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SUPERANNUATION REGULATION AND GOVERNMENT POLICY

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Our superannuation consultants provide a synopsis of regulatory and government policy changes impacting the superannuation industry.

Legislation Supporting Budget Announcements

Legislation supporting the Government's 2016-17 Budget announcements passed through both Houses of Parliament, and received Royal Assent on 29 November 2016.

Very briefly, the changes set out in *The Treasury Laws Amendment (Fair and Sustainable Superannuation) Act 2016* and *the Superannuation (Excess Transfer Balance Tax) Imposition Act 2016* will:

- › Reduce the annual concessional contribution cap to \$25,000 (indexed);
- › Reduce the annual non-concessional contribution cap to \$100,000 (indexed) and only allow non-concessional contributions to be made by individuals with a superannuation balance below \$1.6 million (indexed);
- › Lower the threshold for Division 293 tax to \$250,000;
- › Cap transfers to retirement income streams at \$1.6 million (indexed);
- › Remove the tax exempt status for income from assets supporting transition to retirement income streams;
- › Introduce the Low Income Superannuation Tax Offset (replacing the Low Income Superannuation Contribution);
- › Improve access to concessional contributions;
- › Enable catch up concessional contributions for individuals with superannuation balances below \$500,000 (non-indexed);
- › Remove the anti-detriment payments for death benefits; and
- › Extend the tax exemption for retirement products.

The proposal to remove the work test for people aged 65 to 74 who wish to make contributions did not proceed.

The Government has set an ambitious timetable for the introduction of the changes, with most new measures to take effect from 1 July 2017. However, there is concern within the superannuation industry that it will be difficult to have systems updated and ready to handle the changes by 30 June.

In respect of the application of the \$1.6 million transfer balance cap to defined benefit income streams, the Government's stated intention is to achieve a taxation outcome that is commensurate with the outcome for other (i.e. non-defined benefit) income streams whilst recognising that it is sometimes individuals are not able to commute part of their pensions. The Government has split defined income streams into capped defined benefit income streams, which do not need to be commuted, and other defined benefit income streams.

Income stream pensions which satisfy sub-regulation 1.06(2) (some lifetime pensions), 1.06(7) (life expectancy pensions) or 1.06(8) (market linked pensions) of the *Superannuation Industry (Supervision) Regulations* will not be required to be partially commuted even if the income stream is valued at over \$1.6 million. The legislation also specifies how these income streams are to be valued. For a lifetime pension, the value is simply 16 times the annual pension, irrespective of the pensioner's age or particular provisions of the pension such as the level of indexation.

The Government has released draft regulations which include provisions to expand the existing exceptions to the restrictions on commutations to permit the

commutation of certain superannuation income streams that are done for the purpose of reducing or avoiding an excess transfer balance". This is somewhat confusing because the amendments appear to relate only to income streams that are "capped defined benefit income streams", for which there are already legislative provisions specifically designed to avoid an excess transfer balance and the need to commute.

The draft regulations also includes legislation which will let the trustee of a defined benefit fund elect that deductible personal contributions may be not be made to the fund. These amendments are intended to ensure that funds do not face undue costs if members are able to deduct personal contributions.

The Government also announced that further draft regulations covering valuation rules for the transfer balance cap will be released in early 2017. It is hoped that these regulations will provide some clarification on the treatment of defined benefit income streams which do not satisfy the above mentioned sub-regulations, as the legislation is currently silent on this.

Objective of Superannuation

The *Superannuation (Objective) Bill 2016* was passed by the House of Representatives on 22 November 2016, and then referred to the Senate Economics Legislation Committee. The Committee is scheduled to report on its inquiry by 14 February 2017.

The Bill enshrines in law that:

The primary objective of the superannuation system is to provide income in retirement to substitute or supplement the Age Pension.

The Government has released draft regulations which set out five subsidiary objectives to support the primary objective of the superannuation system. The subsidiary objectives provide a framework for assessing the compatibility of a bill or regulation with the primary objective of the superannuation system. These subsidiary objectives are to:

- › facilitate consumption smoothing over the course of an individual's life;
- › manage risks in retirement;
- › be invested in the best interests of superannuation fund members;
- › alleviate fiscal pressures on Government from the retirement income system; and
- › be simple, efficient and provide safeguards.

Once passed, this legislation will require every bill or regulation relating to superannuation to be accompanied by a statement of compatibility with the primary and subsidiary objectives of the superannuation system.

Retirement Products

The Government has previously stated it will support the development of comprehensive income products for retirement – otherwise known as CIPRs – by removing barriers to innovation in retirement income stream products.

On 15 December 2016, Minister O'Dwyer, released a discussion paper exploring key policy issues to facilitate further development of a framework for the retirement phase of the superannuation system. As part of its consultation, the Government is proposing to rename CIPR's as "MyRetirement products".

The Government intends to facilitate superannuation trustees offering MyRetirement products to provide an anchor to help guide individuals in their retirement income decision making. People will not be forced to use these products – they will simply provide an additional option for managing finances in retirement.

