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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

2016/17 Federal Budget

The changes announced in the 2016/17 Federal Budget are now in effect. A summary of some of the key changes is shown in the timeline of events section of this newsletter.

The *Treasury Laws Amendment (2017 Measures No 2) Act 2017 No 55* received Royal Assent on 22 June 2017. The Act makes a range of amendments to clarify details of the 2016/17 Federal Budget changes relating to the transfer balance cap, concessional contributions, non-concessional contributions, transition to retirement incomes and capital gains tax relief.

2017/18 Federal Budget

In its 2017/18 Federal Budget, the government made a number of superannuation related announcements[1]. Draft Legislation supporting some of these announcements was released on 21 July 2017. The draft *Treasury Laws Amendment (Reducing Pressure on Housing Affordability) Bill 2017 and First Home Super Saver Bill 2017* introduces:

- the First Home Super Saver Scheme (FHSSS), which allows individuals to save for their first home inside superannuation. Under the scheme, first home savers who make voluntary contributions into the superannuation system would be able to withdraw those contributions, and an amount of associated earnings, for the purposes of purchasing their first homes. Voluntary contributions are member contributions and employer contributions that are not SG or Award contributions. Amounts contributed through concessional contributions and withdrawn under the Scheme will be taxed at marginal rates less a 30% offset. A penalty tax will apply if the amount released is not used to purchase a residential property or recontributed to super.
- a downsizing measure which would allow individuals, aged 65 years or over, to make non-concessional contributions of up to $300,000 from the proceeds of selling their main residences to their superannuation accounts. Downsizer contributions can be made regardless of the other contribution caps and restrictions that might apply to making voluntary contributions. This measure would apply to proceeds from contracts for the sale of a main residence entered into (exchanged) on or after 1 July 2018.

Submissions in relation to this draft legislation closed on 4 August 2017.

In the 2017/18 Federal Budget, the government announced it will overhaul the dispute resolution framework with the establishment of a new single one-stop shop service from 1 July 2018 called the Australian Financial Complaints Authority (AFCA), which will have the power to resolve complaints regarding banks, super funds and other financial institutions. Decisions by the AFCA will be binding on both consumers/members as well as financial services providers. The AFCA will eventually replace the Superannuation Complaints Tribunal (SCT).

On 17 May 2017, the government released draft legislation and a consultation paper on the new dispute

1 See Russell Investments' 2017/18 budget announcement summary at https://russellinvestments.com/au/insights/library/2017-federal-budget-update

resolution framework, with submissions closing on 14 June 2017. On 26 July 2017, the government announced the formation of a transition team for advice on AFCA's terms of reference, governance and funding arrangements.

Following the budget announcement, from 1 July 2017, the Australian Securities and Investments Commission (ASIC) will introduce a new levy and the existing Australian Prudential Regulation Authority (APRA) levies will be further increased to meet the evolving regulation needs of new products.

ASIC released its report, *Report 535 ASIC cost recovery arrangements: 2017-2018* on 14 July 2017. For superannuation trustees, the levy will be based on the total value of assets as at 30 June in registrable superannuation entities, excluding assets that are an interest in another registrable superannuation entity operated by the trustee. The first invoices will be issued in January 2019 and will recover the actual costs that ASIC incurred for regulatory activities in the 2017/18 financial year, plus a clawback for some prior year costs.

Legislation to improve accountability and member outcomes in super

On 24 July 2017, the Government released the *Treasury Legislation Amendment (Improving accountability and member outcomes in superannuation) Bill 2017* for consultation.

The legislation will amend the *Superannuation Industry (Supervision) Act 1993*, the *Corporations Act 2001*, and the *Financial Sector (Collection of Data) Act 2001*. In introducing this legislation, the government believes this package will improve accountability and member outcomes by:

- replacing the current 'scale test' with an expanded 'outcomes test' that requires trustees to undertake an annual determination considering a number of features to ensure the outcomes being delivered are in the financial interests of their members;
- providing APRA with enhanced capacity to refuse or cancel a MySuper authorisation, where it believes that the Registrable Superannuation Entity (RSE) licensee may not comply with its obligations;
- providing APRA with improved powers to enable it to intervene at an early stage to address prudential concerns;
- aligning the superannuation director penalty regime with the penalty regime that applies to directors of managed investment schemes;
- requiring people to seek approval from APRA prior to a change in ownership or control of an RSE licensee occurring;
- requiring RSE licensees to hold annual members' meetings to enable members to ask questions about all areas of their RSEs performance and operation; and
- enabling APRA to gather more information on the operational and managerial expenses of RSEs.

