

## GOVERNMENT RESPONSE TO SWG RECOMMENDATIONS

Recommendations	Government Response
<p><b>Universal licensing regime</b></p> <p><b>Australian Prudential Regulation Authority (APRA) licence</b></p> <p><b>Recommendation 1</b></p> <p>The Superannuation Working Group (SWG) recommends that trustees of superannuation entities (other than self managed superannuation funds (SMSFs) or exempt public sector superannuation schemes (EPSSSs)) be licensed by APRA. To obtain such a licence, a trustee should be required to:</p> <ul style="list-style-type: none"> <li>• comply with conditions on a licence, with other legislative requirements and with the covenants in the trust deed;</li> <li>• have adequate resources in place (financial, technological and human resources);</li> <li>• meet minimum standards of competency;</li> <li>• have adequate risk management systems in place, including a risk management plan and adequate arrangements for ensuring compliance with the plan;</li> <li>• have adequate levels of professional indemnity insurance and material damage/consequential loss insurance in place;</li> <li>• have adequate outsourcing arrangements in place; and</li> <li>• meet any other conditions as prescribed in regulations or as required by APRA.</li> </ul> <p>Licensees would also need to meet these</p>	<p>The Government supports this recommendation.</p> <p>The Government considers that all superannuation trustees should have a licence to operate as a superannuation trustee. This would ensure that all superannuation trustees are competent and have adequate systems to look after the interests of superannuation fund members. A universal licence would be consistent with arrangements in place in the managed investments regime.</p> <p>The <i>Superannuation Industry (Supervision) Act 1993</i> (SIS Act) will be amended at the earliest opportunity to require all superannuation fund trustees to obtain a superannuation trustee licence (STL) to operate a superannuation fund. Trustees must also meet licence conditions on an ongoing basis. These conditions will include requirements for trustees to meet minimum standards of competency, have adequate resources, a risk management plan and adequate risk management systems (including a fraud control plan), systems to manage outsourcing, as well as any other conditions that APRA considers appropriate to operate the proposed business.</p> <p>Either the trustee corporation or a ‘notional entity’ of individual trustees would be licensed. Trustees would also be able to ‘buy-in’ expertise to demonstrate competence and other licence conditions.</p> <p>To ensure compliance with the new licensing framework, APRA would have appropriate powers, including to issue directions, disqualify trustees, vary conditions and</p>

<p>licence criteria on an on-going basis.</p> <p>The SWG recommends that the Government consider enforcement powers to enable APRA to suspend or remove a trustee or to revoke its licence where the trustee breaches the conditions of its licence or where an existing trustee fails to obtain a licence from APRA.</p>	<p>suspend or revoke the licence, subject to appropriate safeguards and review processes.</p> <p>The new regime would commence on 1 October 2003, with a two year transition for existing trustees to meet the new requirements.</p> <p>The Government and APRA will consult further with industry and other key stakeholders to develop the detail of the licensing regime.</p>
<p><b>Recommendation 2</b></p> <p>The SWG recommends that the licence apply to either the trustee corporation as a whole, or where the trustee is comprised of individuals and no corporate trustee structure exists, to a 'notional entity' comprising those individuals. The SWG further recommends that the Government consider mechanisms to ensure that trustees as a whole are able to show the capacity to meet the licence criteria, such as enabling the trustees to 'buy in' the expertise to demonstrate the competence to operate the fund, or through the application of 'key person' licensing conditions.</p>	<p>The Government supports this recommendation.</p> <p>See response to recommendation 1.</p>
<p><b>Recommendation 3</b></p> <p>The SWG recommends that licensed trustees be required to register all funds they operate with APRA prior to commencement. As a component of this registration process, trustees would be required to lodge the trust deed and a risk management plan, and certification that the trust deed and risk management plan comply with relevant requirements.</p>	<p>The Government supports this recommendation.</p> <p>The SIS Act will be amended to require all superannuation funds to be registered with APRA prior to accepting contributions. Requiring all funds to be registered prior to accepting contributions is consistent with the managed investments regime, and ensures that all superannuation funds have met regulatory requirements prior to accepting contributions. To be registered, the fund will be required to have a trustee with an STL to operate that type of fund, and lodge the trust deed and the risk management plan for the fund, both of which would be certified to comply with relevant requirements.</p> <p>The new regime will commence on</p>

