Beneficiary, Investor, Citizen

*Characterising Australia’s super fund participants*

By Scott Donald†

Synopsis

One of the primary objectives of the regulatory regime governing superannuation funds is to safeguard the interests of members. However members are implicitly characterized in different ways in different parts of the regulatory regime. This causes inconsistencies in the way different parts of the regime recognize the needs, interests and expectations of members.

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**Introductory comments**

Over the past twenty years superannuation has assumed an increasingly important role in the provision of financial security in retirement. Approximately 90% of the Australian workforce are now members of superannuation funds. The assets held in superannuation funds in Australia now dwarf those in life insurance companies and in non-super investment vehicles such as unit trusts and total benefit payments from superannuation funds already exceed government payments for the Age Pension.

As this retirement ‘nest egg’ has grown, so too have the array of rules regulating its activity. The rules span direct legislative involvement, such as *Superannuation Industry (Supervision) Act 1993* (Cth), (*SIS*) and the *Corporations Act 2001* (Cth) (*Corporations Law*), through legislation having an indirect bearing, such as the *Income Tax Assessment Act 1936* (Cth), to the regulatory rules imposed by APRA and ASIC and the rules of self-regulatory bodies such as the ASX.5

There are many issues that this cacophony of regulation inspires. This paper aims to address one in particular: do different parts of the regulatory scheme exhibit different assumptions about the purpose of the scheme as a whole? This is clearly a question of fundamental importance, capable of being approached from many angles. This paper takes a somewhat unusual approach. It attempts to infer a characterisation of the beneficiaries of the regulation (that is, the members of superannuation funds) from different parts of the regime. In so doing, it attempts to highlight the inconsistencies in a less arid, more lively way than might be the result of a conventional comparison of the relevant statutory and regulatory provisions. It also begins to respond to Pearson’s observation that

> ‘Risks to the consumer have not been sufficiently articulated in the conversations around the massive changes to the regulation of Financial Services in Australia ... If regulation is about collective goals and a moral community ... then the conversations in the regulatory system should involve more than technical discussions about the cost, length or even utility of disclosure documentation and other compliance obligations.’ 7

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1 The term superannuation is used in Australia and NZ synonymously with the way that ‘occupational pension’ is used in other common law jurisdictions, such as the UK, Canada and the US. However differences in the statutory regime and the development of equitable principle make references to jurisprudence in NZ, Canada and the US hazardous.


3 Department of Innovation, Industry, Science and Research, *Executive Briefing: Managed Funds in Australia*, (AGPS, Canberra, 2008).

4 Total benefits from superannuation funds (lump sum plus pensions) in calendar year 2005 were approximately $32.5bn, compared to $22.5bn paid by the government in age pension over the same period. APRA, *Insight*, Issue 2 2007, Table 3, 23; Australian Bureau of Statistics, 5206.0 - *Australian National Accounts: National Income, Expenditure and Product*, Sep 2007.

5 It is not surprising, given the degree of overlap, that the multi-layered nature of this regulatory scheme is increasingly a feature of corporate law also. See for instance Stephen Bottomley, ‘Where did the law go? The delegation of Australian corporate regulation’ (2003) 15 AJCL 105.

6 Some of these are introduced in Michael Adams, ‘Overlap in superannuation licensing doubles the costs’ (2006) *Australian Super News*, Issue 5, 26 May, 82.

A point of departure

The analysis presented in this paper suggests that several distinct leitmotifs clamour for attention within regulatory scheme. This is not a new idea. Lord Justice Hoffman, speaking extra-curially in 1994, described the interplay of four juridical sources at play in superannuation:

- contract;
- equitable principles;
- statutory regulation; and
- administrative discretion.  

A year earlier, Moffatt had sought to apply a conceptual map to the doctrinal developments present in the flurry of pension cases in the UK in the early 1990s. Applying a taxonomy borrowed from the Critical Legal Studies movement, he distinguished three spheres of social life: family and friendship, within which he placed trust law; work and exchange, within which he placed employment law; and state and citizenship. The doctrinal friction present in the UK cases arose, under his framework, because pension plans’ location in both trust and employment law meant they straddled two different spheres. Had he been writing in Australia, he might easily have recognised the impact of compulsory superannuation in bringing superannuation law into the third sphere, state and citizenship, also.

