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Dear Director

Herbert Smith Freehills Kramer Submission – Consultation on enhancing member protections in the superannuation system

1 Introduction

This submission is made by Herbert Smith Freehills Kramer (**HSF Kramer**) in response to Treasury Consultation Paper *Enhancing Member Protections in the Superannuation System* (dated 7 April 2026) (**Consultation Paper**). All views set out in this submission are the views of HSF Kramer and not that of any other party.

HSF Kramer is an international law firm with 26 offices located around the globe. Among other things, it specialises in financial services, including in relation to superannuation, asset and wealth management, and financial services regulation.

This submission is structured by reference to the proposals set out in the Consultation Paper. In our view, while the proposals reflect a well-intentioned response to concerns arising from the collapse of the Shield and First Guardian funds (**Shield/First Guardian Collapse**), we are concerned that they (a) duplicate existing regulatory regimes intended to respond to the same, or substantially similar, concerns; and (b) create new regulatory burdens without properly addressing the root cause of Treasury's concerns. We are also concerned that the proposals may be inconsistent with the policy imperatives of Government with respect to the affordability and accessibility of financial advice, member agency, superannuation portability, and transition to retirement for Australians.

Our submissions in respect of each proposal can be summarised in the following terms:

(a) **Proposal 1**: Having regard to the existing framework of the *Corporations Act 2001* (Cth) (***Corporations Act***), we consider that:

(1) it is unnecessary to define 'Platform Trustee' and 'Platform RSE'; and

(2) the (four) 'Options' aimed at creating an uplift in Platform Trustee governance standards replicate existing obligations, create an additional layer of regulatory complexity and do not directly address the failures that underlay the Shield/First Guardian Collapse.

We consider that a more effective approach to address such failures would be by way of targeted supervision and sustained enforcement of existing obligations.

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(b) **Proposal 2**: We do not express any view upon the merits of Proposal 2 other than that it would be desirable to align the penalties regimes existing under the *Corporations Act* and the *Superannuation Industry (Supervision) Act 1993* (Cth) (***SIS Act***), where appropriate, in order to reduce regulatory complexity and improve consistency of penalties for the same or similar conduct.

(c) **Proposal 3**: This proposal is unlikely to provide members with further protections beyond those already provided by the 'cooling off' regime in the *Corporations Act*. A better approach to protect members from inappropriate super switches would be for ASIC to further utilise its enforcement powers against financial advisers who instigate inappropriate superannuation switching. However, notwithstanding the fact that scam activity was considered to be beyond the focus of the Consultation Paper, we are supportive of a proposal which extends the time in which trustees must action rollover requests where fraudulent or scam activity is reasonably suspected.

(d) **Proposal 4**: We are concerned that this proposal would limit access to financial advice at a time where access to such advice is already under pressure. Again, we consider that sufficient mechanisms already exist for ASIC (under Part 7.7A of the *Corporations Act*) to regulate the financial advice industry, without banning fee charging for specific forms of advice. In our view, better targeted enforcement action would balance the competing objectives of access to advice and ensuring that such advice is appropriate for consumers.

(e) **Proposal 5**: We are concerned that the proposed design of Option 5.1:

(1) requires trustees to maintain two distinct pools of financial resources that are aimed at addressing substantially similar and overlapping risks; and

(2) removes the decision of when to compensate members for certain losses from the responsibility of the trustee, notwithstanding the fact that the trustee will be best placed to consider the relevant circumstances and make this decision on an informed basis.

While we are supportive of proposals to address the legitimate issues exposed by the Shield/First Guardian Collapse, we believe that the existing regulatory frameworks within the *Corporations Act* and *SIS Act* already address the issues raised by Treasury in the Consultation Paper.

2 Proposal 1: Strengthening 'Platform Trustee' governance requirements

2.1 Summary of proposal

Proposal 1 is designed to address the perceived need for uplift in Platform Trustee governance standards. In this context, a 'Platform Trustee' is defined to mean any Registrable Superannuation Entity (**RSE**) licensee that is the trustee of a 'Platform RSE' – being, in turn, an RSE that offers one or more products through which members may directly 'construct a bespoke superannuation portfolio ... from a wide and diverse menu of investment options' (Consultation Paper at page 11). The Consultation Paper seeks to achieve the desired governance uplift – and thereby reduce 'the risk of catastrophic loss of a member's superannuation interests particularly in cases of fraud relating to the underlying product' (Consultation Paper at page 17) – in four different ways.

