

Additional Comments by Coalition Members

1.1 This Bill is the fourth tranche of MySuper legislation and also makes governance changes flowing from the Super System Review (Cooper Review) and the government's response to that review (Stronger Super).

1.2 Whilst Coalition members of the Committee broadly support the majority report, two outstanding issues should be addressed when this legislation is considered by Parliament.

1.3 In the meantime it should be noted that this is yet another piece of legislation in relation to superannuation that appears to have been rushed and poorly drafted and is in need of numerous amendments after being introduced into Parliament as a result.

Independent directors

1.4 Good corporate governance of superannuation funds is of vital importance to those Australians whose retirements savings are entrusted to those funds.

1.5 The goal of regulators must be to deliver the most transparent, the most efficient and the most competitive superannuation system possible, with appropriately high corporate governance and transparency standards.

1.6 Only the most transparent, efficient and competitive superannuation system with appropriately high corporate governance arrangements will lead to Australians' retirement savings through their super being maximised.

1.7 The equal representation model was introduced in 1993, supposedly to balance employer and employee representation. The Cooper Review described a number of reasons why this system was no longer contemporary or appropriate, including:

- The superannuation system has moved substantially away from single-employer defined benefit funds that were dominant in 1993. The introduction of fund choice, together with the prevalence of defined contribution funds today, materially changes (and in many cases severs) the close relationship that previously existed between the employer and the super fund.
- The representatives on many trustee boards nominated by third party organisations, such as trade unions. Current employment and industrial relations practices mean that these organisations do not necessarily represent all employers or all employees. Thus, the democracy that the equal representation policy appears to embed in the governance of superannuation funds is not always present in reality. The equal representation model also could result in a perception that individual trustee-directors are required to answer to the organisation that appointed them in respect of trustee decisions or that they are dictated to by that organisation.

- The large number of employers, employer organisations and employee organisations related to a fund can sometimes result in trustee boards being far larger than makes sense for efficient governance of that fund.
- Equal representation leaves significant groups 'unrepresented.' Key among these are members who are pensioners and members who have joined the fund because they exercised fund choice. These groups of members, already sizeable in some funds, can be expected to grow in the future.

1.8 The Cooper Review recommended an end to the equal representation model on superannuation boards (under which union and employer representatives dominate Industry Super funds):

Recommendation 2.7

For those boards that have equal representation because their company constitutions or other binding arrangements so require, the SIS Act should be amended so that no less than one-third of the total number of member representative trustee-directors must be non-associated and no less than one-third of employer representative trustee-directors must be non-associated.

1.9 The Cooper Review found that the equal representation model was not serving the best interest of Australians saving for their retirement.

1.10 In the Coalition's view the equal representation model creates clear conflicts of interest that disadvantage superannuation fund members—working families across Australia.

1.11 The government has failed to act on this recommendation despite a broad industry consensus on its value, as revealed in the inquiry into this Bill:

Financial Services Council

Mr Bragg: We thought that the Cooper review recommendations were sensible, particularly as they related to independent directors. That was not accepted in the government's response. Subsequently we have said it was important that it move to a more contemporaneous government model. Through self-regulation we have adopted a model of a majority of independent directors for our members. That commences on 1 July 2013, rolling through transition arrangements to 1 July 2014. So, on balance, we thought the recommendations in the review were sensible and so have in part adopted those through industry self-regulation.

Senator CORMANN: If the coalition were to move amendments to give effect to that recommendation of the Cooper review, the FSC would be supportive?

Mr Bragg: The interesting thing is that it has been on the record that the model recommended by people was a step in the right direction.¹

Association of Superannuation Funds of Australia

Senator CORMANN: So does that mean that it would be appropriate to have more diversity of perspectives represented on super boards than is currently the case?

Ms Vamos: Yes. In ASFA's view we have some funds that have adopted the model of 3-3-3: three employer, three employee and three independent. We believe that goes a long way towards ensuring that there is that flexibility to have that breadth of experience on the trustee board.²

Law Council of Australia

Ms McAlister: I believe that, when we made our original submission on the Cooper report, we were in favour of that recommendation. We could see that it had merit—the idea of having, I think it was, one-third independent, one-third employer representatives and one-third members. We could see that there would be some merit in that.³

1.12 The Labor government continues to ignore this important governance reform. This is because the current Minister for Superannuation is more focused on the vested interests of his friends in the union movement than on the public interest as outlined in the Cooper Review. This is even though the Cooper Review was commissioned by his own government.

1.13 It is proposed that this Bill be amended to give effect to the principle that each affected trustee board or group of trustees at a minimum will contain one-third in number of independent directors or trustees.

