permitted under subsection (3)".*

a) Source of contributions

When prescribing limitations we would ask that it is borne in mind that some funds do not, for example, accept contributions from an: -

- overseas fund (e.g. fund is not a QROPS for the purposes of the UK legislation); or
- employer who is not a standard employer sponsor, or associated with the standard employer sponsor.

Ideally any regulations which may be made for these purposes should enable this to continue.

b) Kind of contributions

The legislation appears to contemplate "kinds of contributions" as meaning a contribution type such as concessional, non concessional, spouse, etc. When prescribing limitations we would ask that trustees should be able to refuse "in-specie" contributions, such as shares and property. Ideally any regulations which may be made for these purposes should allow for this to occur.

Furthermore, funds should also have the capacity to direct "how" contributions are made, at least until such time as payment of contributions electronically is mandated.

10) Proposed new sub-section 29TC(2) – lifecycle investment exception

Proposed new sub-section 29TC(2) states: -

> *"A **lifecycle exception** is a rule under the governing rules of the fund that allows gains and losses from different classes of asset of the fund to be streamed to different subclasses of the members of the fund who hold a MySuper product:*
>
> *(a) on the basis, and only on the basis, of the age of those members; or*
>
> *(b) on the basis of the age of those members and other prescribed factors; or*
>
> *(c) on the basis of the age of those members and other prescribed factors in prescribed circumstances".*

It is important to note that a lifecycle option does not "*allow … gains and losses from different classes of asset … to be streamed to different subclasses … on the basis of … the[ir] age or ... the[ir] age … and other prescribed factors or … the[ir] age … and other prescribed factors in prescribed circumstances".*

What a lifecycle exception does allow – on the basis of one or more criteria, such as the age cohort of members - is for the account balance\contributions of those members to be invested in different assets to members of other lifecycle cohorts. Trust law then determines that the income\growth from those assets is attributed - on the basis, and only on the basis – of the extent to which those members' accounts are invested in those assets.

In other words – a lifecycle exception allows in account balances of different cohorts to be invested in different assets. Distribution of gains and losses automatically flows from the beneficial ownership of those assets.

Importantly, once these cohorts are defined, all members within the same cohort of similar characteristics will be invested in the same assets and will receive investment returns on that basis – asset ownership.

It should be noted that, due to the fact that the assets underlying the various lifecycle investment options will vary, the investment costs and investment returns, whilst the same for a particular cohort, will differ between cohorts.

As stated above, if trustees are completed to charge the same investment fee to all cohorts of members this will result in members who are in a more conservatively invested asset portfolio (generally older members) cross-subsidising those whose asset portfolio is invested more aggressively (generally younger member). Given that one of the overarching principles of MySuper is that investment fees should be borne by members on a "cost recovery" basis it would appear anomalous that this should occur.

Accordingly, we submit that a trustee should be able to recover a different quantum of investment fees with respect to each asset portfolio. Importantly, once these cohorts are defined, all members within the same cohort of age and other similar characteristics, who are invested in the same asset portfolio, will have the same investment fee.

11) Division 4—Cancelling authority

Proposed new sub-section 29U(1) permits APRA to cancel an authority to offer a MySuper offering.

With the limited exception of proposed new section 29UB there is no provision in the Bill for what is to occur in the event a licence is cancelled.

At a minimum, the Bill should prescribe what is to occur with contributions received after the notice of cancellation has been received and the period of time in which the trustee must transfer the members' benefits to another MySuper offering.

Furthermore, the nature and design of the Superannuation Guarantee ("SG") system is such that employers must make "default" contributions to a MySuper offering by the 28th day of the month following each quarter and face significant financial penalties if they fail to do so. Given this, it is essential that a fund whose MySuper authorisation is cancelled be under an obligation to advise this to contributing employers, along the lines of sub-section 63(9) of SIS, within a reasonable timeframe.

We note that proposed new paragraph 29U(2)(b) states APRA may cancel an authority if: -

> *"(b) the RSE licensee was authorised to offer that class of beneficial interest in the fund as a MySuper product because section 29TB was satisfied in relation to the class and either:*
>
> > *(i) in a case where that section was satisfied because APRA was satisfied that an employer would be a large employer by the end of a period specified in the authority - the employer was not a large employer at that time; or*
> >
> > *(ii) in any case—that section was no longer satisfied in relation to the class on the last day of the immediately preceding year of income".*

This means, potentially, that APRA could cancel an authority on 1 July with respect to a 29TB MySuper offering where the number of employees who were MySuper members was reduced to 499 only the previous day.

It is unacceptable that an authority be cancelled with immediate effect. Instead the trustees should be permitted a transition period to enable the orderly transfer of members to an alternative MySuper offering.

As such, the Bill should provide that any withdrawal of an authority will be managed carefully by the regulator to as to produce an orderly transitioning of members to another MySuper offering.

