

Default Superannuation Funds in Modern Awards

Productivity Commission

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Default Superannuation Funds Submission

introduction

eo Financial Services Pty Ltd (eo) is part of the eo Group and provides a range of services to the superannuation industry across our six specialised teams. These services include strategy, secretariat and governance, investments, member and employer services, and marketing. The major client of eo is an industry superannuation fund servicing over 450,000 members.

eo welcomes the opportunity to provide its views on some of the significant issues set out in the Productivity Commission's February 2012 Issues Paper on Default Superannuation Funds in Modern Awards (**Paper**).

background

The Cooper Review Report relevantly recommended that –

- legislation be amended so that only MySuper products are eligible to be nominated and that all MySuper products are able to be nominated for 'default fund' purposes in awards approved by Fair Work Australia (Cooper recommendation 1.3); and
- the Productivity Commission conduct a review of the processes by which default funds are nominated in awards to assess whether the processes are sufficiently open and competitive (Cooper recommendation 1.4).

These recommendations were consequent to Cooper Review recommendation 1.2 that the *Superannuation Guarantee (Administration) Act 1992* be amended so that only a MySuper product is eligible to be a default fund nominated by an employer.

The Cooper Review Report recommendations mentioned above were all supported by the Government in its 16 December 2010 Stronger Super response.

Further, on page 2 of the Paper, the Commission states that its approach to fulfilling its terms of reference will be to –

- *consider whether to allow all MySuper products to be eligible for nomination in modern awards or whether there is a net benefit to designing criteria over and above those for MySuper. If additional criteria are required, consideration would need to be given to how those criteria would be implemented.*

submissions on issues in the paper

eo makes submissions on a number of the issues in the Paper and in each case sets out the question posed in the Paper in italics and our submission in regular font immediately following.

Are the criteria required of MySuper products sufficient for the selection and ongoing assessment of superannuation funds eligible for nomination as default funds in modern awards? If so, why?

As members of a default fund are usually individuals who do not make a choice of fund under the SG Act, those members are generally regarded as not as engaged with their superannuation as those who do make a choice of fund. Consequently, the Cooper Review recommended that default fund members and their SG Act contributions be protected in a special way from high costs and unnecessary services. This protection was to be in the form of MySuper.

While the MySuper criteria set out in the 2 draft bills before Parliament (ie, at this writing, the *Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2011* and the *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012* go far in addressing some of the default fund issues identified in the Cooper Review, we do not believe that those criteria go far enough for default funds named in modern awards. Generally, this is because there will be MySuper products which (immediately and certainly over time) will be superior to other MySuper products.

We see MySuper requirements as creating a basic standard but suggest that being named in an award should carry further responsibilities. We discuss this further in the following item.

Is there a case for introducing a set of criteria over and above those required for MySuper products for funds to be eligible for nomination as a default fund in modern awards?

We believe that there is a case for additional criteria (beyond that for MySuper) for a fund's nomination as an award default fund. This is because:

- default funds should be selected on the basis of advancement of members' interests and MySuper products may not all achieve this aim – or at least not to the same extent;
- the criteria for selection of a default fund in a modern award should reflect this aim. This could be accomplished in 2 ways:
 1. making sure that the MySuper products named are comparatively better performers (as to costs and investment returns) than other MySuper products; or
 2. adding further criteria for MySuper products to meet before they can be named in the modern award.

The criteria should be objective and capable of measurement. There should be a rigorous process for assessing default funds against this criteria and funds that are seeking to be included in the award should make application addressing each of the criteria.

We suggest that there should be a new mechanism for assessing the applications and a uniform approach to that assessment. Perhaps an expert panel could be assembled for this purpose, composed of people with a range of skills, including superannuation industry experience, investment knowledge and industrial relations experience. The panel would assess the applicants against the criteria and make recommendations to Fair Work Australia as to whether any, some or all of the applicants are appropriate for inclusion in the particular modern award.

