

THE HON T F BATHURST
CHIEF JUSTICE OF NEW SOUTH WALES
OPENING REMARKS, LAW COUNCIL OF AUSTRALIA
SUPERANNUATION LAWYERS' CONFERENCE
SUPERANNUATION GOVERNANCE REFORM: RADICAL
DEPARTURE OR MORE OF THE SAME?
SYDNEY
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1. I was going to open with a joke about superannuation – but I've been told to save it for later...Sorry to test the limits of your humour at this early hour of the morning but I couldn't resist. Welcome and thank you for inviting me to open the *2013 Superannuation Lawyers Conference*.
2. The title for this year's conference is "Safe Harbour or a Bridge too Far?". While Sydney is no doubt an appropriate location for this theme, I suspect the choice of title has less to do with our proximity to the water and more to do with the far reaching effects on the Superannuation Industry of recent legislative amendments. Those amendments implement the Stronger

Super Reform package and Future of Financial Advice (“FOFA”) reforms and will take effect in the middle of this year.

3. Superannuation has been the subject of significant government and media interest in recent years and, as the current political debate around concessions shows, that is unlikely to change any time soon. It is important to remember the context in which this scrutiny takes place. There is a consensus in this country that superannuation is a necessity. That consensus has led to the superannuation system becoming a national institution of immense importance. APRA estimates that Australia’s superannuation assets are now worth \$1.4 trillion,¹ roughly equal with GDP. This is expected to increase to \$6.2 trillion by 2036.² Superannuation represents an important contribution to national savings and provides significant capital to financial markets.

4. Far more importantly, the superannuation system is essential to ensuring that the minimum needs of older Australians are met and that individuals are able to plan for a secure retirement

¹ http://www.apra.gov.au/mediareleases/pages/12_21.aspx

² Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012, Second Reading Speech, House of Representatives (16 February 2012) at 1575.

through prudent investment. This will become all the more important in coming years, as we face an increasingly ageing population. Only the very rich, or the extremely poor, can avoid making some provision for retirement. The alternative of course is to avoid retiring altogether. That to my mind has many benefits, although I'm not sure that those who have to put up with working with me would agree. In any case I fear I have been thwarted by that pesky statutory judicial retirement age.

5. I make these general observations to emphasise that we should neither regard our superannuation system as inevitable nor underestimate its importance – although I suspect I am preaching to the choir in that respect. As you are all aware, our current system is the outcome of government policy and has a particular social purpose, which is of critical importance to every working Australian. It is in that social and economic context that reforms affecting the superannuation industry should be considered.

6. As in previous years, this Conference brings together many learned speakers, from the judiciary, academia, regulators, private practice and the superannuation industry, and covers all

regulatory issues in what is one of the most significant areas of corporate and legal life. The implications of the recent amendments to the *Superannuation Industry (Supervision) Act* 1993 will no doubt be at the forefront of many of these discussions. In that context, the conference provides an extremely valuable overview of the duties of directors and trustees, having regard to the recent reforms, the present and likely trends in regulation, and the way this will affect corporate governance and administration.

7. In one sense, I was embarrassed about speaking on the issues the subject of this conference, being a sitting judge. However I am consoled that most actions pertaining to the conduct of superannuation trustees will end up in the Federal Court. I take particular fortitude from the fact that Acting Justice Sackville seems to have no hesitation in presenting.

8. I do not want to pre-empt anything that Justice Sackville or Bob Austin will be saying about the duties of trustees or directors. If I did I would probably get it wrong and provide them with the perfect opportunity to show me up. However, I would like to take this opportunity to pose a few questions about the operation of

the amendments introduced by the Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act.

9. Over the past months there has been a lot of discussion and genuine concern about how the new duties on trustees and directors will affect the superannuation industry. Much of this apprehension stems from confusion about how the amendments will change the obligations of trustees and directors in practice.

10. On the one hand, the new covenants do not seem so different to those contained in the *Corporations Act*, the *Superannuation Industry (Supervision) Act* as it currently stands, and those imposed by trust law. However, the context for the amendments, including the Cooper Report's recommendations and the legislature's expressed intention, clearly suggests that the amendments are intended to not only clarify the duties of trustees and directors, but also to impose additional and more stringent obligations.

