



CHARTERED ACCOUNTANTS
AUSTRALIA • NEW ZEALAND

20 July 2015

Manager
Insurance and Superannuation Unit
Financial System and Services Division
The Treasury
Langton Crescent
PARKES ACT 2600

By e-mail: superannuationgovernance@treasury.gov.au

Dear Sir

Submission - Reforms to Superannuation Governance

Chartered Accountants Australia and New Zealand welcomes the opportunity to respond to your invitation for a submission on the Reforms to Superannuation Governance

We are made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over. Our members are known for professional integrity, principled judgment and financial discipline, and a forward-looking approach to business. We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are represented on the Board of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance, and Chartered Accountants Worldwide, which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

Should you require any further information or wish to discuss the contents of this submission, please contact Liz Westover, Head of Superannuation on 02 9290 5704 or by email at liz.westover@charteredaccountantsanz.com

Yours sincerely,

Liz Westover FCA
Head of Superannuation

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Overview of proposed legislative changes

Chartered Accountants Australia and New Zealand are broadly supportive of the measures by the Federal Government to enhance the governance of superannuation trustee boards. We have long been supporters for a move away from the equal representation model for trustee boards to one that delivers a trustee board with a talent pool of professionals. To this end, we believe the inclusion of independent trustees on these boards will better service the needs of Australians saving for their retirement through superannuation.

The equal representation model may have been useful in prior years, however we do not believe that it remains the best model for the superannuation industry into the future.

Whilst we are in overall support of the objectives of increasing independent representation on super trustee boards, we have concerns about aspects of the proposed legislation and indications from APRA as to their role through prudential standards. Accordingly, specific comments are contained below.

With the current proposals under consideration, we take this opportunity to make the following observations:

- ALL trustees, whether they meet a definition of ‘independent’ or not must act in the best interests of members. This is a requirement under superannuation law and under trust law they have a fiduciary duty to act in the interests of the beneficiaries of the fund (the members)
- ALL trustees should be independent in mind in order to act in the member’s best interests and not be influenced by their appointer, employer, union or others.
- The behaviours of the board to ensure member’s interests are protected must be the responsibility of the entire board and should not be exclusive to individual members that are deemed to be independent.
- There may be a need to apply a better lens to all board directors, not simply the independent trustees

Definition of Independent

Fundamentally, Chartered Accountants ANZ are concerned about the proposed definition of independent for a number of reasons. We believe the current proposals are not aligned with why independence is needed. That is, if you need people who can act purely in the interests of members, as required by both superannuation and trust law, then shouldn’t independence be defined as dealing with any conflicts of interest that might impair that person’s ability to make an objective assessment?

We believe the draft legislation

- 1) does not appropriately or adequately define an independent trustee. Legislation, as proposed still allows for substantial relationships to exist that any reasonable person would deem not to be independent
- 2) has passed too much responsibility to APRA by delegating the determination of ‘material relationship’ within the narrow scope (independent of RSE licensee only) contained in the legislation
- 3) APRA has not provided enough certainty regarding their interpretations of ‘independent’ and ‘material relationship’

Chartered Accountants ANZ are concerned that the proposed definition of independent trustee does not adequately cover the range of conflicts that may exist for a potential trustee such they would truly be viewed as an independent in the eyes of fund members or the public at large. We believe that the draft legislation is too narrow in its scope for independence by only referring to material relationships with the RSE licensee.

Under these proposals, the current definition of ‘independent trustee’ contained in Superannuation Industry (Supervision) Act is to be repealed. The replacement definition appears to focus only on the relationship the trustee may have with the RSE licensee and does not address or cover other significant relationships that would give rise to a conflict of interest. We note that some of these specific scenarios are currently seen as a breach of independence. This appears to be a critical change in the way independence is defined, with the new proposals clearly omitting previous breaches of independence, eg a representative of a trade union.

Independence cannot be approached using a tick the box mentality. Independence can be actual or perceived but importantly is a state of mind of the individual person. We are concerned that the current proposals are too narrow in their approach and allows too many gaps for people to be appointed to a board as independent when they are not. We do not believe that the relationship with the RSE licensee is the only one for which independence needs to be ensured.

In previous submissions, we have spoken of the concept of independent being a subjective matter and cannot be dealt with using a tick the box approach. It becomes too easy and open to abuse where people believe that as long as they can tick the box on a range of issues that might indicate independence then they no longer have to consider whether they actually are.

