Trustee Corporations Association of Australia

House of Representatives Standing Committee on Ageing

Long Term Strategies to Address Ageing of Australia's Population Over Next 40 Years

December 2002

EXECUTIVE SUMMARY

The Trustee Corporations Association of Australia is pleased to offer comments on three matters associated with the ageing of Australia's population:

- effective protective arrangements for the aged,
- prudent financial management of retirement villages, and
- the adequacy of retirement incomes.

1. Effective protective arrangements for the aged

We believe that much of the potential trauma associated with the personal finances of the aged, particularly when conditions such as dementia are involved, can be addressed by giving early attention to effective protective arrangements, ie:

- preparation of a will that clearly expresses a person's wishes in respect of their estate, and
- creating an enduring power of attorney, whereby a third party is appointed to make financial (and possibly other) decisions on behalf of a person if that person becomes unable to manage their own affairs.

We submit that:

- relevant legislation should be unified across Australia, to overcome the difficulties that frequently arise with wills and powers of attorney outside the region in which they are drawn,
- a register of powers of attorney should not be established ahead of very careful consideration being given to whether the benefits (such as enhancing accountability and facilitating better protection against abuse) offset the costs (including reduced privacy and increased expense), and
- in situations where elderly people are unable to look after themselves and a Court appoints a financial manager and/or a personal carer, the body charged with reviewing their performance should be independent of those parties.

2. Prudent financial management for retirement villages

We suggest that strengthening the financial management of retirement villages, through enhanced independent checks and balances, would provide greater protection and peace of mind for the aged in relation to what is normally a major investment decision aimed at achieving a comfortable retirement lifestyle.

3. The adequacy of retirement incomes

We suggest that strengthening the regulatory framework for superannuation and managed investments, by enhancing the independent compliance monitoring function, would have a positive impact on retirement incomes by:

- providing greater safety for people's retirement balances, by reducing the prospect of fraud, negligence and exploitation of the elderly,
- helping put downward pressure on the costs and fees associated with the management of retirement balances, and
- better ensuring sound long-term investment practices.

A stronger regulatory framework would also reduce the likelihood of calls on taxpayers or the financial services industry to compensate investors who suffer loss due to fraud.

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1. INTRODUCTION

The Trustee Corporations Association of Australia (the Association) is the national representative body for the statutory trustee corporations industry in Australia. Its 17 member organisations include all of the Public Trust Offices and the great majority of the private trustee corporations.

Background information on the Association and the trustee corporation industry is provided in the attachment.

2. EFFECTIVE PROTECTIVE ARRANGEMENTS FOR THE AGED

For many elderly people, managing their financial affairs can become a challenging and potentially stressful task, both for themselves and their families. This is particularly so when common conditions associated with ageing, such as dementia, are involved.

The Association believes that an important element in the Government's strategies for addressing the ageing population should be to encourage people to give early attention to effective protective arrangements, both for their assets and their personal affairs.

We suggest that this is done most effectively through wills, powers of attorney, Court orders for financial management or personal care, and administration of deceased estates. The Government should seek to ensure that:

- to gain the benefits of properly constructed wills and powers of attorney, and proper and efficient deceased estate administration, these services be widely understood and promoted,
- to prevent abuse of the elderly, those involved in the commercial supply of these important services be appropriately qualified, insured and regulated, and
- to ensure proper regulation and oversight, there be genuine and unambiguous independence between the provider of a service and those charged with regulating the service provider.

2.1 Preparing a valid will

One very important way of minimising some of the potential trauma associated with personal finances is for people to ensure that they prepare a will that clearly sets out how they want their assets to be distributed after their death.

If a person dies without a will (ie "intestate"), their estate will be distributed according to the relevant State/Territory legislation, which may not be consistent with their intentions, and may result in delays and additional costs in settling the estate.

To make a valid will, a person must:

- be of the correct age,
- understand that they are making a will,
- exercise genuine free choice,
- understand the property being disposed of and the manner of its disposition, and
- be free of mental disorder.

It is therefore essential that a person attend to their will <u>before</u> a lack of mental capacity prevents them from doing so. The ageing process, of course, often leads to conditions such as dementia, which affect the ability to prepare a valid will.