	<p>1 October 2003 with a two year transition period for existing funds.</p> <p>The Government and APRA will consult further with industry and other key stakeholders to develop the detail of the new regime.</p>
<p><b>Recommendation 4</b></p> <p>The SWG recommends that existing trustees be given up to two years from the date of commencement of legislative amendments to apply to APRA for a licence and to register existing funds. New trustees would be required to be licensed from the date of commencement of the licensing regime. Consideration will need to be given to how the licensing process can be smoothed administratively during the transitional period to ensure that all applications are not received at the end of the two years.</p>	<p>The Government supports this recommendation.</p> <p>The Government recognises that a transition period is necessary for existing trustees to adapt to the new requirements.</p> <p>It is proposed that the new regime would come into effect on 1 October 2003, with a two year transition for existing trustees to obtain an STL and register all funds under their trusteeship. A two year transition is consistent with arrangements for an Australian Financial Services Licence (AFSL).</p> <p>After 1 October 2003, all new superannuation trustees and superannuation funds would need to comply with the new framework.</p> <p>The implementation detail will be worked out further in consultation with key stakeholders.</p>
<p><b>Australian Securities and Investment Commission (ASIC) licence</b></p> <p><b>Recommendation 5</b></p> <p>The SWG recommends that the requirement for an APRA licence be in addition to the <i>Financial Services Reform Act 2001</i> (FSRA) requirements to have an Australian Financial Services Licence (AFSL) to advise or to deal in interests of the fund. However, a trustee should not be required to gain an ASIC licence to operate the fund.</p>	<p>The Government supports this recommendation.</p> <p>The proposed prudential licence and AFSL are directed at different regulatory aims – the AFSL at consumer protection objectives and the STL at prudential ones. Accordingly, the Government considers that holding an STL should not obviate the need to fulfil consumer protection requirements, including licensing by ASIC.</p> <p>To minimise unnecessary duplication the</p>

	<p>Government will encourage APRA and ASIC to have due regard to each others' assessments in considering licence applications. The Government will also examine the possibility of a single entry-point licensing mechanism (see recommendation 7).</p>
<p><b>Recommendation 6</b></p> <p>The SWG recommends that the Government review the exemption from the AFSL requirements for dealing by trustees of non-public offer superannuation funds.</p>	<p>The Government supports this recommendation.</p> <p>The Treasury will review the relevant provisions, having regard to potential consumer benefits and associated compliance costs.</p>
<p><b>Single entry point</b></p> <p><b>Recommendation 7</b></p> <p>The SWG recommends that the Government consider streamlining arrangements for trustees required to hold both an APRA licence and an AFSL, through the development of a single entry point, so that the trustee need only lodge one application with APRA to cover both licences. The single entry point would only apply to applications for an APRA licence and AFSL submitted after commencement of the APRA licensing requirements. The application would need to contain sufficient information to meet the requirements for each licence. In considering this recommendation, the SWG suggests that the Government examine:</p> <ul style="list-style-type: none"> <li>• the matters which ASIC should consider when licensing an entity which has been or is to be licensed by APRA;</li> <li>• the extent to which the regulators should be required to consult with each other in taking licensing action; and</li> <li>• the memoranda of understanding</li> </ul>	<p>The Government supports this recommendation in-principle but considers that more work needs to be done to implement it.</p> <p>The Government supports measures to reduce unnecessary overlap and duplication. In developing the detail of the licensing regime, the Government expects both APRA and ASIC to work together to do this.</p> <p>Consideration of a single entry point will need to take account of the systems and costs issues, and the implications for the transitional arrangements under the FSRA.</p> <p>The Government notes that there is a demarcation between consumer protection and prudential issues and this issue would need to be managed. The Financial System Inquiry recommended a 'twin peaks' model for the regulation of consumer protection matters and prudential issues, and the Government has, and continues to, support this separation.</p>

<p>which establish information-sharing arrangements between APRA and ASIC.</p>	
<p><b>Implementation issues</b></p> <p><b>Recommendation 8</b></p> <p>The SWG recommends that the Government consider:</p> <ul style="list-style-type: none"> <li>• the current threshold for SMSFs to determine whether it is an appropriate test for determining which funds require prudential regulation; and</li> <li>• whether the existing successor fund provisions contained in the SIS Act are appropriate to deal with any restructuring which may occur as a result of the new licensing requirements.</li> </ul>	<p>The Government does not support examining the current member threshold for SMSFs.</p> <p>Changing the member threshold for SMSFs would result in transferring a small number of funds to the Australian Taxation Office's (ATO's) supervision. This merely shifts supervision from one regulator to another, without solving the underlying concerns as to the safety of these funds. The Government does not believe there is a convincing case for changing the SMSF definition. The Government believes that individuals who wish to be involved in a self managed fund have sufficient scope to do so under current arrangements and that the current membership limit is necessary to ensure that these funds do remain truly 'self managed' in that they are of a size that allows all member trustees to be actively involved in the management of the fund.</p> <p>The Government has asked Treasury to examine the current successor fund provisions to ensure that they are appropriate to deal with any restructuring which may occur as a result of the new licensing requirements.</p>
<p><b>Risk management plans</b></p> <p><b>Recommendation 9</b></p> <p>The SWG recommends that superannuation trustees be required, as a condition of their APRA licence, to prepare and maintain a risk management plan (RMP) in respect of each fund that they operate. The plan would need to be submitted as a part of the fund registration process. Trustees would be required to demonstrate in the RMP how they intend to deal with specific risk areas</p>	<p>The Government supports this recommendation.</p> <p>The introduction of risk management plans would strengthen monitoring by trustees and help ensure that risks are adequately identified, considered and addressed.</p> <p>The Government proposes amending the SIS</p>