12) Proposed new sub-section 29V(3) – definition of investment fee

We submit that "investment fee" should be defined in accordance with the Global Investment Performance Standards. If this definition is not adopted we would suggest consideration be given to the definition utilised by members of the Financial Services Council.

Should neither of the above definitions not be adopted we make the following suggestions with respect to the proposed definition: -

- as the proposed first limb of the definition in sub-section 29V(3)(a) - *"fees in payment for the exercise of care and expertise in the investment of those assets (including performance fees)"* - simply represents one of the many direct, and indirect, costs of investing, we suggest this limb be deleted. An "investment fee" chargeable to a member should reflect all of the investment costs, irrespective of whether they are fees payable to a third party or other direct or indirect costs incurred by the trustee; and
- the definition instead should read: -

  "An **investment fee** is a fee that relates to the investment of the assets of the ~~fund~~ [*investment option or offering*] and includes any *investment* costs incurred by the trustee, or the trustees, ~~of the fund~~ (that are not otherwise *recovered by means of* ~~charged as~~ an administration fee, a buy-sell spread, a switching fee, an exit fee or an activity fee)".

If it were considered necessary, for the avoidance of doubt, reference could be made to performance-based fees by inserting the words "including performance based fees" after the words "investment costs".

Furthermore, as per above, provision should be made to recognise that there may be different "investment fees" for different cohorts within a lifecycle investment option.

13) Proposed new sub-section 29V(1) – switching fee

Proposed new sub-section 29V(5) defines a *switching fee* as being: -

> "*a fee to recover the costs of switching all or part of a member's interest within the fund:*
> *(a) from a MySuper product in the fund to a MySuper product in the fund; or*
> *(b) from a MySuper product in the fund to a choice product in the fund; or*
> *(c) from a choice product in the fund to a MySuper product in the fund; or*
> *(d) from a choice product in the fund to a choice product in the fund".*

We suggest that the definition of "switching fee" in paragraph 29V5(a) be confined to circumstances where the transfer is initiated by the member.

14) Proposed new section 29VA – charging rules

Proposed new sub-section 29VA(2) states as follows: -

> *"(2) This rule is satisfied if:*
> *(a) the fee is charged in relation to all members of the fund who hold the MySuper product; and*
> *(b) the amount of the fee is the same for each of those members".*

Proposed new sub-sections 29VA(3) and 29VA(4) contain similar wording.

Lifecycle strategy investment costs will vary significantly depending on the stage of the lifecycle, the allocation of assets and the extent to which assets are actively managed or are passive.

In order to give effect to the policy of minimising the extent to which cross subsidisation occurs, the Bill should be amended to allow the trustee to charge different investment fees to members in a lifecycle investment option depending on their cohort.

15) Proposed new sub-section 29VA(3) – all members charged same percentage of balance

Proposed new sub-section 29VA(3) states: -

> *"(3) This rule is satisfied if:*
>
> *(a) the fee is charged in relation to all members of the fund who hold the MySuper product; and*
>
> *(b) the amount of the fee charged in relation to one member is a percentage of so much of the member's account balance with the fund that relates to the MySuper product; and*
>
> *(c) the amount of the fee charged in relation to each other member of the fund who holds the MySuper product is the same percentage of so much of that member's account balance with the fund that relates to the MySuper product".*

It is quite common for funds to charge a percentage of assets on the first tier of an account balance, say $200,000, and then a lower fee with respect to the next tier, and so forth. Similarly, percentage based fees can be subject to a maximum or "cap". Often a tiered scale is combined with a cap.

It would appear that this is not possible under sub-section 29VA(3) as currently drafted.

If the practice of tiered and capped asset fees is not allowed to continue this could potentially result in an increase in fees payable by members – surely an adverse outcome.

The "Review into the Governance, Efficiency, Structure and Operation of the Superannuation System" clearly contemplated the use of fee schedules, not just one fee.

Abolishing tiered scales and fee capping potentially could lead in some funds to an exodus of high account balance individuals from MySuper offerings either into choice offerings or even into SMSFs.

We submit that, to accommodate the diversity of existing fee arrangements, the sections with respect to percentage-based fees should be redrafted in terms of there being one percentage fee **scale** used to determine the applicable fee.

16) Sub-paragraph 29VB(1)(b) – administration fees for employees of employer - sponsor

Sub-paragraph 29VB(1)(b) states as follows: -

> "*(1) An administration fee charged to members of a regulated superannuation fund who hold a MySuper product is charged in accordance with the* ***administration fee exemption for employees of an employer-sponsor*** *if:*
> …
> *(b) an employer-sponsor contributes to the fund or would, apart from a temporary cessation of contributions, contribute to the fund for the benefit of one or more members of the fund (the* ***employee members****) who hold the MySuper product and who are:*
> *(i) employees of the employer-sponsor, or an associate of the employer-sponsor; or*
> *(ii) the relatives or dependants of those employees".*

This does not allow for the circumstances where it is an associate of an employer-sponsor who contributes to the fund, as well as the employer. The Bill should be amended to recognise this.