When preparing a will, competent professional advice is usually desirable, and in many cases essential:

- For a will to be valid, specific legal requirements must be met and precise meaning conveyed. If the language in the document is ambiguous, it may be necessary for the Court to provide judicial interpretation. Apart from adding to costs, the outcome may fail to truly reflect the wishes of the deceased, despite best endeavours.
- It is also important to recognize that the law sets boundaries on the types of dispositions that are allowed under a will. Even if the will is crystal clear as to intent, if that would result in these boundaries being crossed, then the Court will prevent the stated intent being implemented. For example, regardless of the

will's intent, investments owned by the deceased in a joint bank account or jointly-owned equities cannot pass into the deceased's estate for distribution. This is because the *"rights of survivorship"* give the surviving owner(s) the whole of the property. It may therefore be important to implement a proper estate plan, of which a will is just one component.

2.2 Administering a deceased estate

Deceased estates can involve unnecessary stress for many elderly people. This can arise because they find themselves as executors of a deceased estate, which carries onerous fiduciary responsibilities and can be administratively complex. Stress can also arise where an elderly person is a beneficiary of a deceased estate of which another family member is executor, and where a family dispute arises.

The Association recommends that the Government consider:

- a legislative requirement that will-makers discuss with their clients the importance of the level of competence of their chosen executor - this could cover such matters as the benefits of an independent executor in situations of potential tension or family conflict, and to minimise potential misrepresentation, concealment or fraud by an executor, and
- greater priority being given to uniformity and, importantly, simplification of succession laws - currently, and notwithstanding work over many years, interstate probate dealings remain unnecessarily complicated and costly due to lack of regional uniformity of the relevant laws and Court practices.

2.3 Granting an Enduring Power of Attorney

It is important that people's wishes about their assets and personal affairs are given effect not only after death, but also in the period before death when they lack either the desire or capacity to attend to these matters personally. Powers of Attorney are the most effective means of enabling this.

A General Power of Attorney permits a person (the donor) to confer legal authority on another person (the attorney) to make various financial decisions on behalf of the donor (for example, while the donor is overseas for an extended period). However, this power ceases to have effect when the donor loses mental capacity.

An Enduring Power of Attorney (EPA), on the other hand, continues to have effect after the donor loses mental capacity, and thus can be a most valuable element of a strategy to ensure that elderly persons are able to continue to have their wishes carried out even as their capacity reduces with age.

An EPA is a practical, flexible and relatively cheap instrument that can be revoked or altered whilst ever the donor has capacity. The donor can specify the time that the power of the attorney is to commence (eg. from the time the document is executed; from a certain date; or on a particular event, such as the donor being deemed to have lost capacity). The donor also is able to specify the actions that the attorney can and cannot take on behalf of the donor in respect of financial matters and personal/health matters.

It is important not only that the attorney be a party trusted by the donor to handle the fiduciary responsibilities, but also that the attorney be competent to do so, and does so without exploitation.

There is evidence that abuse of vulnerable people can and does occur under an EPA, as it does when no EPA is in place. Inappropriate behaviour by an attorney, even if unintentional, can cause irreversible damage to the donor's quality of life. For this reason, the Association supports consideration of proposals that have been made by various State/Territory bodies to strengthen the safeguards applicable to EPAs.

2.3.1 Possible improvements to EPAs

Possible improvements to EPAs are at various stages of discussion or enactment across the States/Territories. Initiatives supported by the Association include:

- More robust standards for the execution of EPAs - this might involve:
  - incorporating in the document an outline of the attorney's responsibilities,

- requiring the EPA preparer to inform the donor of the necessity to consider the professional expertise and business acumen of their chosen attorney, and
- requiring formal acceptance of those responsibilities by the attorney.