<p>relevant to superannuation funds, including particular provisions in the SIS Act. The Government should consult with relevant stakeholders on the risk areas that would need to be addressed in the RMP.</p>	<p>Act to require all trustees to prepare a RMP both for itself and each fund under its trusteeship. The RMP would demonstrate arrangements trustees have in place to mitigate relevant risks including risks relating to investment, outsourcing, governance and risk management more broadly (including a requirement for a fraud control plan), as well as compliance with the legislation.</p> <p>Other requirements would include that the RMP is to be signed off by the trustee; changes of a material nature to be advised to the regulator and members; an annual independent audit of the plan; the RMP is to be available to fund members; and other issues as considered necessary.</p> <p>The RMP is intended to be a living document and trustees would be required to comply with the conditions on an ongoing basis, both for the trustee and the fund. This would include reviewing the RMP when significant events or circumstances require it to be altered. Trustees would provide APRA and fund members with an updated copy where significant changes have been made.</p> <p>The Government and APRA will consult further with stakeholders on the detail of the RMP.</p>
<p><b>Recommendation 10</b></p> <p>The SWG recommends that compliance with the RMP be audited each financial year, as a component of the fund's existing audit procedures.</p>	<p>The Government supports this recommendation.</p> <p>The Government will amend the SIS Act to require the RMP to be audited annually. The Government envisages that this audit could take place within the fund's existing auditing process to reduce costs.</p>
<p><b>Recommendation 11</b></p> <p>The SWG recognises the diversity of trustee structures that exists in the superannuation industry, and recommends that the Government consider, in consultation with relevant stakeholders, mechanisms for independent oversight of the trustee's</p>	<p>The Government supports this recommendation.</p> <p>The Government will examine whether it is feasible to establish a framework which could involve independent oversight of compliance</p>

<p>compliance with the RMP, and for reporting breaches to the regulator.</p>	<p>with RMPs.</p>
<p><b>Recommendation 12</b></p> <p>The SWG recommends that appropriate enforcement measures be put in place to address non-compliance with the RMP. For example, a significant breach could be required to be reported both to APRA and to members, regardless of whether steps had been taken to remedy the breach. In addition, the SWG recommends trustees be required to notify members that they may seek a copy of their fund's RMP from the trustee.</p>	<p>The Government supports this recommendation.</p> <p>To ensure compliance with RMP requirements, and appropriate trustee accountability, the Government will ensure that APRA has appropriate enforcement powers available to it. Trustees will need to report a significant breach to both APRA and members, and trustees would be required to make the plan available to members.</p> <p>Disclosure obligations will be considered in conjunction with existing FSRA requirements, which already require funds to advise members in point of sale documentation of how to access other available information.</p>
<p><b>Power for APRA to make prudential standards</b></p> <p><b>Recommendation 13</b></p> <p>The SWG recommends that APRA be given a prudential standards-making power similar to the one it has in relation to general insurance. The SWG acknowledges that there are a number of practical implementation issues that will need to be addressed progressively in relation to such a power, in consultation with relevant stakeholders.</p>	<p>The Government does not support this recommendation.</p> <p>The Government supports APRA having sufficient powers and autonomy to effectively prudentially supervise the superannuation industry. However, APRA is not the only body administering the SIS Act and it is imperative that all aspects of the superannuation regulatory framework are taken into account in developing regulation in this area.</p> <p>The Government believes that, at this time, APRA can achieve all its objectives within the existing operating standards power in Part 3 of the SIS Act. Further, the proposed new licensing regime and RMP requirements will address the key issues of competency and governance.</p>