First, by requiring Platform Trustees to set and enforce holding limits on investment options – whether on a 'principles-based' or 'prescriptive' basis – to ensure that members hold adequately diversified portfolios and are not over-exposed to products that may experience 'catastrophic failure'.

Second, by introducing a codified due diligence obligation that defines what constitutes prudent initial due diligence in a platform context (such as maintaining a documented onboarding framework, applying consistent product assessment criteria, and retaining evidence of how onboarding decisions were reached).

Third, by restricting certain conflicted arrangements and payments – including listing fees, rebates, and volume-based incentives – that may compromise a Platform Trustee's independence and create incentives misaligned with member outcomes.

Fourth, by restricting the 'trustee-for-hire' (**Trustee for Hire**) model (and similar arrangements where governance may be separated from product operation), with proposed options ranging from targeted operating conditions to outright prohibitions on the model.

2.2 Issues with proposal

Proposal 1 is, by its terms, predicated upon the establishment of 'clear, accessible definitions' for two expressions – 'Platform Trustee' and 'Platform RSE' – that would 'enable Government to more precisely target reforms to the parts of the system most closely associated with the primary issues highlighted by the Shield and First Guardian collapses' (Consultation Paper at page 11). In our view, such reform is unnecessary and unlikely to achieve the stated intention. That is particularly so when regard is paid to the existing legislative regime that governs 'platform operators'.

The legislative framework which governs the provision of financial services in Australia has been variously described as 'porridge', 'tortuous' and 'labyrinthine' – a product of, at least in part, its 'extreme' and 'inconsistent' use of defined terms.[1] To this end, we note that the *Corporations Act* already regulates 'platform operators', being any financial services licensee or RSE licensee that is, or offers to be, the provider of a 'custodial arrangement' (s 964 of the *Corporations Act*). A 'custodial arrangement' is, in turn, defined to mean any arrangement under which a client may instruct the acquisition of a financial product, with the acquired product being held on trust or otherwise giving rise to rights, benefits or a beneficial interest for the client or another nominated person (s 1012IA(1) of the *Corporations Act*).

In our view, the existence of this framework, alongside the fact that all APRA-regulated superannuation trustees (i.e. including platform trustees) are currently governed by the same framework, obviates the need for any new platform-specific regime. To layer an additional regime over the existing legal and prudential framework would be, at best, duplicative and, at worst, a source of (further) regulatory uncertainty.

We also note that definitions which allow for the implementation of 'targeted obligations that apply only in platform contexts' (Consultation Paper at page 11) are, fundamentally, at odds with the 'principles-based regulatory approach' of the *SIS Act*, which is designed to facilitate effective, fit for purpose and flexible regulation in a constantly evolving industry with participants of vastly different shape and scale.

Beyond these definitional issues, each of the proposed 'options' for reform are inhibited by various difficulties in design – for example:

(a) the imposition of mandatory holding limits (Option 1.1) is inappropriate, as many investments offered through a 'Platform RSE' are adequately diversified so as to not warrant the imposition of a holding limit. While an express obligation to consider whether holding limits should be applied is not objectionable, this is in

[1] Such was the view of the Australian Law Reform Commission in 'Confronting Complexity: Reforming Corporations and Financial Services Legislation' (Final Report, Report No 141, November 2023) at, for example, 63 [2.43].

our view inherent in a trustee's general obligation to formulate an investment strategy for the whole of each fund and, in any event, is reflective of industry better practice and codified through industry standards as an expectation of Platform Trustees[2]. The relevant issue which arose in the Shield/First Guardian Collapse was not the absence of holding limits, but rather alleged failures to *enforce* holding limits that had been set by the relevant trustee. The Consultation Paper itself identifies (at page 18) that 'one trustee in Shield and First Guardian [allegedly] failed to enforce a 50 per cent holding limit it imposed for First Guardian and failed to have systems and processes in place to ensure that there was compliance with that holding limit'. To this end, we consider a more productive solution would involve more focused supervisory oversight of the implementation and enforcement of self-imposed holding limits by trustees (i.e. as part of a trustee's *SIS Act*-mandated investment governance framework). We note that such a solution would also avoid the arbitrariness involved in defining/prescribing mandatory holding limits across a diverse market. We further note that imposing holding limits on Platform Trustees and not other types of trustees would create an uneven 'playing field'. It is common practice for funds that would not be considered to be 'Platform RSEs' to offer single sector options and other types of options with limited in-built diversification;

(b) the introduction of codified due diligence requirements (Option 1.2) and restrictions on conflicted arrangements (Option 1.3) are largely duplicative of the existing legislative regime.