- <u>Greater uniformity</u> throughout Australia in the format of EPAs, or mutual recognition among the States/Territories of each jurisdiction's form.
- <u>Requiring attorneys to prepare an annual statement</u> of their financial dealings under the EPA, to ensure a reasonable level of accountability and to discourage inappropriate behaviour.
- <u>Stronger monitoring and investigative powers</u> for relevant bodies. While complaints of abuse of power by attorneys can be referred to the relevant Supreme Court or bodies such as the *Guardianship Tribunal* in NSW, the *Guardianship and Management of Property Tribunal* in the ACT, the *Office of the Adult Guardian* in Qld, or the *Victorian Civil and Administrative Tribunal*, strengthening the monitoring and investigative powers of those bodies (perhaps to include random audits) would ensure more effective surveillance of attorney performance.
- <u>Proper governance</u> practices be applied to the entities charged with protecting the elderly, and indeed vulnerable persons in general. The most important requirement in proper governance is <u>genuine independence</u> between:
  - those entities that undertake the protective arrangements and have charge of vulnerable persons' funds, and
  - the Courts or Government agencies that appoint the financial manager and/or have monitoring and investigative powers to check that the fiduciary responsibility is properly exercised.

The Association believes that the Government should require separation of the appointment, regulatory and financial management roles, so that not only is conflict of interest absent, but is clearly seen to be absent.

2.3.2 Consideration of an EPA register

There have been suggestions that a central (electronic) register of EPAs be established. At present, EPAs generally only need to be registered if the attorney is going to lease, sell or mortgage the donor's house or, in some cases, sell/deal in the donor's shares.

Extending registration to all EPAs would seem to offer potential benefits of enhanced accountability for attorneys and easier monitoring of dealings under EPAs by the authorities. Were the register public, the bona fides of an attorney could be checked.

However, a register is potentially very costly, and raises serious privacy concerns. It is possible that many elderly people would elect to do without an EPA, rather than have their privacy compromised by registration. If this were the case, a registration requirement might prove counterproductive.

If registration were to be adopted, it should be done on a national basis. If EPAs were registered in some jurisdictions only, concerns would arise with regard to cross-recognition and jurisdiction-hopping.

The Association is therefore strongly of the view that a register should not be established without this issue receiving careful thought and consultation. We would be pleased to participate in such an exercise.

2.4 Court orders

If an elderly person needs looking after, but has not put in place an EPA to express their wishes, then in some cases the Courts will appoint:

- a financial manager, and
- a personal carer.

The same entity could undertake both roles.

Tensions can arise between the two roles. Personal carers tend to focus more on current lifestyle, whereas the financial manager focuses more on the need to preserve funds so that a certain lifestyle can be maintained for a longer period. If such tensions need to be resolved, then the Association submits that the relevant review body should:

- be genuinely independent of both the carer and the financial manager, and
- have a reasonable balance of experience in both financial and personal affairs.

Tension can also arise if financial managers are expected to undertake an unreasonable amount of personal care work without compensation, or if personal carers are expected to take responsibility for financial management for which they are untrained. The Association submits that the personal care and financial management roles should be separately identified and costed, even if undertaken by the same entity. We do not object to governments subsidising certain activities (particularly in respect of vulnerable persons) but believe that accounting for any such subsidies should be transparent.

3. PRUDENT FINANCIAL MANAGEMENT OF RETIREMENT VILLAGES

Increasingly, many elderly people are choosing to move to a retirement village with a view to enjoying a comfortable lifestyle in their post-work years. This step normally represents a major investment decision.

Key areas of potential exploitation include:

- the terms on which a retiree buys into a retirement village,
- the manner in which the funds held by the village operator are protected, invested, and utilised, and
- the terms on which monies are repaid to retirees (or their estate) on leaving the village.

The Association believes that the Government should give consideration to strengthening the financial management arrangements for retirement villages, through enhanced checks and balances on their operations, in order to provide greater protection and peace of mind for retirees. Many residents of retirement villages, because of age/capacity factors, are likely to be more susceptible to exploitation than (say) investors in superannuation funds and managed investment schemes.

The *Retirement Villages Bill* now being considered in New Zealand will introduce a range of enhanced administrative, reporting and procedural requirements for retirement village operators, aimed at strengthening the protection of current and intended residents.

