



12 February 2014

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

By email superannuationconsultation@treasury.gov.au

Dear Sir/Madam

Better regulation and governance, enhanced transparency and improved competition in superannuation

IOOF welcomes this opportunity to make a submission on the measures outlined in the Discussion Paper.

The key issues we highlight are:

- the timeframe for rollovers should be extended from 3 days to 14 days (Focus Question 1);
- the definition of independent director to not restrict the composition of a superannuation trustee company being the same as the parent company (Focus Question 2);
- there should be no change to the composition, appointment and renewal requirements for boards and the chair of the board (Focus Questions 3 to 6);
- dashboards should not be required for a MySuper product with less than 10 years investment performance (Focus Question 13); and
- superannuation should not be an industrial award matter and employers should be able to nominate any MySuper product as their default superannuation fund (Focus Questions 28 and 30).

Any questions about this submission can be directed to Melinda Hofman, Corporate Affairs Manager, on 02 9028 1054 or the undersigned on 03 9203 4750.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Christopher F Kelaher', with a long horizontal flourish extending to the right.

Christopher F Kelaher
Managing Director



Better regulation and governance,
enhanced transparency and improved
competition in superannuation

Submission by:
IOOF Holdings Limited (**IOOF**)

Introduction

IOOF is an ASX (Australian Securities Exchange) 200 listed diversified financial services holding company. IOOF (including subsidiaries) has \$124.7 billion in Funds Under Administration, Management and Supervision (FUMAS) at 30 September 2013. IOOF operates across: financial advice and distribution; superannuation and investment products; investment management; stockbroking; estate planning; and trustee services.

IOOF is the parent of three APRA-regulated superannuation trustees: Australian Executor Trustees Limited, IOOF Investment Management Limited and Questor Financial Services Limited. Between them, these superannuation trustees are responsible for approximately:

- \$85 billion in superannuation assets; and
- 600,000 superannuation fund member accounts.

IOOF is unique in the superannuation sector in being independent of the big banks and life insurers. We are positioned to be a distinctive competitor in the superannuation sector which is increasingly becoming concentrated.

This submission addresses Focus Questions 1, 2-6, 8-13, 28 and 30 of the Discussion Paper.

Focus question 1 – regulatory burden

IOOF supports the positions proposed by the FSC in their submission on a better approach to regulation.

Additionally, IOOF considers the 3-day rollover requirement in regulation 6.34A of the *Superannuation Industry (Supervision) Regulations* to be impractical and attempts to meet it may have adverse effect on superannuation fund members and impose cost on superannuation fund trustees.

Superannuation trustees seek to structure fund investments to achieve a good outcome for members. Some structural measures to achieve this include:

- using a diversified investment strategy, which includes foreign assets

- using best practice forward-pricing methodology, so that all members are able to get the next available price and not allow a member to profit from market movements at the expense of the fund through historic pricing
- being fully invested into underlying investments by not holding a cash float.

However the first two of these are incompatible with a 3-day rollover timeframe. Foreign investments necessarily are priced at market close time in time zones later than Australian time zones which can add up to one day to processing times. Using forward pricing means that instead of applying yesterday's price to withdrawals on a member's account the forward price, or price available following the close of business today, is used and obtaining the price can add up to one day to processing times. These two measures put funds at a 2 day disadvantage in processing a rollover within 3 days. Additional time is then taken to make the request to redeem underlying funds, receive and reconcile redemption proceeds, check and then process and make the outward payment.

The above issues can be alleviated by holding a cash float instead of being fully invested, but to do so means that part of the investment strategy of fund members is designed not to achieve their long term retirement needs but to fund short term cash flow requirements of the fund.

Changing systems and procedures to deliver a 3-day timeframe may disadvantage fund members and incur development cost and additional staff costs for the superannuation trustee. Whilst SuperStream improves processing between superannuation funds, many funds support SuperStream through manually assisted internal processes. Imposing an unduly tight timeframe to rollovers may cause controls to be weakened, increase fraud risk or introduce error.

Recommendation:

The timeframe of 3 days for rollovers in regulation 6.34A should be extended to 14 days.

Focus question 2 – independence

While we endorse the recommendation to have independent Directors appointed to the Board of Trustees of Industry Superannuation Funds as part of the measures which have been proposed to achieve "Better Regulation and governance, enhanced transparency and improved competition in superannuation", we have significant concerns about the unintended consequences of extending this requirement to situations such as apply with IOOF where each of the APRA regulated superannuation trustee companies operated as a subsidiary of the Parent Company.

The composition of the boards of IOOF and its three superannuation trustee subsidiaries is the same. Each board has six members, five of whom are independent non-executive directors.