In relation to due diligence requirements, we note that due diligence obligations are imposed upon superannuation trustees by the 'investment covenants' in section 52(6) of the *SIS Act* (see, more generally, ss 52(2)(b) – (c) of that Act). Similarly APRA Prudential Standard SPS 530 *Investment Governance* (**SPS 530**) already requires RSE licensees to 'ensure that effective due diligence that is commensurate with the nature and characteristics of the investment is undertaken prior to the selection of an investment for an investment option'.[3] While additional due diligence requirements could be accepted, care would need to be taken to identify what additional actions are required of a trustee beyond the existing obligations under the *SIS Act* and SPS 530. To our minds, such additional obligations could, in any event, be more appropriately dealt with by APRA through amendments to SPS 530 rather than by way of legislative change.

In relation to conflicted arrangements, we note that Chapter 7 of the *Corporations Act* already prohibits '[t]he receipt by platform operators of volume-based benefits to the extent that such incentives are merely a means of product issuers or fund managers 'purchasing' shelf space or preferential positions on administration platforms'.[4] Specifically, platform operators are subject to the existing prohibitions on conflicted remuneration and volume-based shelf space fees under Part 7.7A of the *Corporations Act*. This regime is broad and captures both monetary and non-monetary benefits, including fees, rebates, marketing payments and other benefits provided in exchange for access to platform, preferred placement, and continued product availability.

[2] Refer to Financial Services Council (**FSC**) Standard 31: *Wrap Superannuation Platform Trustee Investment and Adviser Governance Principles*.

[3] Australian Prudential Regulation Authority, Prudential Standard SPS 530 *Investment Governance* at SPS 530 – 6 [23].

[4] Revised Explanatory Memorandum to the Corporations Amendment (Further Future of Financial Advice Measures) Bill 2012 at [2.61]. See, relevantly, Division 5 of Part 7.7A of the *Corporations Act*.

Accordingly, Options 1.2 and 1.3 run the risk of duplicating existing obligations rather than addressing any identified legislative gap. If the concern of Treasury is that, in particular cases, existing obligations have not been met (or have otherwise not been adequately supervised), a more proportionate and effective response would, in our view, involve targeted supervisory guidance and enforcement of existing regimes. Additional prescriptive obligations would only increase compliance cost, conflict with the approach of ‘principles-based’ regulation in a diverse market, and introduce further regulatory complexity without a tangible benefit to members; and

(c) restrictions on trustee operating models, such as the Trustee for Hire model (Option 1.4), are a disproportionate and imprecise response to the identified mischief. The Trustee for Hire model serves a legitimate commercial purpose – enabling market participants to offer superannuation products without the cost and complexity of direct RSE licensing. Its restriction would impose significant barriers to entry by requiring each product promoter to independently bear the full burden of RSE licensing, whereas under the Trustee for Hire model, this burden is shared (but critically, not reduced). Elimination of the model would raise the minimum efficient scale necessary to participate in the superannuation market, entrenching incumbent operators and reducing the competitive diversity that currently benefits members. More fundamentally, the alleged governance failures associated with the Shield/First Guardian Collapse were not isolated to Trustees for Hire; therefore, in our view, a more appropriate remedy would involve enhanced supervisory oversight and targeted enforcement of existing *SIS Act* obligations and APRA prudential standards, not structural prohibition.

In short, we view the governance failures exposed by the Shield/First Guardian Collapse to not be best remedied by the introduction of an additional definitional regime overlaid upon the existing legislative architecture. A more effective approach would rather be the targeted application of existing supervisory and enforcement powers. This approach would more directly address the identified behavioural deficiencies of the Shield/First Guardian Collapse, without generating the regulatory duplication, definitional overlap and competitive distortions that each of the options under Proposal 1 would, in our view, inevitably produce.

3 Proposal 2: Increase penalties under the *SIS Act*

Proposal 2 seeks to double the maximum penalties under the *SIS Act* or to increase the penalties under the *SIS Act* to better align with the *Corporations Act*.

HSF Kramer takes no view on what the value of any such penalties should be. However, we are, in principle, supportive of the alignment of penalties existing under the *SIS Act* with penalties existing under the *Corporations Act* on the basis that uniformity of penalties for the same or similar conduct across financial services law is important and should be promoted where appropriate.

4 Proposal 3: Introducing a waiting period for inter-fund superannuation switches

4.1 Summary of proposal

Under Proposal 3, members who make certain rollover requests between superannuation funds would be subject to a mandatory waiting period (for example, five days). That request will be deemed to lapse if the ‘transferring fund’ does not receive confirmation of the request in the period between the expiration of the mandatory waiting period and three business days later. It is also proposed that the transferring fund will be obliged to provide a prescribed notification to the member upon receiving the initial request to switch, informing them of all relevant risks involved in superannuation switching.