The present New Zealand legislative regime applicable to retirement villages - the *Securities Act 1978* and the Securities Act (Retirement Villages) Exemption Notice 1999 - generally requires the presence of a "statutory supervisor", approved by the Securities Commission, to represent the collective interests of residents and provide external oversight of conditions of entry for villages and their ongoing financial operations.

The Association submits that the New Zealand model may well warrant investigation by the Government.

4. THE ADEQUACY OF RETIREMENT INCOMES

A person's retirement income depends on a combination of factors:

(a) the level of the person's investments, including in superannuation and managed funds,

(b) the amount of tax paid on those investments,

(c) the level of earnings on those investments,

(d) the level of fees charged by the fund operators and other service providers, and

(e) any losses suffered by funds due to maladministration, negligence or fraud.

This section highlights how the last three items (earnings, fees and losses), and hence the adequacy of retirement savings, can be greatly influenced by the regulatory framework for superannuation funds and managed investment schemes.

4.1 Earnings

Conflict of interest can adversely affect a fund's earnings if there is no independent check to prevent a fund manager:

- outsourcing the investment advice function to a related party that is less capable than unrelated advisors that might otherwise be appointed, or
- acquiring assets at prices higher than would be negotiated at arm's length.

Association members can point to many examples of this being attempted by fund managers before the *Managed Investments Act 1998* (MIA) removed trustee companies as independent scrutineers of fund manager compliance, and replaced them with a regime of self-regulation.

4.2 Fees

The *Australian Consumers' Association* (ACA) has been very critical of what it sees, in some cases, as an "inexcusable" level of charges on superannuation accounts. It has expressed concern at the high level of fees in Australia - around 2 percent compared with 1 percent in the US and 1 .45 percent in Europe.

The ACA has noted that, for the "average" superannuation fund member, a 1% pa asset-based fee charged over the person's working life can reduce the accumulated amount on retirement by about $100,000.

The Association supports moves to provide greater transparency and clarity about the full range of fees and charges levied by funds/schemes. While the *Financial Services Reform Act 2001* (FSRA) purports to add clarity, we share the reservations expressed by various commentators about the usefulness of the Ongoing Management Charge (OMC) in its present format.

Downward pressure on fees would arise if there were:

- clarity about all fees charged by fund operators, including trailing commissions paid to financial advisors,

- clarity about the impact of such fees on long-term retirement balances, and
- independent review of those fees (including fees paid to related parties).

4.3 Losses

Shortcomings in regulatory arrangements, coupled with inadequate compliance, can result in the loss of hard-earned retirement savings. Recent examples include:

- the failure of *Commercial Nominees of Australia Ltd* (CNA), an Approved Trustee for about 500 small superannuation funds - conflicts of interest and possibly fraudulent investments by CNA, which was overseen by the *Australian Prudential Regulation Authority* (APRA), resulted in losses of some $25 million for 25,000 investors, and
- losses of several hundred million dollars suffered by thousands of investors in solicitors' mortgage schemes – those schemes, which were subject to inadequate supervision by the industry bodies (Law Societies), were poorly managed, involved conflicts of interest and fraudulent property valuations.

Inadequate regulation can also result in costly industry or Government compensation to fund members who suffer loss as result of fraud.

The Government, for example, has decided to grant financial assistance of some $12 million to about 180 of the funds that were formerly under the trusteeship of CNA. The case for compensation in respect of the other 300 funds that suffered losses under CNA's management is still being investigated, years after the event. In the meantime, retirees are suffering financial and emotional distress.

It is also interesting to note reports that a group of self managed superannuation funds (SMSFs) which lost several million dollars as a result of the CNA problems are considering suing APRA. Although SMSFs are supervised by the Australian Taxation Office, and hence not eligible for compensation under Part 23 of the *Superannuation Industry (Supervision) Act 1993* (SIS), members of those funds claim that they would not have invested with CNA if it had not borne APRA's "seal of approval."

4.4 Recommended improvements

The Association submits that three key changes should be made in order to strengthen the current regulatory structure for superannuation and managed funds:

- expand the independent compliance function – this would represent a preventative measure to improve governance and reduce the probability of serious problems arising in the operation of funds,
- widen access to the compliance role – to promote competition in the provision of this service, and
- ensure adequate financial underpinnings for fund operations – to provide greater means of non-Government compensation to investors in the event of losses due to negligence or fraud.