The measures in the package have been drawn from past reviews into superannuation, and does not make any changes to the taxation within superannuation.

Submissions on the draft legislation closed on 11 August 2017.

In response to draft legislation, APRA wrote to RSE licensees[2] setting out its approach to the government's super system reforms aimed at enhancing APRA's prudential powers to improve member outcomes. APRA Deputy Chairman, Helen Rowell, said the regulator will consult on potential amendments to its prudential framework, consistent with the draft legislation and according to the ultimate legislated timetable.

As noted above, under the proposed reforms, the current 'scale test' (s 29VN of the SIS Act) will be replaced with an 'outcomes test' requiring MySuper trustees to attest to outcomes promoting the financial interests of members on a broader range of indicators. APRA said it will consider issuing prudential guidance to support RSE licensees to comply with this expanded obligation.

Retirement products

Further to the 2016 Federal Budget announcements around retirement income streams, *Treasury Laws Amendment (2017 Measures No.1) Regulations 2017* was registered on 21 June 2017 and commences on 1 July 2017. These regulations finalise the following changes relating to income stream products:

- Innovative income streams – The regulations set out a new set of product requirements for deferred annuities (life time annuities that commence after a deferral period) and pooled investment pensions and annuities (products that are payable for the life of an individual, but with amounts based on the investment and longevity performance of a pool). The assets backing compliant income stream products would be tax-exempt if they are currently in payment or are held for an individual who has reached retirement.
- Capped defined benefit (DB) income streams – The regulations expand the definition of 'capped DB income streams' to allow pensions that cannot practically commute in response to the transfer balance cap to be subject to additional tax, instead of forced commutation.

2 apra.gov.au/Super/Publications/Documents/Letter%20to%20industry%20-%20IAMOIS%20Bill%20-%20APRA%20consequential%20changes.pdf

The registration of these regulations is a key step in the development of an expanded range of retirement products for members. 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.

In support of the Comprehensive Income Products for Retirement (CIPR) consultation process, the Behavioural Economics Team of the Australian Government (BETA) released a report titled *Supporting retirees in retirement income planning*[3] on 15 May 2017. The report examined member preferences and their comprehension and willingness to take up a CIPR, based on different presentations of information. A key finding of this study was that overall around 50% of surveyed members would be willing to choose a CIPR if it was offered to them—with disclosure format contributing significantly to the outcome.

A key component in the development of the CIPR requirement is the minimum product requirements, with the current proposal being[4]:

1. minimum additional level of income and/or guaranteed level of income
2. broadly constant real income for life
3. flexibility.

The Australian Government Actuary (AGA) released a paper[5] on 29 May 2017 outlining a possible actuarial certification test and process based on the proposed minimum requirements. The context of the paper was third-party certification as a possible model for regulatory oversight or authorisation of a CIPR. The proposed test specifically excluded the flexibility minimum requirement.

Given this is a new and complex area with a number of issues that need to be resolved, Treasury has allotted a reasonable amount of time for consultation. The initial submission deadline was April 2017 and then moved multiple times and finally closed on 21 July 2017.

In a preliminary overview of submissions to date, Treasury has noted the following:

› There is general agreement on the importance of the MyRetirement objectives;

› There is much confusion around the details i.e. there is a wide range of interpretations;

› There is lack of consensus on the best way to achieve objectives.

Treasury has also noted the following three significant issues that have been highlighted in the consultation process thus far:

1. desire for multiple MyRetirement products
2. who should/should not be offered a MyRetirement product
3. likely extent of take-up (trustees and members) and effectiveness of nudge.

In Russell Investments' submission to Treasury on the CIPR discussion paper, we noted the importance of investment outcomes for delivering an adequate retirement income that meets the stated CIPR policy objectives. An approach that compromises investment outcomes to deliver a benefit from mortality pooling may not be the best approach in aggregate. We believe that an approach that allows flexibility in the construction and forms of CIPRs and focuses on the overall outcome for individuals is likely to lead to the best results.

Subject to the views of government, further consultation is likely before the CIPR's framework is finalised.