The ASX-listed parent board, IOOF, meets the independence definition of the ASX Principles and the chair of the board is an independent director. The chair of the IOOF board is the chair of the each of three superannuation trustee subsidiaries.

The current composition arrangements for IOOF and its superannuation trustee subsidiaries are consistent with the law and ASX Principles.

IOOF is a member of the Financial Services Council (FSC). FSC Standard No. 20 *Superannuation Fund Governance Policy* includes a definition of independent director which means that a person who is a director of a parent company is not an independent director of a superannuation trustee.

IOOF considers such a definition should not be adopted as part of the government's reforms. It is inconsistent with general corporate governance relationships between parent and subsidiary companies. For example, a director of a wholly-owned subsidiary is taken to have acted in good faith in the best interests of the subsidiary when acting in the interests of the holding company.¹ For a superannuation trustee the fund members' best interests remain paramount. Subject to that requirement, a superannuation trustee and its parent can align strategy, structure and financial arrangements for the efficient operation of a corporate group. We consider this is best achieved through aligning the composition of the boards.

Details of the directors of board are publicly available, however some retail investors would not consider looking-through the holding company structure to determine who the directors of the subsidiary company are and we consider that aligned composition promotes transparency.

As noted in the introduction, IOOF is a distinctive participant in the superannuation sector and contributes to competition. We consider that competition should not be constrained by the effects of regulatory change aimed at achieving a particular objective, such as superannuation trustee independence. Causing all in the superannuation sector to have the same independent board structure has an adverse impact on competition for a distinctive participant like IOOF. Public policy should lean towards promoting not inhibiting competition. The regulatory changes proposed should address the excessive costs of implementing the existing legislation, without adding new costs or reducing consumer protection.

To require each Registrable Superannuation Entity (RSE) Board to have different Directors from the Parent Company Board will not achieve these objectives, in our view, and will give rise to a number of unintended consequences, including:

- an increased cost of operations, and
- a diffusion of responsibility,
- without enhancing the best interest of members.

The reasons for these unintended consequences are as follows:

1. Increased Costs

IOOF currently operates through a shared services model which ensures maximum operating efficiencies and cost minimisation for members' accounts. Adding different Directors to the RSE Board will increase the direct cost of operations through additional director fees and duplication of services. These costs will need to be passed on to members.

2. Diffusion of Responsibility

Many Directors have acquired significant knowledge of the history and background to the superannuation funds and of the companies of which they act as a director. The issues

¹ s 187 Corporations Act 2001.

arising between superannuation trustees in a group are similar. Shared knowledge of each trustee's operations and group-wide processes that affect these entities help to avoid inefficient or inconsistent outcomes for fund members and promote efficient decision making. An example of where such problems could occur would be where one trustee subsidiary appoints an operational administrator which is inconsistent with the shared services used by the other trustee boards.

If the current regime for APRA's supervision of banks and life insurers work, why can't it continue to be used for superannuation funds?

It is not clear what problem would be solved by extending the policy of requiring independent Directors on superannuation fund Board to a corporate Parent/Subsidiary RSE structure with a majority of independent Directors as exists with IOOF.

IOOF has an aligned structure with 5 of its 6 Directors at the Parent Company level who are independent. When these same Directors sit on the subsidiary Boards, they are also independent, under Corporations Law definitions and are deemed to be acting in the best interests of the subsidiary.

Having more independent Directors at the subsidiary RSE level will never achieve "independence" in practice given that their appointment and remuneration will be determined by the Parent Company. Nor will the diffusion of responsibility introduced by such an arrangement enhance the best interests of members. Indeed, we argue that the opposite will often be the case.

3. Best Interest

The Directors chosen to sit on Parent Company and subsidiary superannuation trustee boards can be expected to have the right mix of skills, experience and knowledge to consider complex strategic transactions and commercial decisions that may occur across different superannuation trustees. The Parent and the Directors can also be expected to have a shared view of the direction of the superannuation funds, i.e., to maximise investment returns, minimise operating costs and build FUM (to achieve economies of scale in operations).

This arrangement ensures that the Directors acting on behalf of members are amongst the best available, have access to comprehensive economic and financial information in order to make informed decisions on behalf of members and are in the best position to maximise the interest of the superannuation fund members. The arrangement also ensures that Directors who are aware of emerging issues in one superannuation trustee can respond quickly to minimise risk or act on opportunities, of which they may otherwise be unaware.

Our view is that there is a restricted pool of suitably qualified and experienced candidates to be Directors of RSE's in Australia. A requirement that Directors of superannuation trustees not be Directors of the Parent Board and not be Directors of competing superannuation funds would further narrow the pool available and do nothing to enhance the best interests of members.