The proposal seeks to (a) properly inform members where a switch results in a change in regulatory environment or exposure to higher risk products; (b) protect members from high-pressure sales, including those involving financial advisers and lead generators; and (c) minimise red tape for consumers, noting the significant volume of superannuation switching that occurs. Such measures align with the Government's objective of 'putting sand in the wheels' of the superannuation switching process to better protect members.[5]

Of note, the scope of risks this proposal aims to address is limited to consumer harms arising from investment in inappropriate products, the charging of excessive fees and, in some cases, the loss of regulatory protections. The flagging of higher-risk transactions relating to fraud and cyber security is expressly outside the focus of this measure, with those risks expected to be addressed through a separate, dedicated approach by funds.

4.2 Current legislative framework

The current obligations of superannuation trustees concerning the obligation to rollover a member's benefits from one fund to another are set out in Division 6.5 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (***SIS Regulations***).

Specifically, regulation 6.33(1) enables a member of a regulated superannuation fund or approved deposit fund to 'request, in writing, that the whole or part of the member's withdrawal benefit in the transferring fund be rolled over or transferred' to a receiving fund. Critically, this is a member driven process and, as per regulation 6.33(2), the relevant member request can be made to either the transferring or the receiving fund.

Once all required information has been provided and validated in accordance with regulations 6.33A(2) – 6.33E, regulation 6.34A(2) requires the trustee to effect the rollover or transfer as soon as possible and, in any event, within three business days of receiving the request. While the trustee may refuse a rollover in limited circumstances, the framework confers no discretion to delay or otherwise refuse upon the basis that the request raises suspicions of fraudulent or scam activity.

As an aside, we note that sections 1019A – 1019B of the *Corporations Act* allow a client to return a financial product to the relevant responsible person, being the person who issued or sold the product in question (**Cooling Off Period**). These provisions also allow for the repayment of the monies paid to acquire the product, within 14 days of the earlier of (a) when the confirmation requirement (if applicable pursuant to s 1017F) is complied with; or (b) at the end of the fifth business day after the day on which the product was issued or sold to the client.

4.3 Issues with proposal

In our submission, for the following reasons, Proposal 3 provides no further protection to members beyond what already exists in financial services law. It is our view that these existing mechanisms should be further utilised or enhanced to achieve the stated goals of the proposal.

First, the proposal does not provide any additional meaningful protection for members above and beyond the protection already provided by the Cooling Off Period. As identified in Section 4.2, a 'cooling off' period already exists in the *Corporations Act* for members to return the product, except if they have already exercised a right under the product. In our observation across the market, member behaviour is unlikely to change if they are required to confirm a rollover request within five days rather than having the option to return the financial product within 14 days. Further, as the Consultation Paper itself notes, a consumer is unlikely to change their decision if they are subject to improper pressure by a financial adviser. Therefore, contrary to its stated goals, the proposal

[5] See press conference transcript by the Honourable Daniel Mulino MP, Assistant Treasurer and Minister for Financial Services dated 10 December 2025.

increases red tape for consumers without any corresponding tangible benefit or protection.

Second, in our view, members would be better protected by ASIC further utilising its powers to regulate financial advisers as opposed to the statutory prescription of a waiting period for super switches. The primary mischief that Proposal 3 seeks to address is the provision of substandard or insufficient financial advice to members that inappropriately influences them to make a switch to potentially higher risk funds. This problem is best addressed through ASIC using the enforcement powers it already has to regulate the conduct of financial advisers (i.e. by taking enforcement action with respect to compliance with best interests and appropriate advice duties by financial advisers) and lead generators (i.e. by taking enforcement action with respect to misleading and deceptive conduct and the provision of unlicensed general financial product advice).

In our view, an increase in scrutiny of financial advisers and lead generators, rather than making switching harder for members, would better protect members, while preserving superannuation portability. The Consultation Paper itself notes that switches can 'provide significant benefits' to members (Consultation Paper at page 25). The portability regime and historical reforms (such as the prohibition of exit fees) were designed to improve member agency in moving between funds, and these objectives should be maintained.

Third, the proposal increases the regulatory burden upon trustees to confirm switches. If the policy is applied to all superannuation switches, this will create a significant burden on trustees and could create significant friction within the system. For example, a member might fail to provide confirmation of a bona fide switching request leading to the request lapsing, only for the member to subsequently reissue a request. This friction would clearly undermine members' legitimate right to exercise their choice as to their preferred fund and create further costs for the trustee (which will inevitably be passed on to members).