The discussion paper states that that the fear of running out of money (i.e. longevity risk) causes people to withdraw too little from their account based pensions, thus reducing their standard of living in retirement. The CIPRs framework is intended to enable individuals to increase their standard of living in retirement through increased availability and use of products that more efficiently manage longevity risk via some form of risk pooling. Australians have generally not been comfortable with the idea of forfeiting part, or all, of their superannuation balance on death. For the CIPRs to achieve the Government's aim, this attitude will need to be changed, and this may only occur slowly over a considerable period of time.

This is a new and complex area and, unlike with some other recent draft legislation, Treasury has allotted a reasonable amount of time for consultation, with the closing date for submissions being 28 April 2017.

Separately, the Department of Social Services has issued a discussion paper on social security means testing of retirement income streams. The paper addresses the means testing treatment of new income stream products which are likely to be developed, such as deferred annuities and group self annuitisation products. The consultation process will also extend to assessing whether the means test rules for existing types of retirement products are fit for purpose.

Progressing existing legislation

Whilst focus has been on the legislation to support the 2016 Budget changes, the Government has indicated that it will continue to pursue other previously announced legislative reforms. In a speech at the ASFA conference in November, the Minister for Revenue

and Financial Services, Ms Kelly O'Dwyer, mentioned that the Government intended to continue progressing superannuation legislation that was previously before the Parliament. This includes legislation:

- › extending choice of fund arrangements;
- › improving superannuation governance by requiring superannuation trustee boards to have a minimum of a third independent directors including an independent Chair; and
- › increasing transparency by requiring superannuation funds to disclose information about their underlying assets and choice products to their members.

The Prime Minister emphasised the focus on governance in an address to the Financial Services Council on 14 December stating that, "in 2017, my Government will reintroduce legislation to address existing inconsistencies, raise the standards of governance and put the interests of members ahead of any self-interest in the superannuation sector".

Productivity Commission Review of Superannuation System

In November 2016, the Productivity Commission released its report on stage one of its review into the efficiency and competitiveness of the superannuation system. In the report, the Commission has developed criteria to assess whether, and the extent to which, the superannuation system is efficient and competitive in delivering the best outcomes for members.

The Commission's approach is to define five system-level objectives, which are within the scope of influence of the superannuation system and specific to the principles of competitiveness and efficiency.

For each of these objectives the Commission has formulated assessment criteria, which are performance standards to assess whether the objectives have been achieved. For each assessment criterion, a set of indicators have been identified to facilitate assessment. In total there are 22 assessment criteria and 89 unique indicators. The Commission acknowledges that the assessment process will be data intensive and it intends to draw on existing data as much as possible. A minor share of the indicators will rely on new data collections via case studies and surveys of funds or members. Participation will be voluntary.

In stage two of the review, the Commission is to conduct a public inquiry to examine alternative models for a formal competitive process for allocating default fund members to products. An Issues Paper titled "Superannuation: Alternative Default Models" was released in September 2016 to facilitate discussion and the Commission's draft report is due in March 2017.

Both stages one and two of the review will inform the Commission's inquiry to review the efficiency and competitiveness of the superannuation system following the full implementation of the MySuper reforms (stage three).

Governance

The Australian Prudential Regulation Authority (APRA) has released updated governance requirements for APRA-regulated superannuation trustees (RSE licensees) with a final revised prudential standard and prudential practice guide on governance.

This release follows consultation on amendments to Prudential Standard SPS 510 Governance (SPS 510) and Prudential Practice Guide SPG 510 Governance (SPG 510).

The original SPS 510 and SPG 510 took effect in 2012 and 2013 respectively, and are being updated to further enhance governance practices across the superannuation industry.

The amendments to the prudential standard include requiring RSE licensees to have in place a governance framework which sets out policies and procedures to support effective governance practices. The amendments also require the establishment of policies and processes for the nomination, appointment and removal of directors including policies and procedures to address board renewal, director tenure limits and board size.

The prudential practice guide has been updated to clarify APRA's expectations regarding key governance practices, to support the new requirements set out in the prudential standard.

Final SPS 510 will take effect on 1 July 2017, but APRA expects RSE licensees to consider the guidance in SPG 510 immediately.

External Dispute Resolution

The expert Panel, appointed by Treasury, has released its interim report on its review of the financial system's external dispute resolution framework. The Panel's approach was to assess the current framework, consisting of the Financial Ombudsman Service (FOS), Credit and Investments Ombudsman (CIO) and Superannuation Complaints Tribunal (SCT) against the Review's core principles of efficiency, equity, complexity, transparency, accountability, comparability of outcomes and regulatory costs, and to incorporate best practice developments from other sectors in Australia and overseas jurisdictions.

According to the Interim Report, the SCT has strengths, including its unlimited monetary jurisdiction, but the rigidity of the statutory model makes it more difficult to match the industry ombudsman schemes in terms of

flexibility and innovation. This is a significant problem as existing pressures on the SCT will continue to grow as the superannuation system matures and an ever increasing number of Australians enter the drawdown (retirement) phase. The Interim Report also noted that the SCT has experienced chronic underfunding and under resourcing. The Panel's draft recommendations include that the SCT be transitioned to a new industry ombudsman scheme for superannuation disputes and that the superannuation industry should develop a superannuation code of practice.

