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# Stronger Super reforms — a kaleidoscope of change awaits the industry

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The government has announced the key design aspects of its Stronger Super reforms, together with the outcomes of the consultation process led by Paul Costello, Chair of the Peak Consultative Group.<sup>1</sup> Further announcements from the government are expected shortly.

## MySuper

### *Delay of mandatory start date for contributions to MySuper to 1 October 2013*

Superannuation funds will be able to offer MySuper products from 1 July 2011.

From 1 October 2013, employers must make contributions for employees who have not made a choice of fund to a fund that offers a MySuper product in order to satisfy superannuation guarantee requirements. Additional transitional arrangements will be developed to deal with situations involving funds nominated in enterprise agreements.

In order for a superannuation fund to be named in a modern award, it will have to offer a MySuper product. Fair Work Australia will review the default superannuation funds named in modern awards to ensure that they offer a MySuper product.

Trustees offering MySuper products will need to transfer the existing balances of their default members to a MySuper product by 1 July 2017. The government will consult on a mechanism to allow for this period to be extended in certain, limited circumstances. Further clarification is required as to how trustees are required to identify who their default members are.

Trustees will not have to transfer the existing member balances that relate to an entitlement to a defined benefit or that relate to certain legacy products.

The government recognises that, under the proposed framework for transition, questions could arise as to whether a trustee has fulfilled its fiduciary obligations to act in the best interests of members. Further consideration of the protection trustees may require will be undertaken in consultation with stakeholders at the legislative design phase.

### *Pricing of MySuper products*

Funds choosing to offer MySuper must offer a product with a single investment strategy and a standard set of fees available to all prospective members. However, employers will be able to negotiate with funds to obtain a discounted administration fee for their employees.

Funds will also have the flexibility to offer employers with more than 500 employees a MySuper product tailored to the needs of the particular workplace. These products will be able to differ from a fund's main MySuper product in terms of investment strategy, member services and fees.

The details of all separately tailored MySuper products and discounted administration fees will be required to be reported to the Australian Prudential Regulation Authority (APRA) and, to improve transparency, will also need to be separately published by trustees.

### *Branding*

The government will provide a limited exception aimed at cases where there is a pre-existing and distinct MySuper or default product acquired by a fund as a result of a merger or takeover. Funds will need to apply to APRA for approval to offer more than one brand of MySuper product.

### *Single, diversified investment strategy*

MySuper trustees will be required to clearly articulate the targeted rate of return (over a rolling 10-year period) and level of risk that the trustee has determined is appropriate for its MySuper members. APRA will consult with industry to determine appropriate metrics for the standard reporting of the return and risk targets for MySuper products. Trustees will also be required to use the same approach for calculating and presenting this information in the new product dashboard.

The government has decided that trustees will be allowed to use a lifecycle investment option as the single investment strategy for their MySuper product.

### ***Authorisation of MySuper providers***

Trustees will not be required to apply to APRA to hold a specific MySuper licence. However, trustees will be required to apply to APRA to be authorised for each MySuper product they wish to offer. APRA will consult on MySuper authorisation requirements in mid 2012.

### ***Fees***

Fees which a member can be charged in MySuper products will be limited to the following:

- administration fee;
- investment fee (which may include a performance-based fee, subject to the limitations below);
- buy and sell spreads (limited to cost recovery);
- exit fee (limited to cost recovery); and
- switching fee (limited to cost recovery).

Trustees may also charge fees for certain member-specific costs — for example, account splitting following a family law decision.

All fees charged for MySuper products must be able to be included under these standard descriptions.

Trustees will not be limited on the types of fees that can be charged in choice products. It will be interesting to see whether this policy creates a larger fee differential between default and choice members than is currently the case.

### ***Performance fees***

In any performance-based fee arrangement with a fund manager in respect of assets of the MySuper product, trustees must include the following provisions:

- a reduced base fee that reflects the potential gains the investment manager receives from performance-based fees, taking into account any fee cap;
- measurement of performance on an after-tax (where possible) and after-costs basis;
- an appropriate benchmark and hurdle for the asset class reflecting the risks of the actual investments;
- an appropriate testing period; and
- provisions for the adjustment of the performance-based fee to recoup any prior or subsequent underperformance.