11. Read against that background, it is far less clear whether the new covenants merely tweak current obligations, or provide for a radical departure from accepted principles of trust law and directors duties. It is not for me to make that determination, but I would like to use the time available to me this morning to point to a few of the new obligations which appear particularly ambiguous and the issues which courts will face in interpreting them.

12. First, the amending legislation creates a number of new duties on trustees in relation to default investment “MySuper products”. Notably, a new section 29VN requires trustees of superannuation funds providing a MySuper product to “promote the financial interests of the beneficiaries of the fund who hold the MySuper product, in particular returns to those beneficiaries (after the deduction of fees costs and taxes)”.³ The rationale for this new obligation is outlined in the Bill’s Second Reading Speech, where it is stated that the additional obligations attaching to trustees in this respect “reflects that these

³ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012 s 29VN(a)*

members have effectively delegated all decisions for their superannuation to the trustee”.⁴

13. It is plainly the expressed objective of the legislature to increase protection in this area. However, it is ultimately courts and legal advisors who will have to interpret the words “promote financial interests”. This will not necessarily be easy. The word “promote” is not generally used in the lexicon of trustees’ duties, as distinct from the well known phrase “act in bests interests of”, which in relation to a general investment power takes into account the beneficiaries’ position, as well as the purpose and object of the trust. To “promote” interests seems to imply taking active steps to advance the financial interests of beneficiaries. That may be possible in the context of individual beneficiaries with specified investment allocations – at its simplest by adopting traditional growth, balanced or conservative investment strategies – but there is a real question as to how one “promotes financial interests” in the context of a default investment option.

⁴ Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012, Second Reading Speech, House of Representatives (16 February 2012) 1575

14. Even if beneficiaries are placed into one of the investment strategy categories I have referred to, that does not mean that steps taken in investing within that particular asset allocation will necessarily advance the financial interests of individual beneficiaries. Indeed trustees of large superannuation funds will not generally know the identity of individual beneficiaries, much less their individual financial circumstances. Section 29VN will presumably have to be interpreted having regard to that fact. Second, section 29VN is described, at least in the Second Reading Speech, as an “additional obligation”.⁵ Even within the context of broad investment strategies, trustees currently have a wide discretion about how to invest. Under the new covenant, trustees will have an obligation to promote returns to beneficiaries. Does this mean that trustees who adopt a safe investment option with relatively lower returns, rather than a more aggressive stance, could be held to have contravened their obligations under section 29VN? Significantly, the defence currently available in section 55(5), namely that the investment was made “in accordance with an investment strategy formulated under a covenant referred to in paragraph 52(2)(f)”,

⁵ Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Bill 2012, Second Reading Speech, House of Representatives (16 February 2012) 1575

has been repealed and what appears to be a significantly more limited defence substituted.

15. Issues of interpretation will also arise in relation to the new general covenants under section 52. For instance a new obligation on trustees has been created to act fairly in dealing with classes of beneficiaries, and beneficiaries within a class.⁶ On one, no doubt dominant view, this obligation may do no more than codify a trustee's duty of impartiality, which has sometimes been expressed as requiring trustees to act "fairly".⁷

16. However, the use of the word "fair" could also be seen to invite parallels to the complaints mechanism under the *Superannuation (Resolution of Complaints) Act 1993*, pursuant to which members can challenge the decision of a trustee before the Superannuation Complaints Tribunal on the basis that it was unfair or unreasonable.⁸ In that context the focus of the enquiry is on the operation of the decision on the applicant, rather than the fairness of the process by which the decision

⁶ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012* s52(e)-(f)

⁷ see Heydon & Leeming, *Jacobs' Law of Trusts in Australia* (2006, 7th ed) at [1711].

⁸ *Superannuation Resolution of Complaints Act 1993* s 14

was arrived at.⁹ As the new trustee covenant imposes an obligation to *act* fairly, it is hard to see how it could direct attention to outcomes. Nonetheless the expression as it stands is ambiguous. In addition, no guidance as to the meaning of “fairness” is provided by the Cooper Report, Second Reading Speech, or the Explanatory Memorandum to the Amending Act. It may perhaps have been preferable to maintain the traditional duty of impartiality.

