

Transfer planning in superannuation: proposed enhancements

UNISUPER SUBMISSION TO APRA DISCUSSION PAPER

Superannuation transfer planning: Proposed enhancements

UniSuper welcomes the opportunity to provide feedback to APRA's Discussion Paper – Superannuation transfer planning: Proposed enhancements.

The proposed enhancements, while well intended, fail to effectively target underperforming funds, and funds that are most likely to be required to undertake a superannuation fund transfer (SFT). The use of a one-size fits all approach to transfer planning could result in members monies in well performing funds being used to undertake expensive tasks, such as preparatory steps, that they know will go unused. This requirement to dedicate resources to pre-position, is arguably not in the best financial interest of a member of a well performing fund.

We note Deputy Chair Margaret Cole's comments to the *Investment Magazine's Chair Forum* in March 2022 where she raised the issue of "bus stop" mergers, where small funds merge with small funds but fail to achieve sufficient viable scale. APRA has provided guidance that funds with assets under ~\$30 billion can face sustainability challenges, due to declining net cash flows and member accounts. Amending SPS 515 to ensure sub-scale funds cannot merge with other sub-scale funds, or funds with poor growth, immature risk, or governance functions, would likely deliver the Australian community with better retirement outcomes.

We strongly support APRA's growing focus on resolving underperforming funds and removing friction from the SFT process. We believe that incorporating the following into the proposed enhancements would result in a better outcome for the community:

- Set a clear performance requirement, greater than simply 'passing' the performance test to trigger transfer planning activities
- Use FUM, combined with growth, as a determining factor for ongoing viability and ability to survive periods of volatility
- Develop a register of destination funds which exceed the regulators expectations in terms of performance, risk, and governance
- Ensure funds likely to undertake an SFT are prevented from entering contracts with service providers that may complicate the transfer process.

Crucially, APRA must be aware that with any transfer there are multiple complex issues that must be overcome to facilitate an SFT. These issues can range from asset transition, administration and product readiness, member communications and servicing, capability, and experience.

As UniSuper just completed a successful merger with Australian Catholic Super (ACS), it is well placed and willing to provide the regulator with feedback based on recent practical experience upon request.

Should you have further queries, please contact Policy and Advocacy Specialist [REDACTED] via email at:

[REDACTED]

1. APRA proposes that all RSE licensees must regularly consider, and plan for, future circumstances that may necessitate a transfer of members into, and out of, the RSE licensee's business operations. Do you agree? If not, please provide views.

UniSuper agrees and supports APRA's position that a fund's level of readiness should be aligned to the level of perceived likelihood that a fund will be required to SFT. With ~\$115 billion under management, the potential destinations for UniSuper to transfer out to are limited. This makes the value of the proposed pre-positioning exercise questionable to large, well performing established funds. UniSuper, like many of its peers, has a mature risk function with a formal stress testing programme and valuation governance framework which includes the assessment of future circumstances. This programme arguably fulfils APRA's expectation that RSE licensees demonstrate credible planning to deal with circumstances that may necessitate a transfer of members.

While the policy is intended to ensure better outcomes for members, saddling funds which are performing well, by APRA's own measurements, with additional compliance exercises may not be in their members' best financial interest. Ultimately, the cost of the additional compliance artefacts and activities must be passed along to the member via fees.

The proposed enhancements could provide an opportunity to further incentivise better performance for underperforming funds, but misses a key opportunity to prepare the industry for further consolidation through the lack of focus on destination funds.

APRA should consider establishing an approved register of potential destinations for underperforming funds. This register should consist of funds deemed to be suitable in terms of scale and performance, both financial and operational based metrics should be utilised, to prevent underperforming small/micro funds merging with other small/micro funds which results in balance erosion and similar member outcomes.

It is necessary to always consider future circumstances, but APRA should also consider the potential impact on investment decision making and risk appetite prior to introducing the transfer planning requirements.

2. What are the minimum preparatory steps that an RSE licensee should take to be prepared for a transfer of members?

As outlined in our response to Q1, preparatory steps should be undertaken by RSE licensees that are underperforming or vulnerable to underperforming, due to scale or failing to meet the expectations of a peer regulator, for example ASIC or AUSTRAC.

Underperforming, or funds with insufficient scale, could be required to prepare a prospectus outlining their governance structure, assets, service providers and fund administrator arrangements. This prospectus, potentially held by APRA, could be provided to potential SFT destination funds either on request or following a pre-determined trigger such as failure of the performance test, or failure to meet the requirements set out in ASIC RG 271 Internal Dispute Resolution which could indicate a failure to fulfil its obligations to members. Also, as part of preparation of a prospectus, it could assist the underperforming fund discover any potential barriers to a transfer which can be removed, such as trust deed amendments where preparations can commence.

The preparation of a prospectus document would allow destination funds to assess the viability of a transfer in a shorter time, which could result in a reduction of legal fees (through fewer due diligence activities) and less of a disruption to members of the transferring fund.

APRA should continue to actively monitor the adequacy of performing funds stress testing programmes, which likely represents the most effective preparatory step to avoid being required to undertake an SFT.

3. How would an RSE licensee look to balance being adequately prepared for a future transfer of members without incurring undue cost?

RSE licensees should view pre-positioning for the potential transfer of members as an integral part of their best financial interest duty. The prudential regulator should provide distinct triggers to undertaking pre-positioning exercises which would incentivise performance and prevent funds from using member monies to prepare for transfers that will likely not occur.