However, this issue is not addressed by applying the policy to particular subsets of inter-fund switches (e.g. switches to self-managed superannuation funds). It is understandable, from a policy perspective, to seek to ensure that members who switch to higher risk funds are appropriately informed as to the risks that they are taking. Despite this objective, a mandatory waiting period for a subset of switches does not assist if members have received poor financial advice. This is because the delay in switching will not actually arm the member (or trustee) with sufficient information to scrutinise whether a switch is inappropriate. Furthermore, consistent with our comments in Section 2 above, applying proposals to subsets of funds creates definitional issues and a potentially fragmented regulatory framework that is contrary to the existing principles-based regulatory regime in the superannuation industry.

This increased regulatory burden on trustees is particularly problematic as trustees have limited visibility over why a member has decided to rollover their fund. As identified in Section 4.2 above, the transferring fund is often only informed of a request to switch by the receiving fund (as opposed to being informed by the member). The transferring fund is unaware of whether the member has received appropriate financial advice or the circumstances otherwise influencing their request. Beyond requirements to verify the personal and membership details of the member, the *SIS Regulations* do not empower the trustee to consider whether the member's request is a consequence of fraudulent or scam behaviour. There is a strict and non-discretionary requirement on the trustee to implement the rollover request.

We would be supportive of a proposal which extends the time in which trustees must action rollover requests. We would also support the introduction of a regime which enables trustees to verify that a request has been made by the member before actioning it, or a discretionary regime to allow trustees to delay a request where fraudulent or scam activity is detected or reasonably suspected. While the Consultation Paper states the proposal is not directed to fraudulent or scam activity and identifies Treasury's expectation for 'funds to take a separate, dedicated approach to flagging' fraudulent activity (Consultation Paper at page 30), the practical reality is that trustees are neither given the power or information, nor time, to make such inquiries. Our proposal would provide (a) a further layer of protection for members against fraudulent financial advice; and (b) a formal mechanism for trustees to fulfil their obligations to exercise their powers in the best financial interests of members.

We acknowledge that Proposal 3 is a well-intentioned response to the concern that members are receiving poor financial advice prior to engaging in super-switching activity. However, we are concerned that the proposal does not achieve Treasury's stated objectives and would have the effect of increasing the regulatory burdens imposed upon both trustees and members. We are only supportive of the introduction of a waiting period for inter-fund switches to the extent it is designed to provide trustees with the ability (both time and information) to scrutinise rollover requests for fraudulent or scam activity.

Otherwise, we consider that existing regulatory protections can be better leveraged. For example, there can be more specific and explicit disclosure regarding the availability of a Cooling Off Period both before and within 14 days after a member makes a super switch.

5 Proposal 4: Limit fee deductions for switching-related financial advice

5.1 Summary of proposal

The two options under Proposal 4 relate to whether, and in what circumstances, a trustee should be permitted to deduct fees from a member's superannuation interest for financial advice that recommends the member switch superannuation funds.

The first proposed option (Option 4.1) would prohibit advice fee deductions where the associated advice recommends a client switch superannuation funds. Financial advisers would be required to disclose to a member, before providing advice, that any switching-related advice fees must be paid out-of-pocket and cannot be deducted from the member's superannuation account. Option 4.1 also includes a targeted alternative (Option 4.1a), under which the prohibition could be limited to prescribed circumstances, such as prohibiting advice fee deductions from Platform RSEs, prohibiting deductions for new members of the receiving fund for a prescribed period, or applying deduction restrictions based on age or balance thresholds.

The second proposed option (Option 4.2) would impose explicit obligations on the receiving superannuation fund in relation to the deduction of fees for personal financial advice in a bid to ensure that advice for which fees are deducted clearly relates to the member's superannuation interest and is in the best financial interests of the member. Option 4.2 encompasses three distinct sub-options:

(a) Option 4.2a, which would require trustees to review advice fee deductions following a switch, such as at the point of first deduction;

(b) Option 4.2b, which would impose mandatory fee caps on switching-related advice deductions, with options including an absolute dollar cap, a percentage-based cap, or a combined or tiered model providing stronger protections for members with smaller balances; and

(c) Option 4.2c, which would introduce clearer minimum expectations for adviser and licensee onboarding and monitoring in relation to switching-related advice fee deductions, including scrutiny of business models presenting heightened risks such as high-volume switching or reliance on lead generation.