1 Mr Andrew Bragg, Senior Policy Manager, Financial Services Council, *Proof Committee Hansard*, 22 January 2013, p. 3.

2 Ms Pauline Vamos, Chief Executive Officer, Association of Superannuation Funds of Australia, *Proof Committee Hansard*, 22 January 2013, p. 9.

3 Ms Pamela McAlister, Deputy Chair, Superannuation Committee, Legal Practice Section, Law Council of Australia, *Proof Committee Hansard*, 22 January 2013, p. 18.

Ban on caps for administration fees

1.14 This Bill is the fourth and (as the government anticipates) last tranche of legislation implementing the MySuper proposal that arose from the Cooper Review. The first bill (Tranche I) established the core provisions for MySuper, which included rules around the charging of fees in relation to member accounts. This included, in effect, a ban on caps for administration fees (as paragraph 6.14 of the explanatory memorandum of the Tranche I Bill discussed):

For any fee that applies to all members of the MySuper product, such as an administration fee or an investment fee, each member is to be charged the fee under the same charging rule. For example, if one member is charged a percentage of their account balance in relation to the MySuper product as an administration fee, then each member of the MySuper product should be charged the same percentage of their account balance in relation to the MySuper product at the same point in time.

1.15 This caused an adverse reaction among industry stakeholders at the time. These stakeholders, as well as the Coalition, were anticipating that the government's current and final MySuper bill (Tranche IV) would include amendments to remove this unnecessary and counter-productive requirement. However, such amendments have not been forthcoming in this Bill.

1.16 As such, the Coalition considers that the current Bill should be amended to allow trustees of MySuper accounts greater flexibility in how they charge fees, and especially in relation to administration fees that are asset-based (ie based on the size of the account balance).

1.17 In particular, a cap or limit to asset-based administration fees should be allowed under the legislation to ensure that fees remain commensurate (or align as close as practicable) with the actual costs of holding accounts, irrespective of the magnitude of their balances.

1.18 Providing super (and other) accounts tend to involve fixed costs (set-up, collecting contributions, investing them, providing statements, reporting, website service, etc) that are large relative to their variable costs. As such, fee formulae are often based on a fixed cost plus a small fixed percentage of the account balance, but only up to a certain threshold or cap, to ensure fees don't become excessive or disproportionate (especially on large account balances).

1.19 The key concern of the Coalition is that, without a cap on fees, a \$500,000 account, for example, could be charged an administration fee one hundred times greater than that of a \$5,000 account. This is despite the fact that the costs to administer those accounts may actually be quite similar and unrelated to size of balance.

1.20 Without caps, the more you have in your super account, the more you can end up paying, even though you might not be receiving any additional service, which is

inherently unfair, inequitable and inefficient (through the perverse signals and incentives that arise).

1.21 Assuming no profiteering (ie that adequate competition in the market place already exists), this will lead to excessive fees being charged on accounts with larger balances being used to cross-subsidise the under-charging of fees on small-balance accounts. Such obvious and significant cross-subsidisation—which in this instance is so easily avoided by allowing caps—is in no way efficient nor equitable.

1.22 The great irony is that the latter principle (equity and equality) is stated as a key objective of the Bill and (quite absurdly) is put up as a key justification for why no cap on fees is being proposed.

1.23 Ultimately, competition and innovation should discipline and drive fee structures, which should wherever possible be left to the discretion of the account/service provider (the expert).

Views of industry stakeholders

1.24 The industry stakeholders that will be imposing the administration fees on MySuper accounts going forward strongly advocate that caps be allowed, as the following key and pivotal comments, particularly from the inquiry's hearing, attest.

Association of Superannuation Funds of Australia

1.25 In its comments to the inquiry's hearing, the Association of Superannuation Funds of Australia (ASFA) not only advocated the flexibility to have caps but also explained the undesirable and perverse incentive that would otherwise arise:

Ms Vamos: So we have advocated for quite some time that there needs to be the flexibility, as there is now, for trustees to ensure that the fees that they charge are equitable **and that, if it is appropriate to put a cap on fees, they are able to do so.** Otherwise, we are going to have the bizarre situation—and it was confirmed by one fund yesterday—that they will feel they have an obligation to contact all of their larger account balance members in their MySuper products and encourage them to move to a choice product. This may not be in their best interest in terms of long-term returns.⁴

1.26 Also from ASFA:

Ms Vamos: I cannot answer on behalf of the government as to why they do not think a cap is appropriate. I can say that certainly we understand as an association that this is an intended policy. We understand this is not a