Realignment of board composition to meet independence requirements increases direct costs through payment of director’s fees for additional independent directors and compliance costs in ensuring that differently constituted boards each meet their obligations. Pursuit of the objective of more independent directors on superannuation fund boards should not be at the expense of qualification and experience.

If the key objective is to introduce principles of independence into the governance of superannuation funds without creating unintended consequences, a simple solution would be to introduce independence requirements for non-listed entities and permit ASX listed groups to retain their current Board composition, consistent with the ASX Principles of Good Governance. Such an approach would permit the ASX Principles of Good Governance to prevail – where they are seen to be working – and also apply high standards to other entities not listed on the ASX. Alternatively, all superannuation trustees could be required to follow those principles in relation to independence and if they elect not to then they would be required to report to members why not.

Recommendation:
There should be no restriction on the appointment of directors to superannuation funds within the same corporate group in the definition of independent director.

Focus questions 3 to 6, 8 to 12

IOOF supports the current composition, appointment and renewal requirements for boards and the chair of the board. Nevertheless, we consider that should any change be made, it should be limited and should be to mirror the APRA requirement for a majority of independent directors and independent chair as is required for banking and insurance entities.

Any changes would best be made through an APRA Prudential Standard which allows for further consultation and flexibility. We consider that an APRA Prudential Standard issued with sufficient lead-time for implementation would give certainty to industry.

Some groups, including IOOF, have established governance arrangements that work for our operating model. Transitional rules that preserve the current definitions for existing directors until retirement would help to provide certainty.

Recommendation:
There should be no change to the composition, appointment and renewal requirements for boards and the chair of the board.

Focus questions 13-19

IOOF supports the positions proposed by the FSC in their submission on choice product dashboard and we make the following additional submission.

MySuper product dashboard – Focus question 13

The key objective of the dashboard is to provide a clear and simple 'like for like' comparison between funds, but the requirement does little to meet this objective where products with long established investment performance are compared to new products with no performance history.

Due to the lack of historical information that will be available to publish where a new MySuper product has been established (as it is the case for IOOF), new MySuper products should be 'carved out' until such time as sufficient data is available to make the dashboard reporting meaningful.

The 10 year performance comparison is only possible once there is 10 full years of history, which for our MySuper product will be from July 2025. There is no point showing a 'since inception' figure as this will not be comparable between funds and therefore meaningless. The dashboard performance comparisons are only useful for funds that have been in operation for 10 years or more.

In addition, existing funds, whilst likely have longer term performance history, comparing that performance to a 10 year net return target such as CPI + a percentage (which has only just been recently introduced with the APRA requirements) is not a reasonable representation of how the fund has historically performed to benchmark, when the benchmark (target return) has only recently been established. This could be misleading, implying that at the end of a reporting period, the 10 year average target may have been met or even exceeded, when in fact, the target did not exist until a few months ago.

Whilst the intention is clearly not to mislead, reporting in accordance with the requirements as they stand, may tend to confuse rather than inform less engaged members.

Recommendation:

Dashboards should not be required for a MySuper product with less than 10 years investment performance.

Focus questions 20-26

IOOF supports the positions proposed by the FSC in their submission on portfolio holdings disclosure.

Focus questions 28 and 30

IOOF supports the positions proposed by the FSC in their submission on enhancing competition we make the following additional submission.

Improved competition in the default superannuation market.

The policy background to MySuper is:

MySuper is a new, simple and cost-effective superannuation product that will replace existing default products. MySuper products will have a simple set of product features, irrespective of who provides them. This will enable members, employers and market analysts to compare funds more

easily based on a few key differences. It will also ensure members do not pay for any unnecessary 'bells and whistles' they do not need or use.²

In light of the public policy rationale for MySuper there is no reason why restrictions should be placed on which superannuation fund or funds an employer nominates as their default superannuation fund. Employers should be entitled to choose any MySuper product.

It follows that superannuation should not be an industrial matter and there should be no role for the Fair Work Commission (FWC) in determining to which superannuation funds should be the default fund for an employer. That the Productivity Commission has identified issues in the existing process for selecting default superannuation funds lends support for removing it as an industrial matter. Requiring FWC to initially select and periodically review the default superannuation fund creates an unnecessary step in the award determination process.

The public policy principles behind creating MySuper as a simple, cost-effective, comparable product indicates that filtering MySuper funds by FWC or any other body should be unnecessary. The current arrangement imposes unnecessary cost on government in filtering funds, on industry in negotiating awards and on the superannuation sector in making submissions about their funds.

Recommendation:

Superannuation should not be an industrial matter or considered by the Fair Work Commission in determining awards. Any MySuper product should be available for nomination by an employer as the default superannuation fund.

² http://strongersuper.treasury.gov.au/content/Content.aspx?doc=publications/information_pack/mysuper.htm