Focusing on 'member fit' is crucial to performing a successful SFT, funds should consider how the profile of their members would fit with the existing members of the potential destination. As the best financial interest duty goes both ways, it is important that a determination of fit is made early in the process.

4. What performance indicators do RSE licensees use to identify where a transfer of members is required? Of these, which indicators would be of most concern, for example, relating to performance, sustainability, and service?

The regulator, APRA, should seek to provide greater clarity on when a fund should transfer members. This should arguably not be based on performance alone, and could incorporate considerations such as sustainability, growth (organic and non-organic) and retention of key staff.

Changing service providers can cover over sustainability issues and present a quick fix to performance and service issues. This relatively simple strategy could allow funds with potentially major issues to avoid exiting until a major event occurs.

5. What guidelines would support an RSE licensee to ensure appropriate due diligence is undertaken without resulting in undue cost and delays?

The current lack of guidelines around required activities, such as equivalency analysis, has added significant cost and risk to SFTs. While there is a clear need to protect transferring members, there needs to be an acceptance, demonstrated through facilitative regulatory settings, that they are transferring for a reason. Changes to the settings could include providing the right of action to the regulator exclusively to lower potential class action risk.

Insurance arrangements, at both the member and group level, remains opaque when a SFT occurs. Guidelines around uniform transfer, and cut off dates, would serve to de-risk the process for both funds and members.

6. In what circumstances would be an RSE licensee conclude that remediation of the RSE's business operations to improve member outcomes is not appropriate, necessitating a transfer of members?

If transfer planning activities are triggered, the assessment of whether to remediate or SFT should be undertaken by an independent third party while ultimate discretion should remain with the board. This assessment should focus on growth and ensure that the decision to transfer out is made prior to potentially expensive remediation activities, which can result in forced asset offloading.

7. Do you have any comments on the proposed requirements relating to the transfer of MySuper assets?

The proposed requirements for the transfer of MySuper assets are currently overly technical and lack considerations of how much it costs to move substantial amounts of FUM, or the impact on a fund if it were to transfer its MySuper product in isolation.

For many funds, transferring a MySuper product in isolation would likely leave a small amount of Choice monies or even Defined Benefit members. This would not be in the best financial interest of the small number of remaining members.

There may be some circumstances where it is feasible for only the MySuper product to be transferred (i.e., a fund where only one small product contains MySuper components). Consequently, we suggest that separate APRA requirements on the transfer of MySuper assets in isolation is not required but could be folded into the overarching Trustee transfer preparation. For example, as part of the preparatory steps considered under Question 2, the Trustee could consider whether it is feasible to transfer MySuper in isolation without material detrimental impact to other members.

8. What are the most significant barriers to a transfer of members, and how can the impact of these be reduced so that transfers are timely, orderly, and less costly?

There are numerous considerations when transferring members, these can include:

- Asset transition
- Data Migration
- Cyber Security
- Governance structures
- Product arrangement
- Harmonisation of system integrations and processes.

Directly addressing the risk these processes present to receiving funds, through the provision of temporary safe harbours, would likely represent the best way to directly address the duration and cost of transfers. There are barriers that have been raised by industry groups which require regulatory or legislative clarifications, including:

- If a transferring member has previously chosen Choice products in the old fund (non-MySuper), the law should be amended to make it clear that, following the SFT, new contributions made by that member can be allocated to whichever investment option their existing balance was transferred into (i.e., even if they have not specifically provided an investment Choice election to the new fund), or the decision should be placed at the trustee's discretion to choose an appropriate investment option. Alternatively put, the new trustee of the new fund should be able to rely on previous investment Choice elections provided by the old fund. This consistency should be extended to binding death nominations which can be deemed non-binding during the SFT process
- APRA could assist exiting trustees by providing regulatory comfort as to how quickly the trustee entity can be wound up following the SFT, thereby avoiding costs associated with ongoing ASIC and ATO lodgements, ongoing D&O insurance premiums, and the preparation and audit of financial statements and so forth
- While not the direct responsibility of APRA, stamp duty and CGT relief should be amended so that the entire SFT does not need to occur within the same financial year to be applicable
- Law reform is required to provide trustees with clarity that customary SFT indemnity arrangements do not violate overly broad State legislation against so-called corrupt benefits for trustees
- Create a standard exemption from the rollover rules under the SIS Regs either side of an SFT implementation date.

9. What additional guidance for transferring and receiving RSE licensees would assist timely, well executed transfers?

Certain issues remain outside of APRA's regulatory regime, such as the MySuper investment choice, and outside of APRA's control, such as the various State Crimes Acts.

10. Which parts of SPG 227 are particularly important to retain?

We do not believe it is critical to retain any parts of SPG 227 – Successor Fund Transfers and Wind-ups.

11. Has APRA sufficiently identified the critical components of the execution phase? If not, what is missing or inaccurate?

The execution phase of a SFT is arguably the most challenging and resource intensive period. A receiving fund needs to factor in multiple dynamic considerations. These considerations can include:

- Developing an asset register – funds don't just have FUM, they also have physical assets which can range from buildings to paintings to car leases to mobile phones
- Retaining key staff – key staff have elevated levels of institutional knowledge which make their retention key for a smooth integration, they can also have complicated employment agreements
- Servicing arrangements for member, employee, and employer experience as a key for retention - clearing house considerations, communications, data archiving
- Technology requirements.

About UniSuper

UniSuper is one of Australia's largest super funds with more than 500,000 members and close to \$110 billion in funds under management. With a heritage of supporting the higher education and research sector, UniSuper opened its doors to all Australians in July 2021.