4 Ms Pauline Vamos, Chief Executive Officer, Association of Superannuation Funds of Australia, *Proof Committee Hansard*, 22 January 2013, p. 6 (emphasis added).

drafting error and that is why it is covered off as one of the significant issues. **We think this is not good policy.**⁵

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Ms Galbraith: ... Cooper was quite clear that MySuper would not only be for the people who wanted a default but would be available by active choice. Just because someone has a higher account balance does not necessarily mean either that they are especially financially literate or, even if they are, that they actually want to take on the risk of having to manage a portfolio. They might rather have the trustee, with their expertise, exercising that. **To have a prohibition on scales and caps meaning that MySuper is no longer a suitable product for people with high account balances, we think, is contrary to the intent.**⁶

1.27 The likely implications, including overall cost to the industry and confidence in the legislation, are further explained by ASFA:

Ms Vamos: ... My concern is that it is a significant cost. Truth be said, I think the concern of some funds is that, if they ring a member and say, 'Look, we cannot apply a cap anymore; even though the overall fees may be lower, yours will be higher,' that starts to have a confidence issue in the system and maybe even in the legislation, and confidence in the system and in the industry is paramount at this time.⁷

Industry Super Network

1.28 In its comments to the inquiry's hearing, the Industry Super Network (ISN) in its opening statement was also categorical about its support for allowing a cap on fees:

Mr Watts: We have raised the issue of the fee cap on asset based fees in our submission is well. **Our view is that the fee cap should apply to administration fees.** We believe it need not necessarily apply to investment fees, but historically there has not been a concern about fee caps in relation to investment fees, that they are generally being treated equally within the industry. **There are some funds that will have an existing cap on asset based fees and the removal of that ability to cap is a concern.** It is not, I believe, a widespread problem within the industry and it is related to administration fees but we should share that concern. That concludes my opening remarks.⁸

5 Ms Pauline Vamos, Chief Executive Officer, Association of Superannuation Funds of Australia, *Proof Committee Hansard*, 22 January 2013, p. 8 (emphasis added).

6 Ms Fiona Galbraith, Acting General Manager, Policy and Industry Practice, Association of Superannuation Funds of Australia, *Proof Committee Hansard*, 22 January 2013, p. 12 (emphasis added).

7 Ms Pauline Vamos, Chief Executive Officer, Association of Superannuation Funds of Australia, *Proof Committee Hansard*, 22 January 2013, p. 10.

8 Mr Richard Watts, External Relations Manager and Legal Counsel, Industry Super Network, *Proof Committee Hansard*, 22 January 2013, p. 21 (emphasis added).

1.29 Also, when asked about caps being disallowed and the likelihood of fees being significantly higher for large-balance accounts without additional services necessarily being provided, ISN said:

Mr Watts: Yes. ISN supports those views that asset based fees should be capped in relation to administration fees. **We believe that there is a finite cost involved in administration of an account. It is not necessarily related to the size of the account beyond a certain point.** Although it has limited application within the industry, we believe that for those funds that have this particular issue it should be resolved: a cap should be imposed on asset based administration fees.⁹

Australian Institute of Superannuation Trustees

1.30 In its comments to the inquiry's hearing, the Australian Institute of Superannuation Trustees (AIST) in its opening statement was also clear on its advocacy for fee caps:

Mr Haynes: In relation to the prohibition of the existing MySuper legislation on fee capping—a matter that has already been extensively canvassed in the hearing this morning—**we too remain that this prohibition is not in the best interests of all members.** Put simply, the prohibition will result in higher account balance members currently entitled to a cap paying more in a MySuper product and, in some cases, much more than they do in the fund's existing default options. This affects only a minority of funds but the funds involved are not insignificant. Amongst AIST members, they include CareSuper, VicSuper, Non-Government Schools Super, Equisuper and Energy Super.¹⁰

1.31 Also, when asked about whether fee caps introduce greater complexity and make fee comparisons more complicated (key arguments put up against allowing fee caps), AIST said:

Mr Haynes: We support one cap. We do not support there being a number of different steps. **We see that that does not introduce a great deal of complexity,** and in any event the government, through changes to the original MySuper structure in relation to, say, the introduction of large employer MySuper products, has been prepared to introduce measures that, to our mind, are significantly more complicated than what we are suggesting here.¹¹

9 Mr Richard Watts, External Relations Manager and Legal Counsel, Industry Super Network, *Proof Committee Hansard*, 22 January 2013, p. 24 (emphasis added).

10 Mr David Haynes, Project Director, Australian Institute of Superannuation Trustees, *Proof Committee Hansard*, 22 January 2012, p. 26 (emphasis added).