After being accepted as a default fund in an award, there should be a regular monitoring of that fund's performance by the expert panel (perhaps on a 3 year basis) so as to ensure that the criteria on which they were selected continue to be met. If the selection criteria are no longer met, Fair Work Australia would remove the fund from the award. This monitoring would be in members' interests because the fund's goal should not be just to be included as a default fund but to operate in an efficient and professional way so that the fund remains in the award.

Should a fund's investment management expertise be factored into the selection of default superannuation funds for inclusion in awards and, if so, how?

Yes. Investment performance should be a significant factor as the function of a default fund should be to maximise retirement outcomes for its members, while trying to contain unnecessary costs and fees.

The criteria should require information about the fund's mechanisms for protecting members' capital amounts, the investment strategy, risk measures and fees as well as the Funds 5 year performance.

Are transparency and contestability desirable features of a default superannuation fund selection process? Is the current process for listing default funds in awards transparent? Is it competitive? Is there a level playing field between industry and retail funds?

In our view, the current process is not competitive or transparent. In our experience, the absence of objective selection criteria is common and in many instances no questioning of the fund's credentials occurs.

The lack of accountability means that funds cannot be sure why they were excluded when other funds were included – especially when funds that are included might not have better investment performance or lower costs than those that were excluded.

Lack of transparency and objective criteria also means that an appearance of both conflicts of interest and conflicts of duty can often arise as there seems to be no basis other than 'who you know' for being successful in the selection process. As mentioned previously, we suggest that a new mechanism should be put in place so that an independent assessment of the applicants takes place and objective recommendations are then made to Fair Work Australia.

Given the statistics in the Paper (page 5), there can be no doubt that the current nomination process is skewed in favour of industry funds at the expense of all other types of funds, with 71% of funds listed in awards being industry funds (both public and no-public offer) and with only 14% being retail funds and 5% being corporate funds. This discrepancy is too great to be explained in any way except that the operation of the relevant principles formulated by the Australian Industrial Relations Commission¹ (and which continue to be applied by Fair Work Australia) together with the restrictions in the *Fair Work Act 2009* about when, on what basis and who may make application to vary a modern award² works overwhelmingly in favour of industry funds.

At present, nominated default funds or funds seeking nomination as a default fund are not required to address or to reveal actual or potential conflicts of interest or duty (or both) and where applicable, nor are applicants to vary an award to nominate a fund as a default fund required to reveal their connection to or interest in the fund. Given the heightened governance standards which will apply to MySuper trustees and the policy role that superannuation plays in Australia's economy, this practice can no longer be accepted nor countenanced. We believe that the existence and management of conflicts of all kinds should be a specific item to be addressed in relation to each default fund or a fund seeking to be a default fund.

Should there be a target number of funds in each award?

We do not consider that there should be a target number of funds for each award but, instead, believe that all MySuper products should be able to apply to be included in the award and those which meet the selection criteria should be listed in the award. The listing of multiple funds that meet the criteria allows for competition and enables the employer to select a fund named in the relevant modern award which best suits the needs of its workforce and reflects its values. This will also require consequential change to legislation to permit funds themselves to apply to become a default fund where this may not be currently permitted.

conclusion

We are of the view that:

- not all MySuper products should be eligible to be named in a modern award;
- there would be a benefit to fund members if criteria were required for funds to be named in a modern award over and above the MySuper criteria; and
- any and all decisions associated with default superannuation selection should be made with the best interests of the member in mind.

We would welcome the opportunity to speak at any hearings that the Commission might hold on these issues and to make further comments on the draft report after it is released for industry consultation.

Yours faithfully

Megah Bolton

Chief Executive Officer

¹ See [2008] AIRCFB 717 (12 September 2008), [2008] AIRCFB 1000 (19 December 2008) and [2009] AIRCFB 800 (2 September 2009)

² See Division 5 of Part 2 -3, sections 157 to 161