
Unfinished business — the superannuation reform agenda continues

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The Stronger Super reform agenda has not eased in 2012, and on 16 February the Superannuation Legislation Amendment (Trustee Obligations & Prudential Standards) Bill 2012 (tranche 2 of the MySuper legislation) was introduced into Parliament. The Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2011 (tranche 1) was introduced on 3 November 2011. A third tranche is yet to be released for consultation.

Both Bills were referred to the Parliamentary Joint Committee on Corporations and Financial Services (PJC). The PJC released its report on 19 March 2012 recommending that the Bills be passed. This recommendation was subject to some clarification of the exception for tailored MySuper plans for large employers with at least 500 members and a provision allowing a grace period where membership fluctuates temporarily below that level. Dissenting committee members expressed objections “around the authorisation process, the licensing regime, a proposed “scale test” and the lack of clarity surrounding the provision of intra-fund advice”.

While the most comprehensive of the reforms surrounds the creation of the new default MySuper product for the superannuation industry, extensive reform initiatives are also being carried out in the “back-office” of the superannuation industry, with respect to trustee governance, and in the SMSF sector.

The Government has also granted the Australian Prudential Regulation Authority (APRA) a prudential standards-making power for the superannuation industry, which brings some much needed consistency to APRA’s powers, given APRA already has such a power within the banking and insurance industries. APRA has released a draft paper which provides an outline of APRA’s proposed prudential standards, which are expected to commence in 2013.

This paper provides a brief overview of the key legislative developments resulting from the Stronger Super reforms, which are:

- MySuper;
- SuperStream;
- SMSFs;
- Trustee governance; and

- APRA’s prudential standards-making power for the superannuation industry.

MySuper

A MySuper product is defined as a class of beneficial interest in a regulated superannuation fund where the registrable superannuation entity (RSE) licensee is authorised under the Superannuation Industry (Supervision) Act 1987 (Cth) (SIS Act) to offer that class of beneficial interest in the fund as a MySuper product.

A “choice product” is defined as a class of beneficial interest in a regulated superannuation fund that is not a MySuper product.

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 2013, and 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 their 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 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.

Mandatory characteristics of MySuper products

A RSE licensee can only offer a MySuper product if certain core criteria are met. These criteria must be set out in the governing rules of the fund to ensure that, for the MySuper product:

- there is a single diversified investment strategy in relation to those assets of the fund that are attributed to the MySuper product (a lifecycle investment strategy can be adopted but must be the same for all members and will be limited to varying the investments for members on the basis of age only);
- all members of the MySuper product in the fund are entitled to access the same options, benefits and facilities (including access to call centres, member education, intra-fund advice if offered, the capacity to make death benefit nominations, online account information or other MySuper services);
- the same process is adopted in crediting or debiting the accounts of MySuper members in a way that does not preference a subgroup of members (except for lifecycle investment strategies and to the extent that a different process is necessary to allow for fee subsidisation by employers);
- if fee subsidisation by employers is permitted, that subsidisation does not favour one member of the MySuper product in the fund over another;
- no limitations are imposed on the source or kind of contributions made by or on behalf of persons who are members of the MySuper product, other than those imposed by or under the general law or a law of the Commonwealth or of a State or Territory;
- a member's interest in a MySuper product cannot be transferred without the member's consent to another MySuper product within the fund or as required or permitted under a law of the Commonwealth; and
- the MySuper product is only for the pre-retirement phase.

Single, diversified investment strategy

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.

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

While trustees will not be required to apply to APRA to hold a specific MySuper licence, they will need to apply to APRA to be authorised for each MySuper product they wish to offer. An application for authority must be in the approved form, contain the information required by the form and be accompanied by an up-to-date copy of both the trust deed and the governing rules of the fund.

Time period for deciding applications

APRA has 60 days from receipt of the application to decide whether to grant the authority to offer a MySuper product, but APRA can extend the period by a further 60 days by providing written notice to the trustee. While APRA can only extend the period once, it can restart the 60-day period by requesting additional information from the RSE licensee. The decision-making period restarts once the RSE licensee has provided the requested information.

