Governance working group

Issues paper on superannuation complaints, death benefit nominations and other issues

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PROPOSED REFORM

This paper considers design and implementation issues flowing from the Government's Stronger Super package of reforms in response to recommendations of the Super System Review, in relation to such matters as insurance disputes and the handling of fund member complaints.

The proposed reforms would:

- provide fund members with longer time limits in which to make any complaints in respect of Total and Permanent Disability (TPD) insurance claims (recommendation 5.7);
- improve the regime relating to death benefit nominations to prevent unintended outcomes and minimise complaints in situations where members personal circumstances change after certain 'life events' (recommendations 5.14 and 5.15); and
- ensure members can obtain information about reasons for trustee decisions in relation to their formal complaints (recommendation 2.9).

The Government also announced that it would consult on:

- impediments to directors voting on trust company business (recommendation 2.8); and
- whether any practical conflict arises from the interaction of section 197 of the *Corporations Act 2001* and section 56 of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) (recommendation 2.10).

RATIONALE

As the Super System Review noted, most Australians do not have life or TPD insurance cover other than through their superannuation. It is therefore important from a governance perspective that the process of choosing insurance or making claims within the superannuation context is as fair, transparent and rational as possible. As part of this, the law surrounding death benefit nominations should not inadvertently cause inequitable outcomes where there are certain intervening circumstances.

The special public policy role of superannuation requires that members have confidence in the transparency of the superannuation system, and by extension, trustees be accountable to members for their actions. It is therefore appropriate that members be able to receive information about reasons relating to their complaints.

ISSUES

Issue 1 - TPD insurance complaint time limits

Recommendation 5.7 of the review was to amend the *Superannuation (Resolution of Complaints) Act 1993* (Complaints Act) to allow the Superannuation Complaints Tribunal (SCT) to consider complaints in respect of TPD insurance claims when the claim has been lodged with the trustee within six years of the member ceasing employment and the complaint has been made to the SCT within two years of the trustee's decision.

Currently, section 14 of the Complaints Act imposes certain time limits for making a complaint to the SCT about a trustee decision on a TPD claim. In particular, a complaint must be made to the SCT within a period of two years after the trustee makes the decision to which the complaint relates (subsection 14(6A)); and the claim must have been lodged with the trustee within two years after the person permanently ceases employment (subsection 14(6B)). Any change to the time limits in this space will therefore require legislative amendments.

Although not mentioned in recommendation 5.7, the Complaints Act also provides similar time limits with regards to retirement savings account (RSA) providers (subsections 15F(5) and (6)) and RSA insurers (subsections 15J(5) and (6)) with limits of one year for both the member to lodge a claim and to lodge a complaint to the SCT.

The general rationale for limitation periods has been elucidated by the High Court as follows:

- as time goes by, relevant evidence may be lost;
- it is oppressive to a defendant to allow an action to be brought long after the circumstances which gave rise to it have passed;
- limitation periods give certainty to people (especially businesses and insurers) in arranging their affairs and provisioning for their liabilities within a definite period; and
- the public interest requires that disputes be settled as quickly as possible.

On the other hand, there may be a number of valid reasons for delaying a claim for TPD benefits, for example, members may believe they will be rehabilitated and return to work, and thus do not want to have to repay benefits; or are receiving other benefits, such as 'Workcover'.

Furthermore, as noted by the review, the SCT is the only practical avenue for review of the trustee's decisions in relation to TPD benefits – as access to traditional court processes for these purposes is often prohibitively expensive and limited in scope of review.

In responding to recommendation 5.7, the Government provided its in principle support for the recommendation. The Government noted that time limits may affect claims and said that it would

consult with relevant stakeholders regarding appropriate limitation periods in which trustees and insurers can be liable.

Question 1.1 What, if any, unsatisfactory outcomes do the existing limitation periods produce?

Question 1.2 To what extent do claims proceed directly to the Federal Court because of time limits in the SCT's jurisdiction?

Question 1.3 What period for TPD claims would be appropriate, and would a longer 'tail' of liability create issues for trustees and insurers?

Question 1.4 What, if any, unsatisfactory outcomes do the existing limitation periods for RSAs produce?

Issue 2 – Death benefit nominations

Recommendation 5.14 of the review was to amend the SIS Act so that binding death nominations would be invalidated when certain 'life events' occur in respect of the member. The review suggested the current arrangements used by States and Territories under which testamentary dispositions are invalidated could be used as guidance for creating a single national model.

Subject to this, recommendation 5.15 was to amend the SIS Act so that binding death benefit nominations only have to be reconfirmed every five years, instead of every three years as required under current law.

Under current law, death nominations are effective until changed or revoked by members, or if they are not reconfirmed every three years. The review found that the current law can lead to inequitable outcomes when members forget to alter their nomination after a significant life event, for example, marriage or birth of a child. It suggested that such events should automatically invalidate binding nominations to prevent an inequitable outcome.

The Government supported the recommendation in principle and agreed to consider the recommendation further, noting the disparity of State and Territory approaches to the invalidity of testamentary dispositions.

The Productivity Commission's *Annual review of regulatory burdens on business: Business and consumer services* research report released on 12 October 2010 noted that the process of reconfirming nominations every three years can be unnecessarily burdensome on superannuation fund members and funds. As such, the research report recommended that the SIS Act should permit non-lapsing binding death nominations.

