SUBMISSION TO THE
PRODUCTIVITY COMMISSION

Default Superannuation Funds in Modern Awards

AUSTRALIAN INDUSTRY GROUP

5 April 2012

DEFAULT SUPERANNUATION FUNDS IN MODERN AWARDS

Introduction

The Australian Industry Group (Ai Group) welcomes the Productivity Commission's public inquiry into Default Superannuation Funds in Modern Awards. Ai Group is very well placed to provide input, given that we:

- Have been an active employer representative in industry superannuation funds for many years and have a particularly close association with AustralianSuper (and its predecessors);
- Have been registered as an industrial organisation of employers for more than 100 years and have a long history of playing a constructive role in the development of fair and productive awards;
- Were a party to more than 100 pre-modern awards in numerous industries;
- Have played a major role in key Tribunal and Court cases over the years relating to award superannuation; and
- Took a leading role on behalf of employers during the award modernisation process, and have an interest in most of the 122 modern awards.

Default funds in awards play a very important role. The majority of employees rely on the default superannuation system, despite having freedom to choose their own fund.

There are three main ways that default funds are selected by employers:

1. Most modern awards contain a list of default superannuation funds and where the award is applicable to an employer and its employees, the employer is able to select any listed fund as the default fund;

2. Employers and employees who have an enterprise agreement have the option of agreeing upon the inclusion of a default fund or a mandatory fund in their enterprise agreement; and

3. If there is no default fund specified in the relevant modern award or enterprise agreement, an employer can choose any eligible fund as the default fund.

In this submission, Ai Group expresses support for the retention of default funds in modern awards and proposes criteria and a process for the selection and ongoing review of such funds.

Superannuation as an award matter

There is a great deal of history associated with the inclusion of superannuation provisions in awards.

Developments in the 1980s were summarised in the Australian Industrial Relations Commission's (AIRC's) **Review of Wage Fixing Principles October 1993 Decision (Print K9700) as follows:**

> *"The provision of superannuation benefits emerged as an industrial issue of prominence in the Commission during the 1980s. This was, in part, the result of industrial disputation over superannuation and decisions of both the Commission and the High Court. In its judgement in Re The Manufacturing Grocers' Employees Federation of Australia and another; Ex parte The Australian Chamber of Manufactures and another [(1986) 160 CLR 341] in May 1986 the High Court made clear that the jurisdiction of the Commission in relation to disputes concerning superannuation was not as limited as had generally been thought.*
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> *In the National Wage Case decision of 26 June 1986 the Commission dealt with an application pressed by the ACTU that there should be awarded a 3% wage equivalent by way of superannuation contributions in satisfaction of an application for a 4% increase in wages and salaries. In the course of its decision the Commission identified a number of difficulties*

that attended the claim. The Full Bench did not accede to the claim but said that the Commission would be prepared to certify agreements or make consent awards dealing with superannuation subject to certain conditions. These included the contributions not involving the equivalent of a wage increase in excess of 3% of ordinary time earnings. A subsequent statement made by the President on 8 July 1986 said:

> *"The decision of the Commission of the 26 June 1986 clearly contemplates that discussions about the introduction and improvement of superannuation arrangements should take place.*
>
> *In particular, parties to awards of this Commission who agreed before the National Wage Case decision to negotiate following the decision, should continue with those negotiations. In these cases, if the talks break down it will not be necessary for direct action to take place before the assistance of the Commission will be available."*

The statement went on to identify what the Commission would expect in other cases.

The National Wage Case decision of 23 December 1986 again dealt with the issue of superannuation. The Commission rejected an application by the Confederation of Australian Industry that a moratorium be imposed on the implementation of the superannuation principle which had resulted from the June 1986 decision.