<p><b>Longer term options — separation of prudential and retirement income provisions</b></p> <p><b>Recommendation 14</b></p> <p>The SWG acknowledges that the SIS legislation is complex, and that separation of the prudential and retirement income provisions of the legislation may assist in achieving the goal of simplification of the legislation. The SWG acknowledges, however, that there are a number of practical implementation issues that will need to be addressed and consulted on in relation to such a proposal.</p>	<p>The Government does not support this recommendation.</p> <p>Given that the Government does not support recommendation 13, the Government considers that the separation of retirement income and prudential requirements in the SIS Act should not proceed on cost-benefit grounds. Separating such provisions would take time and be resource intensive and complex, without a demonstrated significant impact on superannuation safety. Such a separation is unnecessary given the Government’s decision not to proceed with recommendation 13.</p>
<p><b>Prudential standards</b></p> <p><b>Recommendation 15</b></p> <p>The SWG recommends that APRA consider developing prudential standards that cover capital, investment rules, outsourcing, governance and operational risk, in consultation with relevant stakeholders.</p>	<p>The Government notes this recommendation.</p> <p>While the Government does not support the development of prudential standards as outlined in recommendation 13, the Government supports the development of appropriate operating standards and the application of conditions to a trustee’s licence, as well as using other tools such as superannuation circulars, to ensure that the regulatory framework meets its objective of ensuring appropriate risk management systems are in place to minimise the chance of fund failure.</p>
<p><b>Capital adequacy</b></p> <p><b>Recommendation 16</b></p> <p>The SWG recommends that, as a part of the licensing process, APRA should determine the amount of resources, including capital, required to be held by each trustee to address the operational risks relevant to that trustee. The legislation should list the factors</p>	<p>The Government supports in-principle a risk-sensitive framework for the holding of capital to address operational risk, but considers that the combination of requirements that each trustee be licensed by APRA, and prepare a risk management plan, will substantially</p>



<p>APRA is required to take into account in determining an appropriate amount of capital, but should not specify a minimum or maximum amount of capital required for each trustee nor how it should be held. APRA should also provide guidance to industry on the weightings it intends to apply to those factors. The SWG recommends that the revised capital requirements be developed in consultation with relevant stakeholders, and be phased in at the same time as the licensing requirements.</p>	<p>address concerns relating to operational risk. Arguably the need for capital in the future may be substantially reduced as other factors come into play to address operational risk. On this basis, the Government supports the retention of the status quo for capital requirements at this time, to be revisited once the impact of the licensing and RMP reforms can be assessed.</p>
<p><b>Investment rules</b></p> <p><b>Recommendation 17</b></p> <p>The SWG recommends that APRA update its current superannuation circular No. II. D.1 - Managing Investments and Investment Choice (April 1999).</p>	<p>The Government supports this recommendation.</p> <p>An update would help to enunciate more clearly the rules governing the diversification and liquidity of investments.</p> <p>The licensing framework and RMP requirements would also be expected to cover these issues.</p> <p>APRA has indicated that a new circular will be updated following industry consultation, and expects it to be available for public release in the first quarter of 2003.</p>
<p><b>Recommendation 18</b></p> <p>The SWG recommends that trustees be required to:</p> <ul style="list-style-type: none"> <li>• ensure that the fund's objectives are clearly articulated; and</li> <li>• identify in their risk management plan the measures that the trustee is adopting to ensure that the fund's investment strategies match the fund's objectives, and are in compliance with the sole purpose test contained in section 62 of the SIS Act.</li> </ul> <p>The SWG also recommends that trustees be</p>	<p>The Government supports this recommendation in-principle.</p> <p>These requirements will be addressed by the RMP requirements and other licence conditions.</p> <p>The detail of the requirements will be developed in consultation with stakeholders.</p>

<p>required to certify whether a fund's investment strategy is in compliance with the fund's objectives. This would then be subject to the fund's annual compliance audit.</p>	
<p><b>Outsourcing</b></p> <p><b>Recommendation 19</b></p> <p>The SWG recommends that, as a condition of the APRA licence, trustees be required to include a term in any contracts with third party service providers that provides APRA with a right of access to the third party in the event that APRA has concerns about the impact of the activities of the third party on the APRA-regulated entity. The SWG also considers that APRA should be required to notify other trustees using the same service provider of any concerns APRA may have in relation to the service provider</p>	<p>The Government supports this recommendation.</p> <p>Such a provision would assist APRA to prudentially monitor superannuation funds where functions have been outsourced to third parties. This would assist APRA's risk-based supervision of superannuation funds.</p> <p>The detail of the requirements will be developed in consultation with stakeholders.</p>
<p><b>Governance and operational risks</b></p> <p><b>Recommendation 20</b></p> <p>The SWG recommends that, as a component of the licensing framework, trustees be required to demonstrate in their RMP how they propose to deal with governance and risk management requirements.</p>	<p>The Government supports this recommendation.</p> <p>The detail of the requirements will be developed in consultation with stakeholders.</p>