Insurance in superannuation

Insurance within superannuation is increasingly becoming an area of interest from the government and regulators. This is not surprising given Death, TPD and Income Protection insurance cover is primarily provided through the superannuation system in Australia. Additionally, insurance claims handling by some large insurers has been an area that has received adverse publicity and retail insurance (generally outside super) has been subject to an independent review.

The Insurance in Superannuation Working Group (ISWG) was formed in November 2016 and contains representatives from funds, insurers, consumer groups and industry bodies, who will develop leadership on insurance and a Code of practice/conduct for life insurance in superannuation.

The key deliverable for the ISWG is to develop a binding Code of practice/conduct before the end of 2017. However, a number of working papers designed to improve industry practice will be progressively delivered throughout 2017.

It is intended that the Code will apply to Death, TPD and income-related (Income Protection or Salary Continuance) cover where available.

The ISWG previously released discussion papers on *Account balance erosion due to insurance premiums* (on 9 March 2017) and *Claims handling* (on 7 April 2017), which were summarised in our Q2 newsletter.

3 pmc.gov.au/sites/default/files/publications/Supporting-retirees-in-retirement-income-planning_0.pdf
4 Page 16-20. consult.treasury.gov.au/retirement-income-policy-division/comprehensive-income-products-for-retirement/
5 treasury.gov.au/PublicationsAndMedia/Publications/2017/Actuarial-Certification-Test

Member communication and engagement

The ISWG released its third discussion paper, titled *Member communication and engagement* on 5 May 2017. This paper proposes options to enhance member engagement and understanding of their insurance arrangements they have within superannuation. The proposals outlined were developed with the following objectives:

- Improving understanding of insurance by members through the use of consistent plain language and terminology;
- Increasing financial literacy in relation to life insurance to help enable better choices, which could include funds using behavioural economics and undertaking consumer testing;
- Delivery of more timely, targeted and relevant communication to members to ensure members have sufficient information to make informed decisions when they need it; and
- Providing easy access to insurance information, online resources, tools and education to facilitate member understanding of their insurance, their ability to alter or opt-out of their insurance cover and awareness of potential insurance cover limitations.

Data management

The ISWG released its fourth discussion paper, titled *Data management* on 27 July 2017. This paper focuses on improving access to timely and relevant information to improve member insurance outcomes. Better data management is likely to lead to better communications, greater capacity for informed decision making by members and superannuation funds and more robust pricing as the number of unknowns and assumptions made reduces.

The key proposals from this paper include:

- Development of Insurance Data Strategy and supporting Framework i.e. superannuation funds would have a documented strategy and framework, which gives due consideration to their insurance data requirements, process flows and systems;
- Development of data standard (with appropriate controls) be developed for the sharing of data between administrators, trustees and insurers; and
- Leverage SuperStream by making certain optional fields mandatory.

Productivity Commission review of superannuation system

The Productivity Commission is currently undertaking a three-stage review of the efficiency and competitiveness of the superannuation system. In November 2016, the Productivity Commission released its report on stage 1 which 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 released a draft report on stage 2 in March 2017. Stage 2 explored four alternative ways to allocate default members to superannuation funds, as well as setting out criteria to assess the various models (the key criteria being members' best interest). The final stage 2 report will be incorporated and finalised as a part of the stage 3 inquiry.

The terms of reference for stage 3 were released by the government on 30 June 2017. The review represents the third and final stage of the Commission's program of work in relation to a review of the efficiency and competitiveness of the superannuation system following the full implementation of the MySuper reforms. Stage 3 will use the criteria identified through the Commission's stage 1 study of how to assess the efficiency and competitiveness of the superannuation system, including the appropriateness of insurance arrangements. It will also make recommendations on default fund allocation models, developed as part of stage 2. The government has asked the Productivity Commission to complete the review within 12 months, with the draft report to be provided by January 2018.

The Commission released an issues paper, *Superannuation: Assessing Competitiveness and Efficiency* on 7 July 2017. The paper is designed to help superannuation participants in preparation of initial submissions to the inquiry. In its mandate, the Commission is to evaluate the accumulation, transition and retirement phases of superannuation, as well as the default, choice (including self-managed) and corporate fund member segments. Although not out of scope, defined benefit funds are not to be a key focus of the Commission's assessment.

Initial submissions are due by 21 August 2017.

Underpayment of Superannuation Guarantee

Superannuation Guarantee non-compliance has received significant attention over the last year or so.