17) Sub-section 29VB(2), 29VB(3) and 29VB(4)– all employees charged same fee

Proposed new sub-section 29VB(2) states: -

> *"(2) The amount of the administration fee is the same for each of the employee members*".

Sub-sections 29VB(3) and 29VB(4) use similar wording.

We query why the administration fee needs to be the same for all employee members. In circumstances where it is the employer who is subsiding all or part of the fee, why should they be subject to restrictions as to for whom such subsidy can be paid?

Furthermore, we submit that this should be amended to allow for former employee members and relative and dependant members to be charged the same fee, but that this should not be mandatory. In other words, trustees and employers should be free to decide whether they will offer this fee to former employees and relatives and dependant members.

18) Proposed new sub-sections 29WA(3) – strict liability – allocation of contributions

Proposed new sub-section 29WA(3) – with respect to contributions in relation to which no election has been made being paid into a MySuper offering - creates an offence of strict liability.

Even in the best regulated environment inadvertent administrative and clerical errors and omissions do occur, both on the part of the employers and with respect to fund operations. As such, ASFA is concerned with a breach of section 29WA being a strict liability offence.

It is important to note that, even if an error were to occur, an inadvertent misdirection of a contribution into a choice offering as opposed to a MySuper offering is a matter which is readily rectified by reversing the transaction with effect from the date of the contribution allocation. Earnings can be adjusted. Fees can be reimbursed. The member can be reinstated into the position in which they would have been had the error not occurred.

Accordingly, we submit that proposed new section 29WA of the Bill not be a strict liability provision.

19) Part 2—Application and transitional provisions

Item 12 - Applications for authority to offer a MySuper offering for a large employer

Please refer to our comments with respect to proposed new section 29TB. It is unclear as to why an application should need to be made to APRA with respect to large employer offerings at all, given that whether or not the relatively narrow criteria under sub-section 29TB(1) are met can be determined objectively by the trustee and simply assessed by APRA on review.

Even if an application has to be made to APRA, it is unclear as to why, under items 12(2)(a) and 12(2)(b), an application with respect to a section 29TB MySuper offering: -

- will be deemed not to have been received until 1 July 2013, irrespective of when it is actually received; and
- in particular – APRA will have 120 days, in lieu of 60 days, to process the application.

B) DRAFTING ISSUES

1) Proposed new sub-section 29S(5)

Proposed new sub-section 29S(5) states as follows: -

> *"(5) If:*
>
> *(a) an RSE licensee applies for authority to offer a class of beneficial interest in a regulated superannuation fund as a MySuper product; and*
>
> *(b) after the application is made, but before APRA decides the application, information contained in the application ceases to be correct;*
>
> *the RSE licensee must give APRA the correct information, in writing, as soon as practicable after the information in the application ceases to be correct".*

For the avoidance of doubt, we would suggest inserting the words "becoming aware that" after the word "after" and substituting the words "has ceased" for "ceases" in the last line.

2) Proposed new paragraph 29TC(1)(b) - characteristics of a MySuper offering

Proposed new paragraph 29TC(1)(b) effectively states that within a MySuper offering

> *"(b) all members who hold a beneficial interest of that class in the fund are entitled to access the same options, benefits and facilities".*

We submit that this should be qualified with an expression to the effect "to the extent permitted by superannuation law" (suitably defined) or "to the extent permitted under this Act" or "to the extent permitted under the general law or a law of the Commonwealth or of a State or Territory".

3) Proposed new paragraph 29TC(1)(c)

Proposed new paragraph 29TC(1)(c) states that within a MySuper offering

> *"(c) amounts are attributed to members in relation to their beneficial interest of that class in the fund in a way that does not stream gains or losses that relate to any assets of the fund to only some of those members, except to the extent permitted under a lifecycle exception".*

An alternate way of drafting this - which reflects both the legal and commercial reality - would be along the lines that "returns are credited to a member in proportion to the account balance held by that member".

If it is felt that trust law offers insufficient protection to ensure that the above occurs (although arguably it would be a breach of trust to do otherwise), then this could specify that the returns credited to MySuper members must be attributable to MySuper assets.

4) Proposed new paragraph 29TC(e)

Proposed new paragraph 29TC(e) states that: -

> *"(c) if fee subsidisation by employers is permitted, that subsidisation does not favour one member who holds a beneficial interest of that class in the fund and is an employee of a subsidising employer over another such member who is an employee of that employer".*

Notwithstanding our objection to this provision being confined to circumstances where subsidisation occurs (please refer to item 8 in above section), we submit that the word "associate"

should be inserted after the word “employer” where it appears in the final line and the words “or associate” should be inserted at the end of the sentence.

