



Australian Government

The Treasury



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Department of Education, Employment and Workplace Relations

Productivity Commission Draft Report

Default Superannuation Funds in Modern Awards

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THIS SUBMISSION

This joint Treasury and Department of Education, Employment and Workplace Relations (DEEWR) submission does not seek to comment on all issues and recommendations raised in the Commission's Draft Report. Rather, the submission focuses on several key issues arising from the Commission's draft recommendations and seeks to provide information that may assist in the finalisation of the Inquiry.

1. OVERVIEW

1.1.1 The review of the arrangements for determining which funds are listed in modern awards provides an important opportunity to promote outcomes in the best interests of award covered employees and employers, with the overall aim of lifting the retirement incomes of Australian workers. We welcome consideration of options to improve the process for selecting and assessing default funds and agree there is scope for improvement.

1.1.2 In its Draft Report, the Commission notes that the current arrangements for listing default funds in modern awards have delivered stability and above-average investment returns compared to all funds. The conclusion to be drawn from that finding is that, by and large, employees have not been disadvantaged by the current arrangements.

1.1.3 The Commission also notes there is currently no requirement for the list of funds in modern awards to be regularly assessed, and that employees and employers would benefit from arrangements that ensure that decisions about which funds are listed as default funds in modern awards are based on a range of objective criteria.

1.1.4 We consider it important that any changes recommended by the Commission ensure the best performing funds are available to members under default arrangements in modern awards. Allowing for the views of employees, employers and their representatives to be considered in selecting default funds will not detract from this aim. Higher-performing funds currently listed in modern awards should not be excluded simply because of views about the processes by which they have historically been selected.

2. OPTIONS FOR REFORM

2.1 Agency Responsible for Selection and Ongoing Assessment of Default Funds

2.1.1 Draft principal finding 8.1 outlines four options identified and assessed by the Commission for reforming the process for the selection and ongoing assessment of superannuation funds for listing as default funds in modern awards. The Commission is seeking feedback from participants on the relative merits of two of these options – option 3 (process undertaken by an expert panel within Fair Work Australia (FWA)) and option 4 (process undertaken by an expert body independent of FWA).

2.1.2 Option 3 is our preferred approach for the selection and ongoing assessment of default superannuation funds listed in modern awards. FWA is an independent body with power to carry out a range of functions, including those related to the safety net of minimum wages and employment conditions and the making, variation and termination of modern awards. Superannuation is part of an employee's total remuneration and as modern awards form part of the safety net, and superannuation is an award matter, we consider it would be highly undesirable to split responsibility for modern award matters between FWA and another body.

2.1.3 FWA is experienced in considering competing submissions on industrial matters and working constructively with stakeholders in undertaking the many functions for which it is responsible under the *Fair Work Act 2009* (FW Act). This extensive expertise, combined with the administrative simplicity provided by retaining responsibility for modern awards within the one body, means FWA is the most appropriate body to undertake the selection and ongoing assessment of default superannuation funds in modern awards. For example, FWA's responsibilities and annual processes in relation to the setting of the national minimum wage and minimum wages in modern awards – through the Minimum Wage Panel comprising the FWA President, selected members of FWA and other part-time members – are particularly relevant. The process involved in FWA creating modern awards and the current two year review of modern awards is also relevant in demonstrating this expertise. Further, FWA has powers to vary modern awards to remove non compliant funds should there be a requirement to do so.

2.1.4 While FWA is the preferred body to have responsibility for the selection and ongoing assessment of superannuation funds for listing as default funds in modern awards, its role as decision maker in this regard should not be confused with that of the Australian Prudential Regulation Authority (APRA). Whatever process is adopted by the Commission, the respective roles of APRA and FWA must be kept separate and be clearly defined. APRA must retain responsibility for regulatory oversight of the superannuation industry and for authorising funds to offer MySuper products (a prerequisite for any fund seeking listing as a default fund). FWA's role would be to assess funds against relevant factors, and then make 'on-balance' judgements about which superannuation funds should be listed as default funds in modern awards. Careful consideration needs to be given to avoid duplicating APRA's role in granting powers and responsibilities to FWA.

2.1.5 It will be important that there is effective communication and exchange of information between the two bodies. APRA should have a role in providing information

and advice to FWA, as APRA's expertise will help inform the development of FWA's assessment methodology. APRA will have an ongoing role in monitoring the performance of all MySuper products, including those of funds listed as defaults in modern awards, and this information will assist FWA in assessing such funds at regular, defined intervals. Information on changes to the status of listed funds (for example, funds have merged, undergone name changes, had their MySuper authorisation cancelled, etc.) must also be provided by APRA to FWA.

2.1.6 Such a close working relationship would assist FWA exercise its powers in ensuring modern awards remain simple, stable and up to date, as well as giving employers and employees certainty about applicable default funds.

2.2 Process for the Selection and Ongoing Assessment of Default Funds

2.2.1 The Commission makes a number of draft recommendations relating to the process the decision making body should undertake for the selection and ongoing assessment of superannuation funds for listing as default funds in modern awards.