5.2 Current legislative framework

Section 99FA of the *SIS Act* prohibits the trustee of a regulated superannuation fund from charging the cost of personal financial product advice against a member's interest except in accordance with the requirements set out therein. The recent amendments to that section are a product of Recommendation 7 of the Treasury's Quality of Advice Review (Final Report, December 2022) (**Quality of Advice Review**), which relevantly provided:

> **Recommendation 7 – Deduction of adviser fees from superannuation**
>
> Superannuation trustees should be able to pay a fee from a member's superannuation account to an adviser for personal advice provided to the member about the member's interest in the fund on the direction of the member.

Section 99FA also protects members' interests by requiring the trustee to charge the cost in accordance with the terms of a written request or consent of the member.

The primary legal protection against members receiving poor financial advice is found in Part 7.7A of the *Corporations Act* which contains requirements on financial advisers to act in the best interests of their clients and ensure fees are charged appropriately, as well as obligations to avoid conflicted remuneration. Most relevantly, section 961B of the *Corporations Act* sets out the 'best interests' requirement of financial advisers. This includes an obligation for financial advisers to identify the objectives, financial situation and needs of the client, make reasonable inquiries to obtain complete and accurate information and base all judgments on the client's relevant circumstances.

The *SIS Act* does not impose any prescriptive obligation upon trustees to ensure that the advice provided by financial advisers in relation to switching complies with the 'best interests duty'. In this vein, we note that ASIC has published regulatory guidance which, *inter alia*, outlines (a) an expectation for trustees to undertake regular, proactive reviews of advice documents using risk-based and random sampling (directed at confirming that advice was provided and that it is consistent with the sole purpose test); and (b) its view that trustees need not determine the quality, value or appropriateness of the advice provided to their members.[6]

5.3 Issues with proposal

Like Proposal 3, we are concerned that Proposal 4 has several limitations which undermine its ability to achieve its stated goals. We believe that existing mechanisms under the *Corporations Act* should be used by ASIC to protect members from inappropriate super-switching behaviour.

First, the proposal has the effect of undermining the objectives and recommendations of the Quality of Advice Review, the stated purpose of which was 'to ensure Australians have access to high quality, accessible and affordable financial advice'. Removing the ability of Australians to pay for financial advice about their superannuation from their interest in the fund (a) is a financial barrier to seeking financial advice; (b) has a disproportionate adverse effect upon persons who cannot otherwise afford such advice; and (c) inevitably leads to poorer outcomes for members who are otherwise unable to receive professional advice in making decisions about their superannuation.

Second, the proposal is inconsistent with the objectives of the *SIS Act*, which expressly requires trustees of superannuation funds to create a publicly available retirement income strategy (which, in turn, maximises expected retirement income over a member's period of retirement). The intention behind this policy is to create better outcomes for members who are approaching retirement. Access and affordability of advice is a key element of driving improved retirement outcomes for Australians. Obtaining financial advice is an

[6] ASIC Report 781, 'Review of superannuation trustee practices: Protecting members from harmful advice charges' (May 2024).

important way that Australians can make more informed decisions about which investment strategy will optimise their retirement outcome and limiting fee deductions for switching-related financial advice may deter members from seeking advice because this proposal now requires them to bear the costs of financial advice personally.

Third, in our view the better way to address the potential consumer harms associated with poor financial advice would be through ASIC utilising its existing powers to regulate advice providers to ensure that advice is being provided appropriately to members and consistently with the 'best interests duty'. Amending the mechanism through which financial advice is paid for does not address the primary problem, which is the quality of the advice that is being provided. Furthermore, we reiterate that conflicted remuneration is already prohibited under Part 7.7A of the *Corporations Act* and we consider that this is an appropriate regime to regulate the payment and receipt of benefits that may inappropriately influence financial advice.

Fourth, the proposed requirement for trustees to be required to determine whether a switching-related advice fee is reasonable having regard to the nature and scope of the advice as well as the member's circumstances improperly requires trustees to act as a regulator and supervisor of financial advisers. That responsibility is squarely within the power and remit of ASIC. Most problematically, the costs incurred by trustees undertaking this exercise will inevitably be borne by members (as fund money will be used to cover the costs).

Further, trustees are responsible for acting in members' best financial interests when exercising their powers and performing their duties in respect of the fund. Trustees are not responsible for matters outside of the fund, such as advice relationships between a member and their adviser.