5) Proposed new paragraphs 29U(2)(c) and 29U(2)(d)

Proposed new paragraphs 29U(2)(c) and 29U(2)(d) state that APRA may cancel an authority if: -

> *“(c) APRA is no longer satisfied that:*
> *(i) where the RSE licensee is a body corporate - the RSE licensee; or*
> *(ii) where the RSE licensee is made up of a group of individual trustees - each of those individual trustees;*
> *is likely to comply with the enhanced trustee obligations for MySuper products (whether because of a previous failure to do so, or for any other reason); or*
> *(d) APRA is no longer satisfied that:*
> *(i) where the RSE licensee is a body corporate - the RSE licensee; or*
> *(ii) where the RSE licensee is made up of a group of individual trustees - each of those individual trustees;*
> *is likely to comply with the fees rules in relation to MySuper products (whether because of a previous failure to do so, or for any other reason)”.*

As individual trustees nevertheless act collectively it is unclear as to why reference is made to “each of” those individual trustees. If there is a concern about individual trustees, consideration could be given to mandating that only corporate trustees can offer a MySuper offering.

Further, we submit it would be preferable to combine these paragraphs by inserting the words “and fee rules” after the words “obligations” in paragraph 29U(2)(c) and deleting paragraph 29U(2)(d).

6) Proposed new paragraph 29U(2)(i)

Proposed new paragraph 29U(2)(i) states that APRA may cancel an authority if: -

> *“(i) APRA is satisfied that:*
> *(i) where the RSE licensee is a body corporate - the RSE licensee; or*
> *(ii) where the RSE licensee is made up of a group of individual trustees - one of those individual trustees;*
> *has contravened a provision of the governing rules of the fund relating to the MySuper product”.*

Similarly to paragraphs 29U(2)(c) and 29U(2)(d), as individual trustee act collectively, it is difficult to envisage when one individual trustee may have contravened a provision of the governing rules relating to the MySuper offering.

7) Proposed new sub-sections 29VA(2), 29VA(3) and 29VA(4)

Proposed new sub-section 29VA(2) states: -

> *“**All MySuper members charged same flat fee***
> *(2) This rule is satisfied if:*
> *(a) the fee is charged in relation to all members of the fund who hold the MySuper product; and*
> *(b) the amount of the fee is the same for each of those members”.*

Proposed new sub-sections 29VA(3) and 29VA(4) utilise similar wording.

Use of the phrase “charged in relation to” may prove problematic in circumstances where not all fees are actually charged to all members, such as the “buy–sell spread”, “switching fee” and “exit fee” which are only incurred if a member requests a transfer or a roll-over out. Accordingly it may be preferable to substitute words to the effect of “payable by” for “charged in relation to”.

8) Proposed new sub-section 29VA(3)

Proposed new sub-section 29VA(3) states: -

> ***“All MySuper members charged same percentage of account balance***
> *(3) This rule is satisfied if:*
> *(a) the fee is charged in relation to all members of the fund who hold the MySuper product; and*
> *(b) the amount of the fee charged in relation to one member is a percentage of so much of the member’s account balance with the fund that relates to the MySuper product; and*
> *(c) the amount of the fee charged in relation to each other member of the fund who holds the MySuper product is the same percentage of so much of that member’s account balance with the fund that relates to the MySuper product”.*

We would suggest: -

- substituting the words “is a fixed percentage of the member’s account balances” for “in relation to one member is a percentage of so much of the member’s account balance”;
- substituting the word “relate” for “relates”; and
- deleting paragraph (c).

We would suggest a similar approach be adopted for proposed new sub-sections 29VA(4); 29VA(6) and 29VA(7).

9) Comments of the use of the word “product” in the Bill

There is still clarity needed as to whether MySuper must be offered as a separate product or can be satisfied by utilising an investment option (generally the existing balanced, default, investment option). In ASFA’s view, as stated many times, MySuper can be an investment option, product or fund.

Notwithstanding the fact that the definition of “MySuper product” in the Bill is deliberately broad, use of the terms “MySuper product” and “choice product”, as well as the occasional reference in the Bill and EM to just the word “product”, have created an impression that MySuper must be offered as a separate product.

The most significant issue with this is that, if providers have to offer MySuper as a product, then they will need to establish separate accounts. As you will understand, there are many different structures within funds and it is important that MySuper is structurally neutral as much as possible.

Accordingly, we suggest that consideration be given to “globally replacing” the word “product” throughout the Bill with the word “offering”. The word "offering" is sufficiently flexible to cover the possible different structures under which MySuper may be offered, without creating the impression that it must be offered as a separate product.