Authorisation process

Under the new proposed s 29T(1) SIS Act, APRA must authorise an RSE licensee to offer a MySuper product if, and only if:

- the RSE licensee's application is compliant;
- the fund is a RSE, has five or more members, and is not an eligible rollover fund;
- APRA is satisfied that the governing rules require that the product meets the core characteristics of a MySuper product;
- APRA is satisfied that the RSE licensee is likely to comply with the fee charging rules in relation to MySuper products; and
- APRA is satisfied that the RSE licensee is not likely to contravene the treatment of contribution obligations in the new proposed ss 29W or 29WA.

In addition, APRA will also need to be satisfied that the RSE licensee is likely to comply with the enhanced

trustee obligations for MySuper products, as set out in the Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012.

Fees

Under new fee charging rules the types of fees an RSE licensee can charge MySuper members will be limited to a class of six types of fees. These are:

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

The three charging rules under which fees can be charged by an RSE licensee for a MySuper product are:

- a flat fee to all members — each member pays the same fee for the product or service;
- a percentage fee to all members — each member is charged the same percentage of their account balance at a point in time for the service or product; or
- a flat fee plus a percentage fee to all members — each member of the MySuper product is charged the same flat fee and the same percentage of their account balance at a point in time for the service or product.

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.

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.

One MySuper product except in limited circumstances

A fund will be restricted to offering just one MySuper product unless it can satisfy one of two exceptions.

Material goodwill exception

Under the proposed new s 29TA of the SIS Act, an RSE licensee may offer more than one MySuper product per fund in order to preserve a corporate brand, following merger or takeover, where APRA is satisfied that:

- some or all of the persons whose benefits are to be transferred hold a class of interest in the original fund that is similar to the proposed MySuper product;
- there is material goodwill in that class of interest in the original fund, and that goodwill could not be maintained unless the RSE licensee were authorised to offer the proposed MySuper product as an additional MySuper product in the fund; and
- it would be in the best interests of all members of the fund to maintain the distinction between the proposed MySuper product and the existing MySuper product already authorised.

Large employer-sponsor exception

Under the proposed new s 29TB of the SIS Act, an RSE licensee may offer a tailored MySuper product to large employer-sponsors on behalf of their employees where:

- the particular employer-sponsor contributes payments to the fund on behalf of at least 500 members; and
- the governing rules of the fund provide that the only members that may hold an interest in the proposed MySuper product are either:
 - employees of the employer-sponsor, or an associate of that employer-sponsor; or
 - relatives or dependants of those employees.

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 APRA and, to improve transparency, will also need to be separately published by trustees.

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, or 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 that insurance monies 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 phase only

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 post-retirement offering at some time in the future and the framework that should apply.

Capital gains tax rollover for MySuper Reforms

The current capital gains tax (CGT) rollover relief ceased on 30 September 2011. The Government has consulted key stakeholders on CGT consequences that may directly arise from transitioning to MySuper and to what extent, if any, CGT rollover relief should be available.

Superstream

Efficient superannuation transactions and improved flow of super to member accounts

On 2 February 2012, the Government released draft legislation to implement the use of new data and payment standards for superannuation transactions. The

proposals include amendments to the Income Tax Assessment Act 1997 and the Taxation Administration Act 1953 to establish a new administration penalty regime to deal with contraventions of the standards by employers or trustees.

The draft legislation (the Superannuation Legislation Amendment (Stronger Super and Other Measures) Bill (No 2) 2012) provides that the Commissioner for Taxation may determine, by way of legislative instrument, payment standards for trustees and for employers. The Commissioner must consult with APRA in setting the standards.

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, all contributions and rollovers will be required to be made via an electronic system based on the Bulk Electronic Clearing System (BECS), the payment standard prescribed by the Australian Payments Clearing Association. Alternative payment systems (such as BPAY) will also be approved depending on their merits and business coverage within Australia.

The data standards and the use of e-commerce will be mandatory for APRA-regulated superannuation funds and SMSFs for processing rollovers and accepting contributions from 1 July 2013. Data standards and the use of e-commerce will be mandatory for large and medium employers making contributions from 1 July 2014, and for small employers from 1 July 2015.

Consolidation and lost super

Part of the Government's efforts to bring efficiency to the administration of superannuation is the consolidation of multiple super accounts and those super accounts which are lost.

From 1 January 2012, funds have been able to use TFNs to search the ATO's current service for lost super accounts with member consent; and from July 2012, where a member has multiple accounts within a fund, the fund trustee will be required to consolidate these accounts where possible. Consultation on the draft legislation closed on 13 April.