4.4.1 Expand the independent compliance function

We believe that the present roles carried out by a superannuation fund's independent compliance auditor and a managed scheme's independent compliance plan auditor should be expanded. This important function should be performed on a more regular and timely basis than is required at present, in order to better protect investors by minimising the likelihood of losses arising from non-compliance, non-arm's length dealings, and fraud.

This role should entail:

- monitoring the adequacy of a formal compliance or risk management plan,
- monitoring the fund operator's compliance with the compliance plan and other obligations,
- ensuring that competitive prices are negotiated on an arm's length basis for services provided to the fund, often by related parties, such as custody, administration and investment advice,
- monitoring the reasonableness of the investment performance benchmarks, and
- reporting periodically, say quarterly, to the fund operator and, as necessary but

at least annually, to APRA / the *Australian Securities and Investments Commission* (ASIC) and investors on compliance performance.

4.4.2 Widen access to the independent compliance monitoring role

The Association submits that the compliance monitoring function should not be restricted to financial auditors, but opened up to more competition, and to a deeper and broader pool of expertise, by licensing other independent entities which can demonstrate the necessary skills and financial underpinnings to carry out this work effectively.

The Government endorsed such an approach in its interim response to the *Productivity Commission's* review of superannuation legislation. The Commission had noted that, while specific skills and competencies are required to undertake compliance audits, approved financial auditors are not uniquely qualified to acquire them.

Indeed, financial auditors may not necessarily be the most suitable persons to conduct compliance audits given that these involve a high level of operational matters.

The Commission added that separation of financial and compliance audits would bring different perspectives to a fund's position, which could enhance prudent management. This is supported by recent concerns raised about auditor independence, for example in Professor Ramsay's review last year.

The Commission quoted submissions suggesting that potential compliance monitors might include lawyers and actuaries. We submit that other potential compliance monitors include compliance arms of existing superannuation and managed funds, superannuation administrators, trustee corporations, and specialist risk management firms.

In October, the Government, in its response to the report of the *Superannuation Working Group* (SWG) on the safety of superannuation, supported recommendations to improve investor protection by:

- permitting funds whose trustees might lack appropriate skills to "buy in" that expertise,

- requiring trustees to develop, and have audited annually, a Risk Management Plan (RMP) for each fund they operate, and
- examining the feasibility of mechanisms for <u>independent</u> oversight of trustees' compliance with RMPs, and for reporting breaches to the regulator.

More recently, the *Joint Committee on Corporations & Financial Services* (JCCFS) released its report on its inquiry into Malcolm Turnbull's review of the MIA. Recommendations include:

- amending the definition of "external" directors to mean "independent",
- permitting corporate compliance entities to serve on compliance committees,
- for compliance plan auditors, improve independence, expand the role, and require them to report to investors,
- Treasury and ASIC to consider opening up the field for compliance plan auditors, and
- ASIC to monitor, review and report to the JCCFS on third party vs in-house custody.

Enhancing the compliance monitoring role should reduce the likelihood of misconduct by fund operators. Opening up that role to more competition should place downward pressure on operating costs. Both factors would contribute to investors having a larger "nest egg" on retirement.

4.4.3 Ensure adequate financial underpinnings for fund operations

The Association believes that the regulatory regime should ensure that the commercial parties involved in the operation of superannuation funds and managed funds – that is, Approved Trustees, REs, compliance entities and custodians - should have adequate financial underpinnings to address operational risk, including non-compliance with legislative and prudential requirements.

Those financial resources should comprise an appropriate mix of capital and insurance.

Further, capital and insurance requirements should have proper regard to the amount of funds being managed and not be capped at an inappropriately low maximum such as the

present $5 million. It might be noted that the Productivity Commission also recommended that the capital requirements for Approved Trustees be strengthened.

We do not see the need for groups of individual "Not for Profit" trustees (referred to as "notional entities" by the SWG) operating corporate and industry funds to meet minimum capital and insurance requirements, provided these trustees utilise well-capitalised and insured compliance entities and custodians to provide the necessary financial underpinning for those funds.