This paper contains echoes of both these descriptions, but proposes a slightly different taxonomy. It identifies three distinct models:

1. The Traditional Model, essentially an amalgam of contract, equity and employment law;
2. The Investor Model, in which the member is perceived as a risk-taking consumer of financial products; and
3. The Public Model, in which the superannuation fund is treated as a quasi-public institution.

The first three sections of the paper deal with each in turn. Along the way, the paper asks two important questions: Is the Investor model compatible with the Traditional Model it has partially eclipsed? and second, to what extent has the Public Model had an impact on the legal environment in which superannuation funds operate, and is it, in turn, inconsistent with the other models? To the extent that the answer to any of these questions is “No”, then the seminal question, whether ‘different parts of the regulatory scheme exhibit different assumptions about the purpose of the scheme as a whole?’ will be answered in the affirmative. The final section of the paper makes some high-level remarks about how the different models allocate risk amongst the actors in the superannuation arena.

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8 Lord Hoffman, ‘The Direction of Equity and its Role for Superannuation/Pensions in the 90s’ Superannuation 94 – A National Conference for Lawyers on Superannuation.
1. **The Traditional Model**

In the traditional model, superannuation is sited firmly within the general law governing trust law and contracts. This is enshrined in the *SIS Act* which employs both the mechanisms of trust law (the trustee, beneficiary and quarantine of the fund corpus) and its language. Employment law also makes a cameo appearance.

*The member as ‘beneficiary’*

The beneficiary in a traditional trust arrangement is entitled to have the trust administered in accordance with the terms of the trust instrument. In addition, Equity will impose certain constraints (fiduciary or otherwise) on the behaviour of the trustee, to the extent those constraints are not modified or excluded in the trust instrument. The terms of the trust instrument are thus of paramount importance in defining the interests (sometimes termed ‘expectations’, to differentiate them from property rights) of beneficiaries. Moreover, the courts have been loathe to fetter the freedom of settlors to include whatever terms they, the settlors, saw fit to include in the trust instrument, subject to some irreducible core that ensures that the arrangement created remains a trust.

Superannuation funds historically followed a similar pattern. Subject to a few provisions that ensured that the trust respected the concessional taxation treatment they received, neither legislators nor the courts felt a need to interfere in the freedom of employers (mostly) to specify the terms of the superannuation funds they created. The close attention (and respect) paid to the precise terms of the relevant trust instruments in surplus cases, such as *Re Courage Group’s Pension Schemes*, *Mettoy Pension Trustees v Evans* and *Lock v Westpac* is testament to this ‘hands-off’ attitude.

Despite the legislative programme of the past fifteen years in Australia, great flexibility remains. The *SIS Act* imposes a handful of requirements on the structure of the trust but does not prescribe its precise terms. So for instance, s52(2) incorporates a set of covenants into the trust instrument that ensure that certain important trustee duties cannot be excluded or modified. Similarly s62, the so-called ‘sole purpose’ requirement, requires that trustees ensure the fund is maintained for the provision of retirement benefits.

This flexibility has had its critics. There have been repeated assertions that trust law is anachronistic and perhaps ill-suited to the task of governing the activities of the modern financial institution that superannuation funds have become. Others

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10. *Bartlett v Bartlett* (1845) 4 Hare 631, 67 ER 800.

11. Examples include the fiduciary ‘proscriptive’ duties identified by the High Court in *Breen v Williams* (1996) 186 CLR 71, as well as the non-fiduciary prescriptive duties, the equitable duty of care and the duty to invest prudently. Pamela Hanrahan, ‘The Responsible Entity as Trustee’ in Ian Ramsay (ed), *Key Developments in Corporate Law and Trusts Law* (LexisNexis Butterworths, Sydney, 2002), 227.


see the superannuation fund as a ‘sui generis species of trust’\(^{18}\) respecting its genesis in trust law, but requiring a distinct approach.\(^{19}\) Nevertheless the courts continue to recognise the equity that infuses the duties that arise in the trust instrument.\(^{20}\) Similarly, reviews in both the UK and Australia have returned a verdict in favour of trust law after failing to find a viable alternative.\(^{21}\) Thus, despite vigorous suggestions to the contrary, in \textit{Cowan v Scargill}, Megarry V-C concluded that he could find