On 1 December 2016, the Senate referred the matter of the impact of non-payment of the Superannuation Guarantee (SG) to the Senate Economics References Committee for inquiry. The Committee released its interim report on 11 April 2017 and its final report titled *Superbad: Wage theft and non-compliance of the Superannuation Guarantee* on 2 May 2017[6].

On the recommendation of the Committee, the Minister for Revenue and Financial Services has publicly released the multi-agency working group on SG non-compliance report[7], as well as the 2016 review by the Inspector-General of Taxation[8].

Evidence received by the Committee clearly indicates that a failure to adequately detect and address SG non-compliance causes long-term financial detriment to millions of Australian employees, significant competitive disadvantage to compliant employers, and an unnecessary impost to government finances through additional reliance on the age pension. In this regard, the committee is particularly concerned that the individuals most at risk of the negative impacts of SG non-payment often come from the most vulnerable groups in Australian society.

As you would expect, the underpayment of SG is partially due to deliberate non-compliance by employers and partially due to a range of other factors. Some of these factors included: system design and complexity, current salary sacrifice arrangements, misclassification of workers and industry/workforce characteristics.

From a monitoring perspective, there is an expectation the enhanced digital data capture (in particular, through the Single Touch Payroll project of the Australian Taxation Office or ATO) should lead to better SG compliance monitoring.

On 26 July 2017, the government released the *Treasury Legislation Amendment (Improving Accountability and Member Outcomes) Bill 2017: superannuation guarantee (salary sacrifice integrity measures)*. The Bill closes a loophole which was used by some employers to reduce their employee's superannuation guarantee when the employee chooses to make salary sacrifice contributions to superannuation.

Transparency and member engagement

RG97 disclosure

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 and additional look through of fees for interposed vehicles.

The initial date for RG 97 compliance for PDSs was 1 February 2017. However, on 29 November 2016, ASIC announced that the transition period will now end by 30 September 2017 for issuers that notified ASIC in writing, before 31 January 2017, that they intend to take advantage of this extension in relation to a PDS, and provided 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. It appears that most superannuation funds have taken advantage of the extension so the full impacts of RG 97 are not yet known.

There is some debate around the interpretation of these requirements and the level of impact on fees disclosures. In particular, superannuation funds that make greater use of certain types of interposed vehicles are likely to be disclosing higher fees.

The new disclosure standards required these additional disclosures to flow through to member periodic statements from 1 January 2018. However, on 23 June 2017 ASIC registered *ASIC Corporations (Amendment) Instrument 2017/569* amended *ASIC Class Order [CO 14/443]* to defer the first reporting date for these disclosure requirements from 1 January 2018 to 1 January 2020. Additionally, the ASIC instrument amended the Class Order to:

› defer the requirement to make a product dashboard publically available for a choice product for a further two years, until 1 July 2019; and

› extend the relief for certain notification requirements under the portfolio holdings disclosure regime to 1 July 2019.

6 aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/SuperannuationGuarantee/Report
7 treasury.gov.au/PublicationsAndMedia/Publications/2017/Superannuation-Guarantee
8 igt.gov.au/publications/reports-of-reviews/atos-approach-to-employer-obligations-compliance-activities/

Section 29QB Employer Sub-Plan disclosure

ASIC has revised its view on extending existing class order relief for elements of the disclosure requirements under *Superannuation Industry (Supervision) Act* Section 29QB, by issuing *ASIC Superannuation (RSE Websites) Instrument 2017/570*. Section 29QB required certain documents such as trust deeds, 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 to be available on RSE websites. The ASIC instrument provides relief from the requirements in legislation that apply to documents that relate to employer sub-plans.

The ASIC instrument replaces the previous class order [CO 14/509], and extends the relief for a further 12 months to 30 June 2018. Given significant stakeholder feedback, the government is considering the practical implications of applying Section 29QB to employer-sponsored sub-plans.

ASIC Report 529 Member experience in superannuation

On 30 June 2017, ASIC released *Report 529 Member experience in superannuation* outlining its feedback on some key disclosures and practices in the superannuation industry, based on recent ASIC projects and reviews, with a view to enhancing members' experience of and engagement with their superannuation.