The question of how the Commission should deal with the issue of superannuation was further developed by the next National Wage Case decision of March 1987. That decision allowed, for the first time, for the arbitration for superannuation contributions, as part of the wage fixing principles of the Commission. The result could be two amounts, in aggregate, of a maximum of 3% to be phased in. The decision dealt with the submissions of the various parties including those of the Commonwealth whose submission was summarised as follows:

> *"The Commonwealth argued strongly for the need to introduce superannuation 'in a more rational and orderly fashion, without the level of disputation seen in recent times, and in a way consistent with current economic circumstances'. It proposed that the existing principle should continue to operate subject to the same conditions as at present but, in addition, the Commission should be prepared to arbitrate on a case by case basis where agreements cannot be reached. Any new or improved superannuation contributions flowing from such arbitration should be phased in." [Print G6800, p.21]*
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> *By 1989 the principles of the Commission allowed for the arbitration of superannuation contributions up to an amount equal to 3% of ordinary time earnings."*

In the late 1980s superannuation awards were made in many industries, e.g. the *Metal Industry (Superannuation) Award 1989*. These awards typically listed one or more industry funds and required that a three per cent superannuation contribution be paid into such fund if the employer was not already contributing at least this amount to an alternative superannuation fund approved under the relevant legislation.

The Superannuation Guarantee Legislation was introduced in 1992. As a consequence the superannuation provisions in awards became less important but they still had a significant effect by:

- Specifying funds into which contributions were to be paid;
- Defining the 'earnings base';[1] and
- Requiring employers to continue making superannuation contributions for up to a maximum period (usually 12 months) during workers' compensation absences.

[1] The ability for employers to apply less generous earnings bases in awards was removed from 1 July 2008 through an amendment to the Superannuation Guarantee Legislation.

In the **Review of Wage Fixing Principles October 1993 Decision (Print K9700) the AIRC called on the Government to convene a Conference of relevant industrial parties to address problems associated with the relationship between award superannuation and the Superannuation Guarantee Legislation. The Conference was chaired by the Treasury and held on 24 March 1994.**

Following the Conference and other developments, the AIRC decided to conduct a *Superannuation Test Case* to determine what provisions, if any, awards should contain in respect of superannuation. The *Superannuation Test Case Decision* (Print L5100) was handed down on 7 September 1994. The AIRC decided that awards would continue to contain superannuation provisions. The Commission also decided that in determining applications as to the specification of a fund:

- Any fund specified in an award must be one which meets the employer's obligations under the Superannuation Guarantee Legislation; and
- The Commission would have regard to the *Superannuation Industry (Supervision) Act 1993*. In particular, the requirement for equal representation of employers and members on 'standard employer-sponsored funds'.

In conjunction with the *Superannuation Test Case Decision*, the AIRC developed a Model Superannuation Clause which was included in many awards either through a specific variation or as a result of the Award Simplification process in 1997/98.

Award modernisation

During the initial stages of the award modernisation proceedings in 2008, the Full Bench of the AIRC heard extensive arguments about which, if any, default funds should be listed in modern awards.

The Full Bench also considered a submission made by the Minister for Superannuation and Corporate Law, Senator the Hon Nick Sherry, on 18 July 2008 which included the following proposal:

"Therefore, while strongly supporting the continuation of the nomination of default funds in awards, I urge the Commission to ask the parties to awards to consider the performance of the superannuation fund specified in their award when they conduct consultations for the award modernisation process."

During the award modernisation proceedings Ai Group adopted a neutral approach to the issue of default funds. We made no submissions on whether or not additional default funds should be listed in awards or on the criteria which should apply in determining which funds are listed.

The issue of default funds in awards was dealt with in a number of award modernisation decisions of the Full Bench. The following extract from the 2 September 2009 Award Modernisation Decision ([2009] AIRCFB800) includes relevant extracts from earlier award modernisation decisions and statements in 2008:

"SUPERANNUATION

[63] *We turn now to deal with the model superannuation clause and in particular to the question of default funds. The model superannuation clause provides that the default fund may be one of a number of funds specified in the clause or any fund to which an employer was making contributions for the benefit of employees on 12 September 2008. Some suggestions were made that the relevant date should be 1 January 2010 rather than 12 September 2008. It was submitted that this would minimise uncertainty and costs of compliance for employers and minimise negative impacts for employees. These submissions raise some fundamental issues concerning default funds which go beyond transitional provisions.*

[64] *The Commission's statement of 12 September 2008 contains the following passage:*

"[29] We have drafted a model superannuation provision to be included in modern awards if those awards deal with superannuation. The clause will nominate a default fund or funds should an employee fail to exercise his or her right to

nominate the fund to which employer contributions should be made. We do not think it is appropriate that the Commission conduct an independent appraisal of the investment performance of particular funds. Performance will vary from time to time and even long term historical averages may not be a reliable indicator of future performance. We are prepared to accept a fund or funds agreed by the parties, provided of course that the fund meets the relevant legislative requirements."