Self-managed superannuation funds (SMSFs)

Australian Taxation Office determination SMSFD 2008/3 (which is not legally binding) states that section 59 of the SIS Act and regulation 6.17A of the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations) do not apply to SMSFs. This means that the governing rules of a SMSF may permit members to make death benefit nominations that are binding on the trustee, whether or not in circumstances that accord with the rules in regulation 6.17A of the SIS Regulations. However, a death benefit nomination is not binding on the trustee to the extent that it nominates a

person who cannot receive a benefit in accordance with the operating standards in the SIS Regulations.

Question 2.1 What statutory framework would provide an appropriate template?

Issue 3 – Reasons for decisions

Recommendation 2.9 of the review was to amend section 101 of the SIS Act to require a trustee to provide a member with reasons for its decision in relation to the member's formal complaint.

The review intended this recommendation to address what it saw as a weakness in the trust law when applied to the context of compulsory superannuation - that traditionally, trust beneficiaries often cannot acquire information from trustees about decisions that affect beneficiaries' interests.

In responding to recommendation 2.9, the Government considered it appropriate for members to receive reasons for a decision on a formal complaint and said it would consult with relevant stakeholders to determine how best to require reasons in a way that balances the costs with the benefits.

Giving members reasons for decisions would assist in providing adequate transparency and promoting accountability amongst superannuation funds.

Possible models

In the financial services industry, dispute resolution mechanisms can be found within the relevant industry codes. For comparison, in the *General Insurance Code of Practice* released by the Insurance Council of Australia, section 6.9 provides that a dispute (defined as an unresolved complaint) will be responded to in writing with reasons given for the decision. Subtly, the *dispute resolution* stage should be differentiated with the *complaint handling* stage, where it is not necessary to provide reasons, except under special circumstances. Usually, a complaint becomes a dispute when it is reviewed or cannot be resolved at the complaint handling stage. This model to dispute resolution and complaints is broadly consistent across the various industry codes within financial services.

A prescriptive framework governing *how* reasons should be provided is exemplified by the *Administrative Decisions (Judicial Review) Act 1977* (ADJR Act), which imposes certain requirements on Commonwealth agencies and institutions (rather than private parties). Specifically, section 13 provides that the decision maker, on notice from an aggrieved person, would have to 'furnish a statement in writing setting out the findings on material questions of fact, referring to the evidence or other material on which those findings are based and giving reasons for the decision'.

Whilst the framework presented under the ADJR Act is not necessarily a suitable regime to adapt to private enterprise, it might nonetheless be illustrative of a level of accountability and transparency members might reasonably expect given the special public purpose superannuation plays and its significance to member's retirement outcomes. However, the precedent set through other industry codes suggests that this is a space more suitable for industry self governance, in a manner which balances the expectations of the member and the operational efficiency of funds.

Question 3.1 Would requiring a trustee to provide members with reasons for its decisions place unreasonable constraints on the trustee or unduly delay consideration of a member's formal complaint?

Question 3.2 Would an industry code of governance (such as the Code of Trustee Governance proposed by recommendation 2.18) provide an appropriate vehicle for promoting transparency in decision making?

Issue 4 – Other issues

Issue 4.1 – Voting prohibitions

The Super System Review recommended amending the Corporations Act so that any provision of a trustee company constitution that prohibits any trustee-director from voting on any trustee company business (other than in the event of conflict of duty or interest) is ineffective (recommendation 2.8).

The review noted that not all independent trustee directors have the right to vote on trustee company business under the terms of the company constitution.

While the review questioned the validity of such a provision, it suggested that it was important that all trustee directors be eligible to vote on all company business (subject to any conflicts).

The Government supported recommendation 2.8 in principle and committed to consulting with relevant stakeholders on impediments to directors voting on trust company business.

Question 4.1.1 What impediments are there to directors voting on trustee company business?

Issue 4.2 – Section 197 of the Corporations Act

The Super System Review recommended that section 197 of the Corporations Act should have no application to a director of a company to the extent that the company is acting as a trustee of a Registrable Superannuation Entity (RSE) (recommendation 2.10).

Section 197 generally makes a director liable for debts incurred by the trustee when the trustee cannot discharge the liability and is not entitled to be fully indemnified out of trust assets.

Section 56 of the SIS Act deals with the rights of the trustee to indemnity against the fund. The effect of section 56 is that the governing rules of a superannuation entity cannot preclude a trustee of the entity from being indemnified out of the assets of the entity in respect of any liability incurred while acting as trustee of the entity unless, in short, the trustee has failed to act honestly, or intentionally or recklessly fails to exercise care and diligence.

In the event of liability for trustees, the review stated that there appears to be a conflict between section 197 of the Corporations Act and section 56 of the SIS Act as to what a trustee’s right of indemnity encompasses. Therefore, the review recommended amending section 197 so that it does not apply to a director of a company to the extent that the company is acting as a trustee of an RSE.

While there may be particular cases where one section may impact on the operation of the other, it is unclear whether this is of any practical significance and therefore whether clarification of these provisions is necessary.

The Government did not support the recommendation, and said it saw no practical conflict arising from the interaction of the operation of section 197 of the Corporations Act and section 56 of the SIS

Act. While the Government did not support this recommendation, the Government committed to consulting with relevant stakeholders for clarity.

Question 4.2.1 Is there any practical conflict that arises from the interaction of the operation of section 197 of the Corporations Act and section 56 of the SIS Act?