2.2.2 We support the Commission's draft recommendation 8.5 that a four/eight year program of interim/wholesale assessments should be undertaken and that this be timed to coincide with, or even form part of, FWA's four yearly reviews of modern awards as prescribed by the FW Act. We support this approach as it strikes an appropriate balance between the creation of a simple and stable award safety net for the benefit of employers and employees, with appropriate assessments of default funds in modern awards by FWA on a periodic basis. Lastly, it complements the existing frameworks and processes in the FW Act.

2.2.3 We support the Commission's proposed approach that an expert panel within FWA be established to perform this function. This would require amendments to the FW Act to include provisions establishing the expert panel and codifying the list of factors the expert panel must have regard to in undertaking its assessment and selection of default funds. We do not consider that the assessment methodology to be employed by FWA – that is, how funds would be assessed against this list of factors – should be codified. A robust and transparent assessment process should, in our view, be developed by FWA itself. The FW Act provides FWA with broad discretion in relation to how it conducts matters before it and how it may inform itself in relation to such matters. We would expect any provisions relating to an expert default superannuation fund panel would be consistent with this approach.

2.2.4 The Commission expresses concern about contestability and procedural fairness – that is, in its view not all superannuation funds have standing under current processes to apply to be listed as a default fund in a modern award. It makes draft recommendation 8.1 in response to this concern. We consider a more appropriate process is to allow all relevant funds seeking to be listed as defaults in modern awards to participate by presenting information relevant to the criteria for the assessment of default funds to the expert panel through expressions of interest as part of the eight year reviews. An expression of interest process is the most efficient way for these funds to provide relevant information to the expert panel, given the comprehensive nature of the selection

criteria proposed by the Commission. The expert panel would assess the expressions of interests to determine the most suitable funds for inclusion in relevant modern awards as defaults. The expert panel would conclude its assessment by providing a report to a FWA Full Bench listing those funds it had assessed as suitable for inclusion in modern awards as default funds, as well as setting out reasons why it may have assessed some funds as unsuitable for inclusion. Given its broader role in managing the overall review assessment and selection process, and its responsibility for conducting reviews of modern awards generally, the Full Bench would consider the panel's report, hear the views of the industrial parties and determine whether or not to vary the relevant awards, as appropriate. The expert panel's report would form the basis of the FWA Full Bench's considerations of the factors which will guide the assessment of the suitability of funds for inclusion in modern awards.

2.2.5. Such a process would address the Commission's concerns about contestability and procedural fairness by ensuring that all interested MySuper authorised superannuation funds had the opportunity to participate in a rigorous and transparent assessment process overseen by the expert panel. From a practical perspective, it would also ensure that the consideration of default superannuation fund issues by FWA as part of its modern award review process is as streamlined as possible given the potential for it to be both overwhelmed and made unworkable by large numbers of funds seeking to be listed as default funds. Importantly, the continued involvement of the industrial parties in the process will ensure that the interests of employees continues to be a key consideration for the FWA Full Bench in determining which funds to list as default funds in modern awards but that the interest of employers are also considered.

3. FACTORS TO BE CONSIDERED

3.1 Introduction

3.1.1 The Draft Report states that the selection and ongoing assessment of superannuation funds for listing as default funds in modern awards should have the best interests of members as the primary objective.

3.1.2 In its draft recommendations, the Commission identifies a number of factors it considers should, at a minimum, be taken into consideration in assessing individual funds for inclusion in specific awards. Assessment of funds against these factors would inform the decision making body's decisions regarding fund suitability. We broadly support the Commission's proposals in this area, but offer the following comments on several aspects of the Draft Report.

3.2 Fund versus product

3.2.1 We note that current award arrangements involve the listing of 'funds', whereas under the Stronger Super reforms MySuper will operate at the product level. We consider it appropriate to continue the established practice of listing funds as, under the proposed Stronger Super legislation, only funds offering a MySuper product will be eligible to be listed as a default fund in a modern award.

3.2.2 While it is expected that most funds will offer a publicly available 'generic' MySuper product, funds will also be able to offer additional MySuper products for large employers. However, large employer MySuper products will be limited to employees of particular employers and therefore are not the appropriate benchmark for assessment of a fund's suitability for inclusion in an award. As a result, assessment for listing in the awards must be undertaken in respect of a fund's 'generic' MySuper product.

3.3 Appropriateness of fees charged

3.3.1 The Commission identifies as a relevant factor the appropriateness of fees charged by the MySuper product, given its stated investment return objective and risk profile.

3.3.2 MySuper trustees will have a duty to promote the financial interests of MySuper members, in particular returns after the deduction of fees, costs and taxes. Net returns (that is, returns after the deduction of fees, costs and taxes) are one focus of the Stronger Super legislation. Net returns must be the core criteria used to assess fund performance.

3.3.3 The Stronger Super legislation also seeks to shift the superannuation industry's focus away from relative (or peer group) performance comparisons to clearer reporting of individual fund performance against that fund's investment objective. For example, if a fund promises to deliver CPI plus 4 per cent, it should be assessed against this objective. A shift away from peer group comparisons will provide members with a clearer picture of fund performance.