In response to the SWG report, the Government undertook to revisit the question of the appropriate level of financial resources for trustees in the light of experience with the new licensing and RMP requirements.

More recently, the JCCFS recommended that ASIC review its net tangible asset and insurance requirements for the responsible entities of managed funds to determine whether they should be subject to periodic adjustment to take into account, for example, CPI rises or the quantum of funds under management.

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Attachment

TRUSTEE CORPORATIONS ASSOCIATION OF AUSTRALIA

The Trustee Corporations Association, formed in 1947, is the national body for the trustee corporations industry in Australia.

It represents 17 organisations, comprising all 8 Public Trust Offices and all but 2 of the 11 private statutory trustee corporations.

The Association has a staff of 4 and operates out of premises in Sydney. It is controlled by a National Council, which comprises the Chief Executive Officer of each member institution, and an Executive Committee, comprising a small group of those persons.

Member products and services

In the 1870s, Governments first enacted legislation to extend the role of executor or administrator of an estate, traditionally taken on by a natural person, to licensed trustee corporations. This was to benefit the public by providing greater expertise and resources than are available from an individual, together with perpetual succession to a client establishing a long-term trust.

Today, trustee corporations provide a wide range of financial services to individual, family and corporate clients. Services include:

- **Traditional personal wealth management**
  - Wealth protection and transfer
    - estate planning
    - writing wills
    - acting as executor of deceased estates
    - establishing, and acting as trustee of, personal trusts, including testamentary trusts
    - administering client assets under Powers of Attorney
  - Protecting vulnerable members of the community
    - by acting as guardian or financial manager, usually under Court order, for persons unable to look after their own affairs, including minors and the intellectually-disabled
  - Administering charitable trusts and foundations
    - including for medical research, galleries, museums, and education scholarships
- **Other personal business**
  - trustee or administrator for small superannuation funds
  - providing tax advice and preparing tax returns
  - financial planning

- **Funds management**
  - offering most types of unit trusts and common funds
- **Corporate activities**
  - registry operations
  - custodial services
  - trustee for debenture and convertible note issues
  - securitisation facilities
  - compliance monitoring
  - trustee or administrator for retail superannuation funds

Member organisation characteristics

- Reputation of trust, based on:
  - High professional and ethical standards
  - Prudent corporate governance
  - Specialist skills
- Providing security and peace of mind to clients, based on:
  - Over a century of experience
  - Continuity of operation, including operating perpetual trusts
- Quality customer service and advice, based on:
  - Courtesy and empathy
  - Integrated, competitive product offerings
  - Reliability of service delivery

Association objectives

- To advance and protect the interests of beneficiaries of trusts and other operations administered by statutory trustee corporations
- To advance the cause of investor protection in the Australian financial system, by promoting the importance of independent review generally and independent compliance monitoring specifically
- To represent and advance the interests of member statutory trustee corporations
- To be recognised as an important group of non-banking financial institutions
- To provide professional education and set professional standards for officers of statutory trustee corporations

Industry statistics

In aggregate, trustee corporations have about $300 billion of assets under administration, and capital resources of about $600 million. They employ more than 3,500 staff in over 90 offices around Australia.

Almost 2 million Australians have wills recorded with trustee corporations.

Each year trustee corporations:

- write about 60,000 wills and powers of attorney
- administer about 10,000 deceased estates
- administer assets under agency arrangements or guardianships for about 10,000 people
- prepare about 50,000 tax returns.

Association members

ANZ Executors & Trustee Company Ltd
Equity Trustees Ltd
Guardian Trust Australia Ltd
National Australia Trustees Ltd
Permanent Trustee Company Ltd
Perpetual Trustees Australia Ltd
Public Trustee for the ACT
Public Trustee New South Wales
Public Trustee for the Northern Territory
The Public Trustee of Queensland
Public Trustee South Australia
The Public Trustee Tasmania
Public Trustee Western Australia
Sandhurst Trustees Ltd
State Trustees Ltd
Tasmanian Perpetual Trustees Ltd
Tower Trust Ltd