The accounting profession has dealt with the notion of independence with a principles based approach. APES 110 issued by the Accounting Professional and Ethical Standards Board is the Code of Ethics for Professional Accountants and extensively deals with actual and perceived independence for auditors.

Where threats to independence can be identified, appropriate safeguards must be put in place to mitigate those risks to an acceptable level. If those risks cannot be reduced to an acceptable level, then the auditor, would need to remove themselves from, or not accept an engagement. Importantly, consideration is given to not only actual independence but any perception of lack of independence.

Current auditing standards refer to the requirement for auditors to adhere to a code of ethics, specifically referencing APES 110 and have the force of law behind them.

We note that as a result of the Stronger Super reforms requiring registration of self-managed super fund auditors, APES 110 became hard coded in legislation (SISA) for all SMSF auditors (regardless of any previous professional requirements to adhere to the standard). This decision was made after determining that a ‘tick the box’ option of mandatory outsourcing of SMSF audit activity would not adequately resolve perceived conflicts of interest and therefore not ensure SMSF auditor independence.

The important issue for our profession is that in determining independence, an auditor would be required to cast a wide net and consider a wide range of factors including personal, professional and associative relationships as well as any other relevant factors that may impact on their ability to conduct an audit and form an unbiased, independent opinion, free from conflicts of interest. This includes addressing circumstances that others may perceive as a breach of independence.

Clearly there will be circumstances in which no appropriate safeguards can be put in place and guidance from the professional accounting bodies and the regulators is provided to auditors to identify these as well as work through risks and appropriate safeguards.

We believe that legislation for independence for super trustee boards must cast a wider net and ensure potential trustees consider a far greater range of factors other than what is currently proposed in this legislation or suggested by APRA.

We would encourage guidelines for superannuation boards regarding specific breaches of independence or inclusion of these circumstances in legislation. We note that current identification of these specific relationships are proposed to be removed from SISA. Guidance can then be provided on ‘grey’ areas, helping to identify the risks, how to safeguard against them and what to do if they cannot be reduced or eliminated.

We are also concerned that the determination of material relationship has effectively been passed to APRA. To date, they have only indicated what they are ‘likely’ to include to be a material relationship. In light of the uncertainty that this brings, it is difficult to support this new definition of independent.



The current definition of independent trustee contained in legislation is too narrow, fails to address concepts of independence and defers too much responsibility to APRA.

APRA have not provided enough certainty as to how they will interpret ‘independent’ and ‘material relationship’.

Appointment of independent directors

In the absence of any real legislative requirements for appointment of independent directors, Chartered Accountants ANZ does not believe enough detail exists as to how APRA intends to deal with this issue. Notwithstanding their apparent intention to expand requirements currently outlined in SPS 510 to include processes for nomination for board positions and the framework used to assess the suitability of these candidates for appointment, we remain concerned that there is insufficient detail on which we can be confident that the objectives currently being sought will be achieved.

Chartered Accountants ANZ believe all trustee boards should establish a nominations committee. This committee would be responsible for making recommendations to the Board regarding the desired skill sets for the Board, gaps that may exist as well as developing processes for the appointment of directors. Processes for performance evaluation of individual trustees and the means by which underperforming members will be dealt with could also be included.

Importantly, boards and nominations committees must be transparent about their processes and be held accountable for adherence to agreed processes.



Greater clarity on intended processes for appointment of independent directors is needed.

Chartered Accountants ANZ believe boards should have nominations committees that are accountable for policies and ensuring those policies are adhered to.

APRA prudential standards – regular assessment of independence

We note that APRA has indicated they will be looking to require each RSE licensee board to undertake regular assessments of the independence of each director as per the Government’s proposals to require 1/3 independent trustees on an ongoing basis.

APRA has not been definitive in what they believe to be ‘regular’. Again, it is difficult to form a view on the proposed measures when lack of clarity is absent at this stage.

Fundamentally however, we believe this requirement may be problematic in light of proposed definitions in that as soon as a trustee is appointed, they will then take on a material relationship with the RSE licensee and therefore immediately fail the independence test.




Chartered Accountants ANZ believe that the proposed definition of an independent trustee will result in the failure of trustees to be independent on an ongoing basis as the appointment to a board in the first instance will mean a material relationship exists with the RSE licensee which then fails the definition.