11 Mr David Haynes, Project Director, Australian Institute of Superannuation Trustees, *Proof Committee Hansard*, 22 January 2012, p. 28 (emphasis added).

Treasury

1.32 In its comments to the inquiry's hearing, the Treasury spelt out the types of administrative costs involved in providing a member with an account and acknowledged that these costs would not likely vary much with the size of the account's balance:

Mr Rollings: I think the point I was making was to at least question the argument that administrative costs rise with the member's account balance, even below a cap. Given the level of automation for nearly all cases, the administrative service being provided to a member is that of collecting their contributions and investing it, providing regular statements and providing a website service and information. These sorts of costs are pretty much generic across the membership. So the argument that the costs for particular members go up with their account balance is at least open to some questioning.¹²

1.33 Treasury admitted that the government was trying to strike a balance among key design parameters:

Mr Rollings: ... but there are some competing considerations on this issue. The starting point with MySuper, as you know, is to treat all MySuper members equally and equitably. The goal here is not to have different tiers or classes of members within MySuper—first-class members and second-class members. Prima facie, the ability to have tiered pricing arrangements opens the door for that kind of outcome. I am not saying it would be impossible to deal with that, but there is a complexity, once you allow caps, to ensure that they are applied in an equitable way.¹³

1.34 The Coalition argues that, precisely by *not* allowing a cap on asset-based administration fees, tiers of first class and second class members (the very inequity the rules try to avoid) will arise. This is because significant cross-subsidisation cannot be avoided.

1.35 Unless a flat fee only is charged for all members (a recipe for cross-subsidisation and inequity), with asset-based fees and no cap, members with large account balances will inevitably end up cross-subsidising those with small account balances.

1.36 Without the allowance of a cap, there are insufficient degrees of freedom for trustees to deliver equitable outcomes to their members in terms of aligning actual

12 Mr Jonathan Rollings, Principal Adviser, Financial System Division, Treasury, *Proof Committee Hansard*, 22 January 2013, p. 36.

13 Mr Jonathan Rollings, Principal Adviser, Financial System Division, Treasury, *Proof Committee Hansard*, 22 January 2013, p. 34.

costs with fees charged. This is despite Treasury's observation at the inquiry's hearing that 'there are options at the trustees' disposal... [to] recalibrate their fee structure'.¹⁴

1.37 Treasury further added:

Mr Rollings: There are competing arguments on all of these things. There are trade-offs to be made between the sorts of arguments that have been put forward and the arguments around MySuper **for equitable treatment of members, simplicity and comparability** that some of the witnesses also talked about—none of which on their own are determinants; they require balancing up against each other.¹⁵

Conclusion – current ban on fee caps (remaining from Tranche I Bill)

1.38 Treasury's comments make clear that this is ultimately a delicate balancing act involving a number of trade-offs and that industry stakeholders provide vital intelligence and practical insight into how that balance can be best struck.

1.39 The key industry stakeholders in this inquiry and its hearing make clear that the current ban on caps for administration fees on MySuper accounts is inappropriate and counter-productive in terms of equality, equity and efficiency and that such a ban should be removed for the benefit of members and the industry more generally.

1.40 The Coalition supports this consensual view and considers that, at the very least, the ban on caps for asset-based administration fees (ie those based on the size of the account balance) that remains from the Tranche I Bill be removed – by adding an amendment to this Tranche IV Bill. More generally, competition and innovation should provide the discipline and motivation for what fee structures arise and prevail and, wherever possible, this should be left to the discretion of the account/service provider (the experts in the field).

1.41 As such, the Coalition proposes to move amendments to this Bill to allow trustees of MySuper fund accounts greater flexibility in the charging of fees so they can remain commensurate with actual costs, and in particular, the ability for trustees to cap asset-based administration fees on superannuation accounts.

Recommendation 1

1.42 That the Bill be amended to give effect to the principle that each affected trustee board or group of trustees at a minimum will contain one-third in number of independent directors or trustees.

14 Mr Jonathan Rollings, Principal Adviser, Financial System Division, Treasury, *Proof Committee Hansard*, 22 January 2013, p. 35.

15 Mr Jonathan Rollings, Principal Adviser, Financial System Division, Treasury, *Proof Committee Hansard*, 22 January 2013, p. 35.

Recommendation 2

1.43 That the Bill be amended to remove the ban on caps for asset-based administration fees.

**Senator Sue Boyce
Deputy Chair**

**Senator Mathias Cormann
Shadow Minister for Superannuation**

Paul Fletcher MP

The Hon. Tony Smith MP