[65] *In its decision of 19 December 2008, the Commission, in commenting on the model superannuation clause, said:*

"[90] The terms of the exposure draft concerning the default fund provision were the cause of a number of submissions from employer and employee interests, from superannuation funds and the superannuation industry. We have decided to allow as a default fund any fund to which the employer was making contributions for the benefit of employees on 12 September 2008. This approach is likely to minimise inconvenience for employers. While funds other than those provided for will not qualify as default funds employees may still exercise their right to choose in favour of these funds."

[66] *In our view the nomination of default funds should be made on some readily ascertainable basis and one which does not lead to any disruption. For that reason it was decided to provide for named default funds as the primary basis. The secondary basis was any fund to which the employer was making contributions before 12 September 2008. That date was chosen because it was the date on which the exposure drafts of the priority modern awards were published.*

[67] *A number of funds have since made applications to be included as named default funds on the basis that the fund was nominated as a default fund in an award-based transitional instrument relevant to the coverage of the modern award or on the basis that the representatives of the main*

parties covered by the award consent. In our view either basis would constitute a good reason for the fund being specified as a default fund in a modern award. Where such grounds exist an appropriate application could be made. We do not intend to deal with such applications, however, in this decision.

[68] *Returning now to the proposal that we should change the relevant date from 12 September 2008 to 1 January 2010, and assuming the proposal could be characterised as a transitional provision, we doubt whether such a variation would go to the heart of the matter. Most funds voicing objection to the default fund provision did so on the basis that they are fundamentally opposed to any limitation on the ability of an employer to choose the default fund. Simply substituting one date for another would not remedy that complaint. Indeed, it might create a deal of disruption in the industry between the publication of this decision and 1 January 2010.*

[69] *The relevant legislation provides for default funds to be included in awards. Our present view is that we should continue to provide for default funds where there is a history of award regulation of superannuation in the industry or occupation the modern award covers. It should be emphasised, however, that, self-evidently, the default fund provision only operates where the employee does not nominate a fund. The superannuation legislation enshrines the right of an employee to choose the fund into which the employer should make contributions. Consistently with the legislation the award provision does not limit an employee's right to nominate a fund. Nor does it limit the ability of superannuation funds which are not default funds to market their products to employees and employers. We have decided, on the basis of what has been put in the proceedings, not to alter the date of 12 September 2008.*

(Emphasis added)

In a decision of 19 January 2010 ([2010] FWAFB 12), the Award Modernisation Full Bench made the following statement in determining an application to vary several awards re. Westscheme Pty Ltd:

> *"**[2]** The Full Bench decision of 2 September 2009 ([2009] AIRCFB 800 at para 67 indicated that there were two grounds upon which a fund could be considered for inclusion in a modern award; where the fund was nominated as a default fund in an award-based transitional instrument relevant to the coverage of the modern award (eg. a Notional Agreement Preserving a State Award (NAPSA) or a federal award) or where the representatives of the main parties consented."*

Since the above Full Bench decisions were made, various individual Members of Fair Work Australia (FWA) have applied the above criteria in determining applications made by particular funds to be included as a default fund in modern awards.

Criteria for selecting and reviewing default funds in modern awards

In this section of our submission, criteria are set out for:

- Reviewing existing default funds in modern awards; and
- Selecting additional default funds in modern awards.

Such criteria will ensure that there are strong protections for employees, without imposing an unreasonable regulatory burden upon employers.

It is essential that employers be able to choose any of the funds listed in the relevant modern award as the default fund, as is currently the case. Employees have the right to choose a superannuation fund. For employees who do not exercise choice, it is appropriate that the employer select the default fund from those listed in the award.

Reviewing existing default funds in modern awards

It would not be logical, and would be very disruptive for employers and employees, if an existing default fund in a modern award was not retained in the award if the fund continues to meet appropriate criteria. We propose the following criteria:

1. ***The fund has met the requirements of the MySuper legislation***

   The *Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2011* is currently before Parliament. This Bill would require that:

   - Employers make superannuation guarantee contributions on behalf of employees who have not exercised choice, to a superannuation fund that offers a MySuper product; and
   - Funds pay the contributions of members to a MySuper product unless a member has elected, in writing, for contributions made on their behalf to be paid to a specified choice product.