On 3 February, Minister O'Dwyer expanded the terms of reference for the review to include:

- › the making of recommendations (rather than merely observations) on the establishment, merits and potential design of a compensation scheme of last resort; and
- › consideration of the merits and issues involved in providing access to redress for past disputes.

Supporters of a compensation scheme of last resort argue that it will build trust and confidence in both industry ombudsman schemes and the financial system more generally. The cost of funding the scheme would, of course, be an additional impost on the financial services industry and there is also a risk that the very existence of a last resort scheme increases the potential for moral hazard.

Efficiency – ATO guide for APRA funds

The ATO has released a guide for APRA funds, which summarises changes which have been made, or will be made, to standardise the exchange of information and money between the ATO and superannuation funds. The guide is based on government policy announcements, recent legislative changes and consultative discussions with the industry on changes to the superannuation system. The information provided by the ATO is intended to help funds understand reforms being implemented over the next few years and to prepare for the changes. It also provides information about what members can see and do online. The ATO will regularly update information about these changes and their planned implementation.

Issues covered in the guide include unclaimed superannuation, providing and using TFNs, online services for fund members, rollovers and defined benefit schemes, contribution caps and member contribution statements (MCS).

The online services, which can be accessed via the myGov website, allow members to see all their superannuation information in one place, no matter which fund holds their superannuation. ATO-held amounts are also displayed. With the information displayed online, it is now very easy for members to consolidate their

superannuation accounts using the 'transfer super' functionality.

Members of defined benefit funds can request a rollover of a defined benefit, but it is up to the fund trustee to determine whether to allow the rollover of a defined benefit because it is not subject to the compulsory portability legislation. The information reported by funds in their Member Contribution Statement allows the flagging of accounts which cannot be rolled over and the myGov website will prevent a member from selecting these accounts to roll over.

Transparency and Member Engagement

In late 2015, ASIC issued *Regulatory Guide 97 (RG 97): Disclosing fees and costs in PDSs and periodic statements*. Under RG 97, issuers of most superannuation products and managed investment products issued to retail investors, must meet expanded requirements for disclosing fees and costs in Product Disclosure Statements (PDSs) and periodic statements. RG 97 requires disclosure of certain transaction and derivative costs incorporated in investment performance.

The date by which the requirements must be met for PDSs is 1 February 2017. However, on 29 November 2016, ASIC announced that the transition period will now end by 30 September 2017 for issuers that notify ASIC in writing by 31 January 2017 that they intend to take advantage of this extension in relation to a PDS, and provide ASIC, before 1 March 2017, information about the fees and costs that would be required to be included in this PDS had they complied with the updated fees and costs disclosure requirements.

ASIC will be amending class order 14/1252 *Technical modifications to Schedule 10 of the Corporations Regulations* to give this extension effect. ASIC will also publish instructions and the forms to provide the above information by issuers seeking to take advantage of the extension.

The new disclosure standards will flow through to periodic statements for statements given to members from 1 January 2018.

ASIC has also written to trustees of superannuation funds with employer subplans reminding them that certain documents for those subplans must be disclosed from 1 July 2017. The documents include the trust deed, governing rules, actuarial reports for defined benefit funds, product disclosure statements, annual reports and summaries of each significant event notice in the previous two years.

Timeline of events	
Timeframe	Event
1 February 2017	Updated fee and cost disclosure requirements apply to Product Disclosure Statements (unless issuers have advised ASIC that they wish to take advantage of the extended deadline of 30 September 2017)
No later than 1 July 2017	ADAs transferred to MySuper product
Financial years beginning on or after 1 July 2016	AASB 1056 (financial reporting for superannuation funds) takes effect
1 July 2017	Product dashboards to be publicly available for choice products (largest ten investment options only)
1 July 2017	Imposition of \$1.6 million cap on transfers to retirement phase
1 July 2017	Reduction in annual concessional and non-concessional contribution caps to \$25,000 and \$100,000, respectively
1 July 2017	Reduction in threshold for Division 293 tax to \$250,000
1 July 2017	Introduction of additional income tax rules on recipients of certain defined benefit income streams in excess of \$100,000 per annum
1 July 2017	Anti-detriment deduction removed for deaths occurring after 30 June 2017
1 July 2017	Remove the requirement that an individual must earn less than 10% of their income to be able to claim a deduction for personal superannuation contributions
1 July 2017	Removal of the Low Income Superannuation Contribution (LISC), to be replaced by the Low Income Superannuation Tax Offset
1 July 2017	Include product dashboard with periodic statement
1 July 2017	Disclosure of RSE documents for employer-sponsored sub-plans
31 December 2017	First reporting day for the portfolio holdings disclosure requirements
1 January 2018	Updated fee and cost disclosure requirements apply to periodic statements
1 July 2018	Employers with more than 20 employees to use Single Touch Payroll enabled software for reporting PAYG withholding amounts and superannuation contributions to ATO
2019-20	First year that additional concessional contributions can be made under the unused concessional contributions cap provisions
1 July 2021	SG increases resume (9.5% to 10%)

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