SUPERANNUATION LEGISLATION AMENDMENT (TRUSTEE GOVERNANCE) BILL 2015 AND ASSOCIATED REGULATION: GOVERNANCE ARRANGEMENTS FOR REGISTRABLE SUPERANNUATION ENTITIES

SUMMARY OF CONSULTATION PROCESS

In June 2015, the Government released exposure draft legislation proposing changes to the governance arrangements for all Australian Prudential Regulation Authority (APRA) regulated superannuation funds. The amendments in the exposure draft legislation proposed that:

- all APRA regulated superannuation funds be required to have a minimum of one-third independent directors on their trustee board, and an independent chair;
- the definition of "independent" is to include persons who do not have a substantial holding in the trustee or do not have (or have not had within the last three years) a material relationship with the trustee, including through their employer;
- trustees of funds that do not have a majority of independent directors be required to report on an "if not, why not basis"; and
- a three year transition period to apply for existing funds.

The exposure draft legislation took into account feedback received on the governance reforms in response to the *Better regulation and governance, enhanced transparency and improved competition in superannuation* discussion paper the Government released in November 2013, and in relation to the Final Report of the Financial System Inquiry.

Consultation process

Consultation on the exposure draft legislation was conducted between 26 June and 23 July 2015.

A total of thirty one submissions were received, three of which were confidential.

Targeted consultation was also conducted with stakeholders during August 2015 to respond to some more technical changes in the draft legislation.

Summary of key issues

Implementation through legislation rather than APRA prudential standards

The majority of stakeholders said that the exposure draft legislation could be improved by putting more detail in the legislation and leaving less to APRA's prudential standards in order to provide stakeholders with greater clarity about their legal obligations, without changing the policy intent.

Repeal of equal representation and the two-thirds voting rule

Most industry funds and their representative associations opposed the proposed repeal of equal representation from the *Superannuation Industry (Supervision) Act 1993*, although other

stakeholders recognised that the legislation still provides flexibility for equal representation to continue in a modified form (with the remaining two-thirds of board directors able to be split evenly between member and employer representatives).

Abolition of policy committees

Some stakeholders said abolishing policy committees was a retrograde step when they serve a valuable accountability purpose. Other stakeholders questioned the value of policy committees and supported their abolition noting that how funds choose to engage with members should be up to trustees to decide.

Requirement of an independent chair

Some stakeholders supported the requirement for trustee boards to appoint an independent chair on the basis that this is consistent with contemporary governance standards and with requirements of other prudentially regulated entities including banks and insurance companies. Other stakeholders argued strongly that the skills and attributes of the Chair should be a decision for the board. One of the major issues raised was that forcing the board to appoint a Chair from the one-third independent directors would severely limit the available choice.

Requirement of 'if not, why not' reporting

Some stakeholders supported the requirement for 'if not, why not reporting'. Others considered that the disclosure obligation to report on a majority of independent directors is inconsistent with the legislative obligation for one-third board composition requirement and that they should not be required to report on a measure that is not a legal obligation. In addition, stakeholders have suggested that this provision adds to red-tape and has the potential to increase uncertainty and create member confusion.

Three year transition period

Most stakeholders supported the introduction of a three-year transition period. However, some stakeholders said the transition period should commence no earlier than 1 July 2016.

Treatment of corporate funds

There is a concern that new requirements for independent trustees for some types of funds might result in significant changes to the total costs of remuneration for these boards, adding to the overall costs.

Application to pooled superannuation trusts

Some stakeholders have questioned whether trustees of pooled superannuation trusts will be captured by the reforms.

Application to exempt public sector superannuation schemes

There are some state public sector superannuation schemes that choose not to be regulated by APRA and as such, the proposed governance changes will not automatically apply to them.

APRA consent to adverse alteration of a beneficiary's right

Stakeholders suggested that rather than deleting Superannuation Industry (Supervision) Regulations 13.16(2)(a)(ii) and (5), the regulations should be modified so as to retain the power for any trustee to ask APRA to consent to an adverse alteration to a beneficiary's right or claim to accrued benefits (that do not relate to prescribed minimum benefits of members).

APRA's power to determine independence

Stakeholders suggested amending the Bill to either remove APRA's power to determine independence or at least narrow the scope of the proposed new APRA powers.

Technical matters

There were some technical drafting suggestions to clarify the policy intent and to ensure the legislation did not result in unintended consequences.

Refinements to legislation

Following consultation with industry the Government amended the legislation to:

- contain more detail, including a revised definition of independent in the law. The term 'substantial shareholding' was also amended so it applies to profit generating shares only, and not to nominal value shares;
- have both the transition period and commencement of the new requirements from Royal Assent;
- insert a regulation making power that will specify circumstances that would result in a person being either independent or not independent;
- retain the power for any trustee to ask APRA to consent to an adverse alteration to a beneficiary's right or claim to accrued benefits;
- clarify APRA's role in determining independence; and
- adopt technical drafting suggestions to clarify the policy intent and to ensure that the legislation does not result in unintended consequences. These include:
  - clarifying that the:
    - independent Chair is not in addition to the one-third independent directors; and
    - the proposed APRA appointment and removal prudential standard will set out requirements relating to how independent directors are appointed/removed but will not affect whether a director is in fact independent or not.
  - ensure that s95 (now 93B) covers both governing rules and the constitution of the corporate trustee. The Bill has also been amended so that an equivalent provision applies to RSE licensees during transition; and

- ensure that the period for filling a vacancy in the membership of individual trustees or the board of a corporate trustee is 120 days and not 90 days, with APRA discretion for a longer period.

The Government has clarified in the Explanatory Memorandum that boards not be required to have an independent Chair until the end of the transition period to allow time for new independent directors to become sufficiently experienced before potentially having to take on the role of Chair.

The Government will also write to the States and Territories to highlight the significant changes to the legislation and to encourage them to amend their superannuation schemes to reflect these legislative amendments.

Thank you to all participants in the consultation process.