2. ***The fund has complied with legislative and regulatory requirements and maintained appropriate governance standards***

3. ***The fund has an acceptable fund performance***

   It is proposed that 'acceptable fund performance' be defined as performing in the top three quartiles over the previous five years based on returns to members net of costs.

4. ***The fund does not permit automatic 'flipping'***

   A fund that is included in a modern award as a default fund should not contain clauses that involve the *automatic* transfer of an employee's account into another MySuper product when the employment relationship with the current employer ceases (or under other circumstances). Any such 'flipping' should only be able to occur with the express consent of the employee (or former employee) and following a transparent disclosure of any change in fees, investment strategy and the like. Unless a criterion like this is included, it will be relatively easy to circumvent the purpose of having criteria aimed at protecting the best interests of the superannuant.

Selecting additional default funds for modern awards

Ai Group proposes that FWA have regard to the following criteria when selecting additional default funds for modern awards:

1. ***Whether the fund was nominated as a default fund in an award-based transitional instrument relevant to the coverage of the modern award***

   This criterion was determined by a Full Bench of the AIRC and is currently being applied by FWA.

2. ***Whether the representatives of the main parties covered by the award consent to the fund being listed in the award***

   This criterion has been determined by a Full Bench of the AIRC and is currently being applied by FWA.

3. ***Whether a substantial proportion of the employees in the industry or occupation covered by the modern award are an existing member of the fund***

   This is an important criterion. It would not be appropriate to have a large number of default funds in an award, as this would increase complexity for employers and employees.

4. ***Whether the fund had complied with legislative and regulatory requirements and maintained appropriate governance standards***

5. ***Whether the fund had an acceptable fund performance***

   See page 11 of this submission.

6. Whether the fund permits automatic 'flipping'

See page 11 of this submission.

Process for selecting and reviewing default funds in modern awards

Under section 156 of the *Fair Work Act 2009,* FWA must review modern awards every 4 years. The 4 Yearly Reviews would provide the ideal opportunity for the default funds in modern awards to be reviewed.

It would be beneficial to amend section 156 to include a new subsection (6) setting out the requirement upon FWA to review the default funds.

At the time of each 4 Yearly Review, APRA should give a report to FWA providing information in a standard format about fund performance, regulatory compliance and other relevant matters about each default fund listed in a modern award.

Flexibility should be provided for a fund to be removed from a modern award between 4 Yearly Reviews in exceptional circumstances, e.g. where the fund failed to meet legislative and regulatory requirements.

Default funds in enterprise agreements

It is not uncommon for an enterprise agreement to specify:

1. A default fund into which superannuation contributions will be paid if an employee does not choose their own superannuation fund;
2. A single fund into which all superannuation contributions will be paid; or
3. A choice of, say, two funds where all superannuation contributions will be paid.

Ai Group supports the retention of all of the above options. It is common for agreements to include provisions about superannuation and it would not be logical to permit parties to negotiate about other aspects of superannuation but not the specification of funds.

Option 1 enables an employer and its employees to reach agreement on a default fund and to specify that fund in an enterprise agreement. There is no merit in preventing the parties reaching agreement over this issue during bargaining.

With Option 2, the employees are in effect exercising their choice collectively when they vote to approve the enterprise agreement. This argument was pursued by Ai Group when the *Superannuation Legislation Amendment (Choice of Superannuation Funds) Bill* was being developed between 2002 and 2004. The argument was accepted by the Government at the time, and the argument is equally valid today.

Option 3 has merit for the same reason as Option 2.

Insurance

Insurance is an important element of superannuation for members. The diversity of occupational conditions and risks makes it an element that is best considered in the context of the industries and occupations covered by awards. This diversity of experience is an example of how, under existing arrangements, default funds whose governance arrangements include representatives of the relevant employers and employees are in a very good position to assess appropriate insurance offerings.

Conclusion

Default funds in modern awards play a very important role and need to be retained.

Ai Group has proposed criteria and a process for the selection and ongoing review of default funds in modern awards which we urge the Commission to adopt within its recommendations.