<p><b>Annual meetings</b></p> <p><b>Recommendation 21</b></p> <p>The SWG recommends that the proposals contained in the Issues Paper to require superannuation funds to hold annual general meetings or that members be given the right to request a meeting at any time, not be proceeded with.</p>	<p>The Government supports this recommendation.</p> <p>The Government considers that an increase in member participation and improved trustee accountability can be achieved through the recommendations on disclosure and RMPs. However, the Government will leave open the option of re-examining the appropriateness of annual meetings, should the measures above not adequately address member participation.</p>
<p><b>Public disclosure of annual returns</b></p> <p><b>Recommendation 22</b></p> <p>The SWG recommends that for funds other than those with fewer than five members and EPSSSs, ASIC utilise its existing electronic facilities to make publicly available the audited accounts of funds and the fund information required to be given to members, provided the costs are reasonable.</p>	<p>The Government supports this recommendation.</p> <p>Making publicly available the audited accounts and fund information would enhance the transparency of superannuation fund operations. It would also enhance decision making by members, because while members already get this information, they will benefit from the assessments of funds which will arise through increased public scrutiny.</p> <p>It is proposed that the audited financial statements and key fund information, currently made available to members, will be made publicly available through ASIC's existing database facilities.</p>
<p><b>Recommendation 23</b></p> <p>The SWG recommends that trustees be required to notify superannuation fund members of the presence, and nature, of any qualification of the fund's auditor's report.</p>	<p>The Government supports this recommendation.</p> <p>In general, the Government considers that notification of important events, such as a qualification of the audit report, needs to be improved. The Government will undertake the necessary steps to require superannuation fund members to be notified of the presence and nature of any qualification of the fund's</p>

	auditor's report.
<p><b>Member approval for giving benefits to related parties by trustee</b></p> <p><b>Recommendation 24</b></p> <p>The SWG recommends that the Government consider reducing the length of time that grandfathering arrangements contained in Part 8 of the SIS Act apply for all funds other than SMSFs and EPSSSs.</p>	<p>The Government does not support this recommendation.</p> <p>The transitional provisions which grandfathered amendments to the in-house asset rules in 1999 to 2009 were arrived at after extensive consultation and ensure that superannuation funds need not unwind investments that were made by trustees in accordance with the legislation that existed at the time. These transitional provisions have been relied upon by industry for their operational decision-making and any change would involve significant amount of retrospectivity. The Government does not plan to amend them.</p>
<p><b>Recommendation 25</b></p> <p>The SWG recommends that trustees be required to disclose in their Product Disclosure Statement (PDS) any in-house assets held by the fund.</p>	<p>The Government supports this recommendation.</p> <p>The disclosure of in-house assets in the PDS will increase disclosure to prospective fund members, and in particular the level of transparency and accountability to fund members. The Government will undertake the necessary legislative amendments to implement this.</p>
<p><b>Recommendation 26</b></p> <p>The SWG recommends that the definition of 'significant event' in the ongoing disclosure requirements under the Corporations Act be amended to require the disclosure of non-investment transactions that are entered into by trustees with related parties.</p>	<p>The Government supports this recommendation.</p> <p>The Government will amend the relevant provisions to require the disclosure of non-investment transactions entered into by trustees with related parties.</p>

<p><b>Financial assistance to failed superannuation funds</b></p> <p><b>Recommendation 27</b></p> <p>Given that the current provisions contained in Part 23 of the SIS Act have not yet been fully tested, the SWG recommends that the provisions not be changed at this time. However, the SWG recommends that the Government review the operation of Part 23 and consider possible amendments to it once the first decision under Part 23 has been made.</p>	<p>The Government supports this recommendation.</p> <p>Since 14 June 2002, the Government has made over 190 determinations (relating to two events) to grant financial assistance to funds that have suffered loss as a result of fraudulent conduct or theft.</p> <p>The Treasury will review the operation of these provisions, in consultation with key stakeholders.</p>
<p><b>Contributions</b></p> <p><b>Recommendation 28</b></p> <p>The SWG considers that the Government should examine the need to specify a timeframe within which salary sacrifice superannuation contributions should be paid to a superannuation fund on behalf of an employee.</p>	<p>The Government supports this recommendation and has asked Treasury to review this issue.</p>