No TFN Contributions

From 1 July 2013, where superannuation contributions for an employee are not accompanied by a TFN, the employer will be required to forward the contributions to a fund, and if the fund is unable to obtain a TFN and other identifying details within a specific time frame, the money will be sent to the ATO as part of the unclaimed moneys process.

Regular information to employees on employer contributions

From 1 July 2012, employers will be required to report regularly to their employees, payments they have made or will make. If the employer is required to give a payslip to their employee and the employer can make a contribution to a regulated superannuation fund or a retirement savings account, and that contribution relates to the salary or wages on the payslip, then the employer must ensure that the information prescribed in regulations is included on the payslip. The requirement to do so will be a civil remedy provision under the Fair Work Act 2009 (Cth).

The prescribed information will include reporting of actual contributions paid as well as the date on which those contributions were (or will be) paid, rather than just reporting the entitlement to contributions.

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.

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.

Superannuation roundtable

The Government’s Superannuation Roundtable, chaired by Bill Shorten MP, held its first meeting on 23 February. The discussion focused on the administration of concessional contributions caps for individuals over 50 with a fund balance of less than \$500,000.

The Roundtable will also consider proposals to expand options in the draw-down phase, such as annuities and deferred annuities, as well as savings offsets.

Self-managed superannuation funds***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 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 beneficiaries when that duty conflicts with other duties and interests and to ensure that duties to beneficiaries are met and their interests are not adversely affected despite the conflict;
- strengthening the requirements for individual directors;
- 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 superannuation trustee;
- 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; and
- expanded trustee duties to MySuper members.

Time to lodge TPD claims with the Superannuation Complaints Tribunal

The time limit for members to lodge a total and permanent disability claim with the Superannuation Complaints Tribunal (SCT) 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.

Code of Governance and APRA’s prudential standards making power

The Government supports a voluntary code of governance developed by industry in consultation with APRA, rather than a mandatory code co-ordinated by APRA. The Government has also confirmed it supports granting APRA the power to make prudential standards in superannuation.

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 directors of corporate trustees be required to include in their deliberations the impact of their decisions on the environment, the community and the fund's reputation. The Government will ask APRA to consider whether this issue should be addressed through relevant guidance material.

APRA prudential standards-making power

Following the Government's decision to grant APRA a prudential standards-making power for the superannuation industry, APRA released a discussion paper outlining its proposals for prudential standards in superannuation. APRA expects to finalise the prudential standards during 2012 for commencement in 2013.

The new prudential standards-making power will reside in the SIS Act and will provide APRA with similar powers in relation to superannuation to those it has under the Banking Act 1959 (Cth), the Insurance Act 1973 (Cth) and the Life Insurance Act 1995 (Cth).

The discussion paper outlines 12 areas on which prudential standards will be made. Six of these will be standards common to those which currently exist in the banking and insurance sectors and will be extended to cover superannuation, with minor necessary amendments. These are:

- SPS 510 Governance;
- SPS 520 Fit and Proper;
- SPS 231 Outsourcing;
- SPS 232 Business Continuity Management;
- SPS 220 Risk management; and
- SPS 310 Audit related matters.

The remaining six prudential standards are new and will focus on areas specifically relevant to superannuation. These are:

- SPS 530 Investment governance;
- SPS 521 Conflicts of interest;
- SPS 160 Defined Benefit Funding and Solvency;
- SPS 114 Operational Risk Financial Requirement;
- SPS 250 Insurance in Superannuation; and
- SPS 410 Transition to MySuper.

APRA prudential practice guides

APRA issued two Prudential Practice Guides on 4 April 2012. Prudential Practice Guide SPG 270 addresses

contribution and benefit accrual standards for RSE's and Prudential Practice Guide SPG 280 addresses payment standards for regulated superannuation funds and approved deposit funds.

These reflect legislative changes introduced since the existing guidance was issued as Superannuation Circulars in 2006, but do not introduce any new requirements.

Other minor legislative reforms

In order to ensure the *Stronger Super* reforms operate optimally, it is necessary for small changes to be made in areas other than the big-ticket reform items. Some of the recent legislative changes are below.