17. The newly imposed covenant on trustees to “give priority to the duties to and interests of...beneficiaries” in circumstances of conflict also presents some difficulties.¹⁰ The obligation appears to be framed very differently from the fiduciary standard at general law, which requires a person to avoid conflicts except with the informed consent of the beneficiary. On the one hand the express contemplation that trustees may continue to act in circumstances of conflict could be seen as a retreat from fiduciary standards. On the other, the related obligation to “ensure that the duties to beneficiaries are met despite the

⁹ *Pope v Lawler* (1996) 41 ALD 127 at 134

¹⁰ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards)* Act 2012 s 52(2)(d)(i)

conflict” and that their “interests...are not adversely affected”,¹¹ may suggest an outcome based duty foreign to fiduciaries’ traditional obligations, which could arguably increase trustees’ exposure to liability. APRA’s power to make prudential standards in relation to conflicts may provide some guidance in this area.¹² However, ultimately the courts will have the essential and difficult role of clarifying how trustees are to behave in situations of conflict and the extent to which this should be informed by the standards imposed on fiduciaries under general law.

18. I have already mentioned section 55(5). Given the title of this conference, it would be remiss of me not to consider this section, which has been said to provide a “safe harbour” to trustees, in more detail. The amendments to this provision are somewhat curious. It is said that the section operates as a defence to loss or damage, but in its newly amended form it is only available if the trustee has complied with all covenants imposed by the Act relating to investment. I cannot help but

¹¹ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012 s 52(2)(d)(ii)-(iii)*

¹² *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012 s 52(2)(d)(iv)*

wonder how, in those circumstances, there can be a cause of action.

19. I do not mean that facetiously. It is difficult to see how section 55(5) will in fact work. Regardless of any legislative defences, a trustee, or person acting on the trustee's behalf, will not be liable for loss or damage suffered by a person as a result of the making of an investment, unless it has breached one or other of the covenants that apply to investment. Put another way, applying general equitable principles of causation, there must be some causal link between the breach and the loss.¹³ However, if the person who suffers loss *can* establish breach and causation, s 55(5) can have no operation, its availability being predicated on there being no breach.

20. The High Court has in recent times emphasised that construction begins and ends with the words of the section. In those circumstances, it will be interesting to see how courts grapple with the changes to the relatively calm waters of s 55(5).

¹³ *Re Dawson* [1966] 2 NSW 211 at 215; *YouYang Pty Ltd v Minter Ellison* (2003) 212 CLR 484 at [44]

21. The legislative amendments to the duties of directors of trustee companies may also have significant implications. Pursuant to section 52A, directors will now be required to exercise the degree of care, skill and diligence that a prudent superannuation entity director would exercise if the director was the director of the trustee, and that trustee made investments on behalf of beneficiaries.¹⁴ A “superannuation entity director” is defined as someone whose profession includes being director of a corporate trustee of a superannuation entity.¹⁵ Apart from being quite a mouthful, this amendment effectively requires all directors to exercise the degree of care, skill and diligence of a professional superannuation director. As noted by Justice Ashley Black speaking extra-curially, the new requisite standard appears to be wholly objective, without regard to the skill, experience or financial qualifications of the director and without distinguishing between the roles of executive and non-executive directors.¹⁶

¹⁴ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012 s 52A(2)(b)*

¹⁵ *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012 s 29VO(3)*

¹⁶ see Black J “Simply Super: Understanding the Impact of Recent Cases on Directors Duties” (24 February 2012) at 4.

22. These issues are of considerable importance. Increased and unclear regulation places a greater burden on trustees. Ambiguity as to obligations and changes to the potential liability of trustees and directors are also likely to increase compliance and professional indemnity insurance costs. These costs will ultimately be borne by members.

23. None of this is to suggest that there should not be changes to the obligations of trustees or indeed directors. We are now dealing with the retirement plan of a nation - a very different position from the management of the interests of a third generation wealthy UK landowner. Different strategies, requirements and regulatory regimes are necessary to cope with this fact. Although I have focussed on trustees' and directors' obligations, the evolving roles and duties of financial advisers, lawyers and accountants will also be extremely important in this context.

24. However, one imperative common to all actors within the superannuation industry is that the obligations placed on them are clear and well understood. In that context, while I would not necessarily say that the recent Stronger Super and FOFA

reforms are “bridge too far”, perhaps the path across the water is a little shrouded in mist.

25. What this means is that the presentations you will hear and discussions you will have over the course of this conference are all the more important. The Superannuation Committee of the Law Council of Australia is to be commended for once again providing this valuable - indeed essential - opportunity. It is my pleasure to formally declare this conference open. I wish you all the best for the coming two days.