APRA prudential standards – sub-committees

Under updates on these proposed measures released, APRA have indicated they will be requiring the majority of audit and remuneration sub-committees to be made up of independents. We note that this could place a significant burden on those trustees belonging to smaller boards. That is, circumstances will arise in which the independents will have no choice but to sit on these sub-committees. This may prove problematic when considering the skill sets required on a board that may need to be sought for incoming independent trustees. There is a risk that potential independent trustees may need to have relevant skills for these sub-committees rather than being assessed against the overall skill requirements for the board. Larger boards with greater numbers of independents will have more flexibility. We note that we do not believe that it is practical for many trustee boards to increase the number of independents for a variety of reasons, including costs associated with doing so.

We also note that the time commitment for independent trustees may be in excess of that required for other trustees. This may result in super trustee boards becoming unattractive compared to directorships of other entities, particularly as the remuneration levels for super boards is far below that which is frequently paid to directors of corporate entities.

Consideration to having at least one independent on sub-committees for smaller boards and a majority for larger boards may be needed.

	Requirements by APRA for the composition of certain sub-committees to contain a majority of independents may be problematic for small boards. This may impact on costs of fund, skills of funds and the burden on independent trustees.
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Independent Chair

Chartered Accountants ANZ remains supportive of the move to independent chairs for super trustee boards. We believe this will enhance the overall success of these measures and assist in addressing potential issues of the independent trustees being in the one third minority.

Tenure

The issue of tenure has not been addressed in the proposed legislation. Chartered Accountants ANZ is supportive of limited tenure for trustees and suggest a maximum period of five years. We believe that a period of less than five years may be counter-productive to a goal of best talent trustee boards and undermine the benefits from continuity of board membership.

We do however believe that the Board may need some flexibility around periods of tenure to ensure continuity, consistency and experience is maintained on the Board at any given time. A five year tenure period could be accompanied by a two year extension where the Board believes that the members' best interests would be best served by an extended period. This may be because no appropriate replacement is available or the skills of that board member are critical to a current project or period of the board or fund.

	The issue of tenure needs to be addressed. Chartered Accountants ANZ believe boards should be appointed for a five year term with flexibility to extend a further two years where required.
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Remuneration

Traditionally, remuneration for super fund trustees has been low compared to directors for other entities. On average, remuneration for trustees has been less than \$50,000 per annum. Frequently, trustees, particularly those acting for corporate super funds receive little or no remuneration. We are aware that corporate funds can pay no remuneration to their trustees and where they may pay an independent trustee, the cost of remuneration is borne by the corporate, not the fund.

Chartered Accountants ANZ are concerned new requirements for independent trustees for some types of funds will see significant changes to the total costs of remuneration for these boards, adding to the overall costs of running the fund. It is highly likely that independent trustees will require some form of remuneration and corporates will be reluctant to absorb these additional costs. This is particularly relevant in the context of constant pressure on funds to reduce the overall costs of operating the funds which are ultimately borne by the members of the fund.


We note also that the relatively low remuneration averages for the super industry will mean that remuneration levels will need to increase across the board, simply to be able to attract new independent trustees with the requisite skills sets to the super industry.

Corporate Super Funds

We would encourage further consideration as to whether the current proposals for independent trustee requirements are warranted for all types of funds, particularly non-public offer funds. As discussed above, remuneration amounts and payments are different for corporate funds and the impost of the current requirements could be significant, which will ultimately impact on fund members.


Defined Benefit Funds

Chartered Accountants ANZ is also concerned that the current proposals for independent trustees may not be suitable for defined benefit (DB) funds or partly DB funds. Significantly, risks associated with DB funds are fundamentally borne by the employer sponsors of those funds, rather than the members. We question whether the same requirements for independent trustees are appropriate for these types of funds as with other APRA regulated funds where the risks are borne by the members of the fund who look to the trustees of the fund to act in their best interests in looking after their savings.

	<p>The relevance and appropriateness of the current proposals for some types of super funds may need to be re-considered.</p> <p>The impost on corporate super funds and DB funds may result in increased costs and counter productive outcomes.</p>
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Transitional arrangements

Chartered Accountants ANZ believe that the three year transitional period will provide adequate time for superannuation fund boards to make arrangements to comply with the law including changes to their governance rules, transition existing trustees and source and appoint new trustees.

	<p>Chartered Accountants ANZ are supportive of the time frames for super funds to transition to the new requirements.</p>
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