The report has a heavy focus on the insurance component of superannuation, specifically the lack of adequate upfront and ongoing disclosure to members about insurance cover and the use of inappropriate defaults when transferring members between different divisions of funds. The report also covers product dashboards, calculators, branding and vulnerable consumers. As you would expect, ASIC expects trustees to take a consumer-focused approach and make their disclosures as effective as possible. The report makes a series of recommendations and sets out what it would expect from the superannuation trustees in relation to the identified issues.

The findings from this report will inform ASIC's 2017 compliance projects around 'Employers and Super' and 'Insurance in Super', as well as the Insurance in Superannuation Industry Working Group''s work around the development of a binding code of practice/conduct.

The report flags ASICs intention to take further regulatory action where it finds poor disclosure or it considers consumers are being poorly treated.

Single Touch Payroll

Single Touch Payroll is an ATO initiative whereby employers will report salary or wages, pay as you go (PAYG) withholding and super information electronically to the ATO directly from their payroll systems, at the same time they pay their employees.

Single Touch Payroll would be available on a voluntary basis from 1 July 2017 and would be compulsory for all employers with 20 or more employees from 1 July 2018. The ATO's current schedule has some functionality available for a small number of employers from 1 July 2017 with a wider rollout including additional functionality to occur later in 2017.

In June 2017, the ATO released a consultation paper on online choice of fund design (part of the employee commencement service)[9]. The ATO paper, which focused on employee commencement services sets out:

- background on the scope for new Single Touch Payroll Services supporting the commencement of a new employee (including the provision of pre-filled TFN declaration and choice of superannuation fund online forms);
- an outline of how the proposed draft principles will influence the design of the new choice of fund screens in ATO Online.

The key differences between the existing choice form and the new Single Touch Payroll ATO Online form is shown below.

Table 1: Existing choice form comparison with Single Touch Payroll Online form

	Existing choice form	STP employee commencement service (in ATO Online)
Details of member's existing super accounts	Not Provided on standard form provided by the employer to employee. Employee has to locate and add account details and may provide the wrong account identifier.	All existing super accounts for the employee are pre-filled and the member can choose. (SMSF accounts from 2018/19)
Details of employer's default fund	Pre-filled on standard form by the employer or provided separately to the employee as part of commencement process.	Not pre-filled in the current design. Has to be provided by the employer as part of a 'welcome pack' to their new employee.

9 Australian Taxation Office, Single Touch Payroll Consultation Paper

The proposed design for the ATO Online form will only show current superannuation accounts together with balances, insurance and recent contributions. Importantly, the ATO form will not show the new employer's default fund, citing the complexity in capturing this information from the employer. The employee would have to elect a generic employer default option within the ATO form, which will notify the employer to create a new default fund account for the employee. If this approach is adopted, employers would have to demonstrate the comparative value of their default fund as a part of their onboarding process.

Where an employer chooses to on-board an employee using their own business management software, the ATO will provide TFN and super choice pre-fill data.

Initial submissions closed on 25 July 2017.

The obligation to report superannuation payment information to the ATO is currently being reconsidered.

Tax Ruling: Income tax deductions to superannuation funds

The ATO has issued an addendum to *Taxation Ruling TR 93/17*, which relates to income tax deductions available to superannuation funds.

The updated ruling clarifies the income tax treatment of certain expenses incurred by a superannuation fund, such as actuarial costs, accountancy fees and the superannuation supervisory levy. It also provides further guidance on the apportionment of expenses between a fund's assessable and non-assessable income, including where extraordinary expenses are incurred or income is derived as a result of a merger.

Timeline of events

Timeframe	Event
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	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	Extension of earnings tax exemption to 'innovative' superannuation income streams
1 July 2017	Departing Australia Superannuation Payment (DASP) tax rate increased to 65%
30 September 2017	Updated fee and cost disclosure requirements apply to Product Disclosure Statements (for the majority of providers who have applied for the extended deadline of 30 September 2017)
1 January 2018	Updated fee and cost disclosure requirements to apply to periodic statements
Late 2017	Binding ISWG Code of Practice for insurance in superannuation to be released
1 July 2018	Employers with more than 20 employees required to use Single Touch Payroll enabled software for reporting PAYG withholding amounts and superannuation contributions to ATO
1 July 2019	Product dashboards to be publicly available for choice products (largest ten investment options only). Product dashboard to be included in periodic statements
31 December 2019	First reporting day for the portfolio holdings disclosure requirements
1 January 2020	Updated fee and cost disclosure requirements apply to periodic statements
1 July 2021	SG increases resume (9.5% to 10%)

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