It is impractical and duplicative for trustees to be across the exact financial circumstances of each member. Personal financial advice is provided based on the personal circumstances of the member, which are unlikely to be known by the trustee. The proposal also risks causing significant delays in the superannuation system and would hinder trustees' ability to provide financial services in a manner which is cost efficient and timely by requiring them to effectively conduct due diligence on, and supervise all, switching-related financial advice. In other words, as mentioned above, the trustee will essentially assume a regulator/supervisory role for financial advice; this fundamentally alters the function of a superannuation trustee under law and in our superannuation system.

With respect to the proposal which clarifies expectations of trustees for adviser and licensee onboarding obligations, it is important to recognise that trustees currently have discretion as to how they apply these onboarding obligations in a manner consistent with the size, complexity and needs of their fund. We would discourage any new rules which seek to restate expectations in a manner which is prescriptive or 'one-size-fits-all'. This approach is inconsistent with the principles-based regulatory regime which exists for superannuation funds in Australia, which is necessary due to the breadth and diversity of the market. We also submit that ASIC (and APRA) already have the power to monitor and engage with trustees on their current onboarding practices, and concerns should be responded to on a case-by-case basis.

6 Proposal 5: Requiring Platform Trustees to compensate members for eligible losses

6.1 Summary of proposal

Proposal 5 comprises two options directed at improving member redress. Under Option 5.1, Platform Trustees would be subject to a legal obligation to compensate members for 'eligible losses' – being losses arising from external fraud or theft that result in the collapse of an investment product (excluding losses attributable to ordinary investment performance or market volatility). The mechanism would be 'activated' by an independent body (that determines whether an 'eligible loss' has occurred and directs compensation accordingly) and funded through trustee capital (not RSE assets), with each Platform Trustee required to maintain a dedicated, risk-based capital pool. Rules would govern the quantum of compensation available, being referable to either initial capital invested, capital indexed against a counterfactual benchmark, or a capped proportion of the loss. This obligation would operate as the 'first pathway' for affected members, with other existing redress mechanisms available only if a Platform Trustee is unable to meet it.

Under Option 5.2, ASIC would be granted a directions power enabling it to require a Platform Trustee to commence a remediation process in accordance with ASIC Regulatory Guide 277 *Consumer remediation*, where ASIC has reason to suspect that the Platform Trustee has engaged, or will engage, in conduct constituting a contravention of a financial services law that may have led to member losses. Upon receiving such a direction, the Platform Trustee would be responsible for scoping the misconduct or failure, determining whether it bears responsibility for the relevant member losses, and providing an appropriate outcome – monetary or non-monetary – to affected members.

6.2 Current legislative framework

APRA Prudential Standard SPS 114 *Operational Risk Financial Requirement* (**SPS 114**) requires RSE licensees to, in short, maintain, manage and utilise financial resources to protect beneficiaries from losses due to 'operational risks'. That expression is given colour by APRA Prudential Standard CPS 230 *Operational Risk Management* (**CPS 230**). Under CPS 230, an APRA-regulated entity must (a) identify, assess and manage operational risks that may result from inadequate or failed internal processes or systems, the actions or inactions of people, or external drivers and events; and (b) manage their full range of operational risks, including legal, regulatory, compliance, conduct, technology, data and change management risk. This is a deliberately broad formulation, extending to, for example, governance, oversight and due diligence failures by the trustee itself.

Financial resources required to be held under SPS 114 (**ORFR Financial Resources**) may be used to, *inter alia*, address operational risks that could reasonably be considered to have caused (or could cause) one or more beneficiaries to sustain a loss or be deprived of a gain to which they otherwise would have been entitled, or to meet CPS 230's requirements for the effective management and prevention of operational risk incidents, including the remediation of identified material weaknesses. The target amount and tolerance limit of ORFR Financial Resources – including how and why those amounts have been determined to be appropriate – as well as the processes and parameters for determining how and when ORFR Financial Resources can be used are required to be set out in a board-approved 'ORFR strategy'. The target amount and tolerance limit must be determined on a prudent basis that suitably reflects the RSE licensee's operational risk profile and risk assessments, the permitted uses of the relevant ORFR Financial Resources, and the size, business mix and complexity of its business operations.

In addition, Part 23 of the SIS Act provides a mechanism for superannuation trustees to apply to the Minister for a grant of financial assistance in circumstances where a superannuation entity suffers loss as a result of fraudulent conduct or theft.