Importantly, if a performance-based fee arrangement does not contain each of these provisions, a trustee can still enter into a performance-based fee arrangement, provided the trustee can justify that the differing arrangement continues to be in the best financial interests of the members of the MySuper product.

### ***Insurance***

Trustees must, as a minimum, allow members to opt-out of life and total and permanent disability (TPD) insurance within 90 days of the member joining a fund,

or on each anniversary of the member joining the fund. However, if trustees are unable to obtain opt-out cover at a reasonable cost, trustees of MySuper products will be required to offer compulsory insurance, while trustees of choice products can either offer compulsory insurance or no insurance. These arrangements will not apply to defined benefit funds that have insurance cover as part of the benefit design.

It will be left to the trustee's discretion whether to offer income protection insurance, on an opt-in or opt-out basis (if at all).

The government believes it is in the best interests of members to align insurance definitions with the conditions of release, so that insurance is consistent with the purpose of superannuation and so that insurance moneys are available to members at the time of their disability.

MySuper products will be required to offer a standard, default level of life and TPD insurance. Members of MySuper products will be able to increase or decrease their insurance cover (if offered by the trustee) without having to leave the MySuper product.

Within a MySuper product, it will be possible for the standard insurance cover to be replaced by a default insurance strategy tailored to meet the specific requirements of the employees of a particular employer. The 500-employee minimum does not seem to apply in this case.

### ***Post-retirement products***

The government has decided that, for the time being, a MySuper product will only cover the pre-retirement phase. Government will consult with relevant stakeholders on whether MySuper products should be required to include a post-retirement offering at some time in the future, and the framework that should apply.

### ***Capital gains tax (CGT) rollover for MySuper reforms***

The current CGT rollover relief ceases on 30 September 2011. The government has confirmed that it will consult key stakeholders on CGT consequences that may directly arise from transitioning to MySuper and to what extent, if any, CGT rollover relief will be available.

### ***SuperStream***

#### ***Efficient superannuation transactions and improved flow of super to member accounts***

The Standard Business Reporting (SBR) framework will be used as the platform to develop the taxonomy and message structures for superannuation transactions, along with the use of extensible Business Reporting Language (XBRL) for exchanging information. Additionally, the payment standard prescribed by the Australian Payments Clearing Association and international

financial messaging standards prescribed by the International Organisation for Standardisation (ISO 20022) will be used.

The government will legislate to mandate the use of the new data and payment standards for superannuation transactions and reporting to government in order to maximise the efficiencies.

The timeline for the introduction of the data and e-commerce standards is as follows.

- **Early 2012:** Data standards published and available for use by funds (voluntary uptake).
- **July 2013:** Data standards and use of e-commerce become mandatory for APRA-regulated funds and self-managed superannuation funds (SMSFs) for processing rollovers and accepting contributions (that are provided by employers in the new format).
- **July 2014:** Data standards and use of e-commerce become mandatory for large and medium employers making contributions.
- **July 2015:** Proposed application of data standards and use of e-commerce to small employers subject to further consultation on impacts.

### *Consolidation and lost super*

The timeline for the account consolidation proposals is as follows.

- **July 2011:** Funds can use tax file numbers (TFNs) as the primary locator to find accounts within a fund.
- **January 2012:** Funds can use TFNs to search the Australian Taxation Office's (ATO's) current service for searching for lost accounts — but only with member consent.
- **July 2012:** Where a member has multiple accounts within a fund, funds will be required to consolidate these accounts, where possible.
- **July 2012:** The ATO will provide a new online facility for members to view their active (but not their inactive) superannuation accounts that are currently reported to the ATO, in addition to their lost accounts and other superannuation moneys held by the ATO (for example, unclaimed money). Funds will also be able to search the account information, with member consent.
- **October 2013:** Funds will have to report all inactive accounts and lost accounts, as well as active accounts, to the ATO.
- **January 2014:** Commencement of auto-consolidation of lost and inactive accounts (two years without contributions or rollover) with a balance of less than \$1000 and accounts in eligible

rollover funds. The process will be initiated by the ATO and conducted annually.