Superannuation Legislation Amendment (Early Release of Superannuation) Act 2011 (Cth)

This Act facilitated the transfer of the administration of the early release of superannuation on compassionate grounds from APRA to the Chief Executive Medicare. Since 3 February 2011, Medicare Australia had carried out the day-to-day functions in relation to the administration of early release of superannuation in APRA-regulated superannuation funds by way of a service delivery agreement. The provisions of the Act took effect from 1 November 2011.

Tax Laws Amendment (2011 Measures No 2) Act 2011 (Cth)

This Act, which was passed on 28 June 2011, allowed trustees of superannuation funds, and retirement savings account (RSA) providers, to use TFNs to locate amounts held on behalf of the RSA or member. From 1 July 2011, superannuation fund trustees and RSA providers have been able to use the TFNs of members as a primary locator to locate lost member accounts and contributions. From 1 January 2012, TFNs may be used to consolidate accounts both within funds, and between different funds.

The passage of this Act was instrumental in the Government's SuperStream reforms to clean up the back-office of the superannuation.

Amendments to the Corporations Regulations 2012 (Cth)

On 12 March consultation closed in respect of the Government's proposed legislative amendments that will bring limited recourse borrowing arrangements (LRBAs) within the definition of "financial products" for the purposes of Ch 7 of the Corporations Act 2001 (Cth) when such arrangements are entered into by regulated superannuation funds under ss 67A and 67B of the SIS Act. This would require persons dealing in these arrangements to hold an AFSL, although an existing AFSL covering derivatives will suffice for authorisation purposes.

Superannuation Industry (Supervision) Amendment Regulations 2012 (No 1) (Cth)

The Superannuation Industry (Supervision) Regulations 1994 (the SIS Regulations) were amended on 3 February 2012 to give effect to the Government's announcement to extend the current draw-down relief for account based, allocated and market limited pensions. The minimum payment amounts for 2012–2013 are the same as for 2011–2012, and similar changes were made in respect of pensions and annuities paid from RSAs.

MyEFO reforms

On 29 November 2011, the Government released its mid-year economic and fiscal outlook, which announced that GDP growth expectations were weaker than at Budget, and that the revised economic outlook has reduced tax receipts by more than \$20 billion over the forward estimates. In response, the Treasurer announced a number of budgetary measures concerning superannuation.

Concessional contributions cap — one-year pause in indexation

The Government will pause the indexation of the superannuation general concessional contributions cap for one year in 2013–14, so that it remains at \$25,000. Indexation of the cap will be deferred until 2014–15, when the cap is expected to rise to \$30,000.

The pause in indexation of the general concessional contributions cap will also result in a pause in the indexation of the concessional contributions cap for individuals aged 50 and over, and the non-concessional contributions cap.

Reduction in the minimum payment for account-based pensions in 2012–13

The Government will extend pension draw-down relief for a further year by reducing the minimum payment amounts for account-based, allocated and market linked (term allocated) pensions by 25% for 2012–13.

The Government previously provided pension draw-down relief in 2008–09, 2009–10 and 2010–11 by halving the minimum payment amounts, and in 2011–12 by reducing the minimum payment amounts by 25%. While the Government indicated that the minimum payment amounts would return to normal in 2012–13, equity markets continue to be volatile and extending drawdown relief for a further year will assist retirees to recoup capital losses as equity markets recover over time.

Reduction to the matching rate for co-contributions

From 1 July 2012, the matching rate for co-contribution will be reduced to 50%, with a maximum co-contribution of \$500 for people with incomes up to \$31,920 in 2012–13 (with the amount available phasing down for incomes up to \$46,920).

This is a reduction from the current matching rate of 100%, with a maximum co-contribution of \$1000 for people with incomes up to \$31,920 (phasing out at \$61,920).

Restricting the operation of certain superannuation trust deed clauses

The Government will ensure that certain trust deed clauses cannot be used to avoid what would otherwise be excess contributions from being counted against the caps.

Some funds include a clause in their trust deeds which is designed to treat amounts that would otherwise have been considered contributions to the fund as not having been accepted by the fund if those contributions would lead to a breach of the contributions caps.

Under this measure, the fund will be deemed to have accepted such contributions, notwithstanding the trust deed clause, if the contributions have not been returned promptly and have in effect been intermingled with assets of the fund.

Conclusion

The reforms to the superannuation industry will have a considerable effect on the current landscape. Even though the Government is using a staggered implementation, members of the industry should not delay in preparing themselves for the commencement of these far-reaching reforms.



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