6.3 Issues with proposal

Option 5.1 seeks to impose a compensation obligation upon Platform Trustees in respect of 'eligible losses' that arise from external fraud or theft and result in the collapse of an investment product. This framework is intended to expressly exclude losses arising from trustee maladministration, on the basis that such losses are already addressed through the ORFR model. In our view, such a distinction is unworkable in practice. In cases involving significant compensation claims, it is unlikely, at least *prima facie*, for an act of external fraud to be alleged as the sole cause of member loss. Instead, it is more likely to be claimed that such loss was derivative of some mixture of external fraud and trustee governance failures – including failures of due diligence, investment monitoring and enforcement of investment limits. Where loss has a composite cause of that kind, it will prove practically difficult (and, indeed, highly time-consuming) to attribute it to 'external fraud' *or* 'trustee operational failure' for the purposes of determining which compensation mechanism is to apply – a problem Option 5.1 does not appear to address.

This ambiguity is compounded by the proposed funding approach: by requiring Platform Trustees to maintain a dedicated compensation reserve alongside the ORFR Financial Resources, the implementation of Option 5.1 would fragment a trustee's financial resources across two different pools that are directed at substantially overlapping risks. To this end, we note that, under SPS 114, the relevant 'target amount' and 'tolerance limit' of ORFR Financial Resources must already be determined on a 'prudent basis' that suitably reflects the RSE licensee's operational risk profile and risk assessments, the permitted uses of such resources, and the size, business mix and complexity of its business operations. In our view, this existing reserve is capable of responding to the full range of relevant risks which Proposal 5 seeks to address and remedy, without the inefficiencies and additional cost that a bifurcated structure would necessarily entail.

We also note in this regard that the risk of external fraud occurring in respect of an investment is a risk that can arise for all superannuation trustees and not only in the context of Platform Trustees. Accordingly, we do not support the imposition of an additional compensation obligation for 'eligible losses' on a subset of the industry in circumstances where all superannuation trustees may potentially be exposed to the risk of an 'eligible loss'. To our minds, the imperative for protecting members from an 'eligible loss' is arguably greater in the context of a MySuper product, where the member has not expressly selected the particular investments to which they are exposed.

The proposal to vest activation of the compensation obligation in an independent third-party body is, in our view, also inappropriate. The Board is already deemed accountable for oversight of operational risk management, including business continuity and the management of service provider arrangements. Further, the trustee bears (as *per* the *SIS Act*) primary and non-delegable obligations to act in the best financial interests of members and maintain adequate risk management systems. In our view, the trustee is, therefore, naturally the entity best placed – and, indeed, already legally obligated – to identify, assess and respond to member loss arising from events within its platform/fund.

Indeed, an independent activator would operate at a temporal and informational disadvantage relative to the trustee, lacking both the proximity to the relevant events and the access to member-level data required to make timely and accurate determinations. The machinery required to operationalise such a body – encompassing determinations of eligible loss, apportionment of liability across multiple responsible parties, quantification of individual member compensation, and management of the interface with concurrent AFCA, court and ASIC proceedings – would introduce precisely the complexity and delay that is inconsistent with the proposal's stated objective of 'timely' member redress (see, for example, Consultation Paper at pages 42 and 51).

We further note, in this regard, that the question of whether an external fraud has occurred is a question of law. It is not clear to us how an independent third-party body would form a view on whether an external fraud has occurred without going through the necessary evidentiary processes that would otherwise be carried out by way of a criminal investigation. Undertaking such a process before paying compensation would not achieve the proposal's stated objective of 'timely' member redress.

It also appears to us that requiring a superannuation trustee to be liable for the fraudulent conduct of third parties may incentivise fraudulent activity (on the basis that perpetrators may be less concerned about being pursued for recovery) and make it more difficult for trustees to seek to recover such losses from the perpetrators of such alleged fraud.

Consideration would also need to be given as to the interaction between this proposed new compensation regime and Part 23 of the SIS Act. Without legislative amendment, a Platform Trustee that pays compensation for an external fraud would, on the face of the law, have the right to make application for financial assistance under Part 23 of the SIS Act.

We also note that questions as to remediation and compensation often raise disagreements between trustees and financial regulators, such as ASIC and APRA. These disagreements have historically been contested through litigation, where courts have provided views on remediation undertaken by trustees. Giving a regulator the power to direct a remediation would undermine any court process in respect of a remediation. Indeed, this power would effectively allow a regulator to make findings of liability requiring remediation, before the trustee is afforded an opportunity to have the matter heard before a court. Accordingly, we would caution against any proposal to give a regulator a power to direct a compensation obligation to occur.

7 Conclusion

Thank you for providing us the opportunity to comment on the Consultation Paper. If you would like to discuss the matters raised in this submission, please contact any of us at the details below.

Yours sincerely

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