- **July–December 2014:** The enrolment process for new employees will be modified so that employees can actively consider account consolidation at this time. If the new employee does not exercise choice, the default option will be to create a new account. Any lost and inactive accounts with a balance of less than \$1000 will be transferred into the new account through the auto-consolidation process previously mentioned.
- **Latter half of 2014:** The threshold for auto-consolidation of lost and inactive accounts will be increased to at least \$10,000, subject to a review of the threshold by the Treasury, the ATO and APRA.

### *No TFN contributions*

From 1 July 2013, where contributions are not accompanied by a TFN, the employer will be required to forward the contributions to a fund (rather than the ATO, as was recommended by the Super System Review). If the fund is unable to obtain a TFN and other identifying details within a specific timeframe, the fund will send the money to the ATO as part of the unclaimed moneys process.

### *Regular information to employees on employer contributions*

The mandatory data and payment standards, coupled with the new reporting obligations, will require employers to be mindful of the new landscape and its impact on their operations. It is likely that we will witness an increase in the use of clearing house facilities.

From 1 July 2012, employers will be required to report on payslips an “expected payment on or before” date in addition to the current entitlement during the pay period.

From 1 July 2013, subject to there being no significant payroll system costs, payslip reporting of actual contributions paid rather than just accrued contributions will commence, including the provision of information about which fund the contributions are being paid into.

Also from 1 July 2013, funds will be required to either issue six-monthly statements which show contributions made, or report electronically to members on whether they have “received” or “not received” any superannuation contributions for that quarter. The six-monthly statements commonly issued by funds which show contributions made would discharge this obligation.

### *Advisory Council*

The government has decided to establish a SuperStream Advisory Council from early 2012 to provide advice to government on continuity in the governance and oversight of the SuperStream data and e-commerce standards.

### **SMSFs**

#### *SMSF auditor independence*

SMSF auditors will be required to comply with the Accounting Professional and Ethical Standards Board's APES 110: *Code of Ethics for Professional Accountants* as a condition on their registration.

#### *Transactions involving related parties*

Related party transactions will be required to be conducted through a market where one exists. If no market exists, the transaction must be supported by a valuation from a suitably qualified independent valuer.

#### *Other SMSF issues*

All other SMSF recommendations will be implemented in line with the government's response to the Super System Review in December 2010, with one exception. The government will not amend the superannuation legislation to automatically deem anything permitted by the superannuation or taxation legislation to be permitted by SMSF trust deeds.

### **Governance**

#### *Trustee governance*

As anticipated, the concept of a new statutory office of "trustee-director" has not been accepted. Instead, the particular issues of concern identified by the Super System Review and by many in the industry will be addressed by the following changes to the law:

- introducing a duty for trustees and directors to give priority to the interests of fund members when that duty conflicts with other duties;
- strengthening the requirements for individual directors in relation to managing conflicts of interest;
- increasing the standard of care, skill and diligence required of trustees and directors of corporate trustees from an ordinary prudent person to that of a prudent person of business;
- clarifying the duties applying to individual directors of corporate trustees to act honestly and to exercise independent judgment; and
- introducing a requirement for trustees to devise and implement an insurance strategy and impose a statutory duty on trustees to manage insurance with the sole aim of benefiting members.

How this will be achieved remains unclear and there is a risk that some of these ideas for improving trustee governance will be deemed unnecessary. This is on the basis that the existing obligations on trustee directors as a matter of statute and general law already cover these matters.

#### *Investment governance*

The government will expand the covenants to which APRA-regulated fund trustees must have regard when developing an investment strategy, at either the fund or investment option level, to include its expected costs, expected taxation consequences, and the availability of valuation information.