3.3.4 While net returns are a prime consideration in determining fund performance, we recognise that fees might be a relevant assessment factor. However, we note that the calculation of fees can be manipulated, for example, investment structures can allow fees and profits to be moved down a chain of entities, rather than being reflected in headline fees. Accordingly if fee comparisons are to be made they should, if possible, adjust for these variations.

3.4 Governance structures and conflicts of interest

3.4.1 The Commission believes that good governance arrangements are critical to protect the security of monies held and the interests of fund members. The Commission also proposes that, when assessing funds for listing, consideration should be given to the policies and procedures put in place by fund trustees to deal with conflicts of interest.

3.4.2 The Stronger Super reforms seek to significantly improve governance and conflict of interest arrangements through new trustee and director duties. APRA must be satisfied that a trustee and its directors are likely to comply with these obligations to obtain MySuper authorisation.

3.4.3 Where APRA is no longer satisfied that a fund trustee is likely to comply with the trustee obligations (including in respect of conflicts of interest), it will have grounds to cancel the trustee's authority to offer a MySuper product. A decision by APRA to cancel a trustee's authority would be merits reviewable. The cancellation of authority to offer MySuper products will remove a fund's ability to accept default contributions, and a term in a modern award nominating such a fund would have no effect. APRA would be required to notify FWA if it cancels a fund's authority to offer a MySuper product, and FWA would be able to remove any reference to the non-compliant fund. It is not anticipated that non-compliance would occur very often.

3.4.4 Given the fundamental relationship between governance issues and APRA's prudential regulation, and in particular that APRA's capacity to remove authorisation for MySuper products from a fund means it would be unable to be listed in the award, we question the need for further consideration of governance issues as part of the assessment process.

3.5 Administrative efficiency of the fund

3.5.1 The Commission has proposed that a fund's administrative efficiency be assessed according to a set of benchmarks, which would be determined by APRA (or other appropriate body) in consultation with the industry (draft recommendation 6.3).

3.5.2 We support administrative efficiency as a relevant factor in the assessment process. However, given APRA's primary focus on prudential regulation, it would not be best placed to set relevant efficiency benchmarks. Nor should this task fall to FWA, given its role is assessing funds against this and other criteria.

3.5.3 The Government is establishing a SuperStream Advisory Council to provide advice to Government on the efficient and effective implementation of the new superannuation data and payment standards and e-commerce requirements resulting from SuperStream. The Council is to have an ongoing role post-implementation of the SuperStream reforms in monitoring the success of the standards and recommending refinements and improvements to the standards where appropriate. The SuperStream Advisory Council, in consultation with other parties, may be well-placed to develop benchmarks for administrative efficiency having regard to the implementation of the SuperStream reforms.

4. EMPLOYER ABILITY TO CHOOSE A FUND

4.1.1 Draft recommendation 8.2 proposes that employers selecting default funds for employees to whom the superannuation provisions of modern awards apply should be able to choose a fund not listed in the relevant award, though they should be required to justify their alternative choice (under arrangements that are not canvassed in the Draft Report) and demonstrate that the employees are 'at least no worse off' as a result. We do not support this proposal and consider it raises considerable risks to the integrity of the proposed default fund arrangements, the safety net and FW Act framework.

4.1.2 As a matter of principle and at law, an employer cannot unilaterally determine to 'opt out' of the safety net, including 'opting out' of provisions of a modern award. While the Commission states in the Draft Report that many pre-modern awards allowed employers to choose any fund, this is not the case. Pre-modern awards did not give employers the ability to unilaterally 'opt-out' of a safety net provision – any deviations from such provisions required agreement or approval. The FW Act provides mechanisms through which an employer may alter provisions of the safety net; for example, the making of an enterprise agreement. Importantly, these mechanisms are based upon employee agreement and an assessment that the employee's terms and conditions will be 'better off overall' when compared with the applicable award or agreement.

4.1.3 In light of this, any process to allow employers to choose a default fund that applies to their award covered employees and which is not a fund listed in a modern award would need to be rigorously administered. For example, how would an employer demonstrate an employee is 'at least no worse off'? Would this criterion apply to one, all, or a majority of employees within the workplace (or a particular class or classification of employees)? It is difficult to see how the proposed mechanism, with sufficiently rigorous administration, would provide a workable option for employers. The proposed justification requirement could also impose a significant red tape burden on employers. Further, failing strict administration of this criterion, employees would be exposed to the risk that a fund selected is not in their best interests.

4.1.4 As set out above, employers wishing to select a fund not listed as a default fund within the applicable modern award are able to negotiate an enterprise agreement with their employees to achieve this end. There is significant flexibility in agreement making under the FW Act and, should an employer and their employees wish, the agreement can be limited to just the choice of superannuation fund, deferring to the applicable modern award for all other conditions.

4.1.5 Additionally, it is important to note that regardless of the default funds listed in modern awards, all employees have the right to exercise choice of fund and nominate their preferred superannuation fund.