The Super System Review also recommended that all large APRA-regulated funds should publish their proxy voting policies and procedures, and disclose their voting behaviour to members on their websites. The government will ask APRA and the Australian Securities and Investments Commission to address this issue.

#### *Operational risk financial requirement*

The government will introduce an operational risk financial requirement which will replace the existing trustee capital requirements after a suitable transitional period.

APRA will develop a prudential standard which will set out the approach for determining the financial requirement for individual funds.

The standard will also describe the roles that operational risk reserves and trustee capital will play in meeting the new financial requirement. The content of the prudential standard is to be the subject of detailed consultation between APRA and the superannuation industry. Industry will be interested to see the impact of the standard on retail and mutual funds and if there is a commonality of approach.

The requirement will be a subjective test against the prudential standard. Given the restrictions in relation to the recovery of fees for MySuper products, trustees will need to carefully determine how to fund the required reserve.

#### *Time to lodge TPD claims with the SCT*

The time limit for members to lodge a TPD claim with the Superannuation Complaints Tribunal will be increased from two years to six years, unless they have lodged a claim with their trustee within two years of ceasing employment (in which case, the time limit will be increased to four years). This will more closely align these times with the time limit under which a member can bring a similar claim in the courts.

***APRA prudential standards making power***

The government has confirmed that it supports granting APRA the power to make prudential standards in superannuation, and it is proposed that draft legislation to establish this will be introduced.

APRA has released a discussion paper in which it outlines 12 draft prudential standards. Six of these are behavioural standards which apply to authorised deposit-taking institutions, general insurers and life companies, as well as to superannuation, and six of them are superannuation-specific. APRA proposes that some elements of its existing guidance material will become mandatory obligations in the prudential standards, and the guidance material will be revised accordingly.

APRA is seeking comments on its proposals, and expects to release draft prudential standards in early 2012, with a view to finalising the prudential standards later that year.

APRA will also consult on draft prudential practice guides to support the prudential standards in due course.

***Code of governance***

The government supports a voluntary code of governance developed by industry in consultation with APRA, rather than a mandatory code coordinated by APRA.

***Offer of range of investment options***

Trustees that offer a “choice” product will be required to offer a range of investment options sufficient to allow members to obtain a diversified asset mix if they choose.

***Changed statutory investment duty***

Trustees will be required to exercise due diligence in the selection and monitoring of investment options and ensure that trustees operate in accordance with the covenants set out in s 52(2) (rather than just s 52(2)(f)) before relying upon s 55(5) as a defence to liability.

***Binding death benefit nominations***

No changes are proposed at this time to the existing requirements in relation to binding death benefit nominations.

***Giving reasons***

Trustees will be required, on request, to provide reasons for their decisions to members and eligible third parties in relation to a formal complaint. In many respects, this is an acknowledgement of current industry practice, which will now become mandatory.

The Super System Review recommended that directors of corporate trustees be required to include in their deliberations the impact of their decisions on the envi-

ronment, the community and the fund’s reputation. The government will ask APRA to consider whether this issue should be addressed through relevant guidance material.

***Next steps***

These reforms are an important and welcome development. However, they do not contain the government’s position on a number of other important issues for industry, including:

- “intra-fund” advice; and
- what costs can be funded from the MySuper product, such as clearing house services for employers, or services to workplaces designed to educate or benefit members.

The timing of the government’s next instalment on Stronger Super is not clear, but industry will be crucially interested in these issues as funds determine their MySuper and other related strategies going forward.

The reforms will be introduced in several tranches beginning in 2012, and consultation will be undertaken on each tranche of legislation.



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***Footnotes***

1. The press release from the Hon Bill Shorten MP, Assistant Treasurer and Minister for Financial Services and Superannuation, is available at <http://ministers.treasury.gov.au/>

DisplayDocs.aspx?doc=pressreleases/2011/  
131.htm&pageID;=003& min;=brs& Year;=& DocType;=0. The  
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