‘no reason for holding that different principles apply to pension fund trusts from those which apply to other trusts’.\(^{22}\)

Naturally, superannuation’s unique context affects the way trust law principles apply to superannuation funds. Characterising the member, not as the hapless and vulnerable beneficiary of Equity lore, but as a competent economic actor, influences the way in which the courts interpret the trust instrument and balance the equities between the parties.\(^{23}\) Lord Browne-Wilkinson in the House of Lords and Justice Bryson, in the Supreme Court of New South Wales, have been especially critical of simple-minded application of trust principles to commercial applications, including superannuation. Browne-Wilkinson LJ in \textit{Target Holdings v Redforns},\(^{24}\) a case involving a payment to a solicitor as part of a conveyancing transaction that gave rise to a ‘bare’ trust, noted

‘The fundamental principles of equity apply as much to such trusts as they do to the traditional trusts in relation to which those principles were originally formulated. But in my judgment it is important, if the trust is not to be rendered commercially useless, to distinguish between the basic principles of trust law and those specialist rules developed in relation to traditional trusts which are applicable only to such trusts and the rationale of which has no application to trusts of a quite different kind.’\(^{25}\)

Specifically in the superannuation context Bryson J has noted,


‘it hard to see the point of debate on whether occupational pension schemes should continue to be regulated by trust law’,

noting that superannuation funds require some legal form and implying that trust law is as good a starting place as any, 124.


\(^{21}\) See for instance Law Reform Commission, above at n 16, and in the UK; \textit{Report of the Pension Law Review Committee (the Goode Report)} (HMSO, 1993).

\(^{22}\) [1985] 1 Ch 270 at 290. In Australia, see \textit{Fouche v The Superannuation Fund Board} [1952] 88 CLR 609; \textit{Locke v Westpac} (1991) 25 NSWLR 593. See also Gummow J’s obiter muse on whether construction of a superannuation trust deed required any ‘special’ approach, such as that proposed in some UK cases; \textit{Caboche v Ramsay} (1993) 119 ALR 215, 233. The implication of the comment, though it is admittedly ambiguous, is that no special approach is required.


\(^{24}\) [1995] 3 All ER 785.

\(^{25}\) Above at n 24, 795.
The parties’ relationship [in a superannuation fund] is quite different to the relationship between beneficiaries and trustees who are administering a trust instrument which expresses the bounty of a settlor. ... The context ... is a contractual context in which an employee ... and the employer adhere to the Plan as a set of rules to regulate part of their employment relationship. Superannuation rights are not granted out of grace or bounty and members contribute their own money. 26

As Bryson J notes, the point of distinction between superannuation funds and trusts in general that is typically highlighted is the fact that members are typically not volunteers.27 That is, superannuation members have generally provided consideration to secure their participation in the trust. In Australia they are also not volunteers in the colloquial sense of the word; membership of a complying fund is more or less compulsory for adults in the workforce.28

Notwithstanding these caveats, the ‘paternalism’ present in general trust law plays a role in superannuation. It is present in the SIS Act also. Trustees of superannuation funds are required by the SIS Act to act in the best interests of members29 and to exercise their discretions with the care, skill and diligence appropriate to their position,30 requirements that are based on familiar trust law principles. The positive, selfless nature of these obligations imbues the role of the trustee with a protective flavour. This protectiveness, together with the limited right of beneficiaries to influence or impugn the decisions of their trustee, justifies the description of the trustees’ role as ‘paternalistic’.

One area in which the paternalism infused through the Traditional Model becomes obvious in the superannuation environment is in the debate surrounding a trustee’s duties when offering Member Investment Choice.31 Where members are offered Member Investment Choice, responsibility for the selection of an investment strategy for the member falls to the member. Only if the member fails to make a selection will the responsibility revert to the trustee. The question then arises, to what extent is the trustee responsible for the choices made by the individual member? Are the trustees, for instance, responsible to ensure the range of choices they make available to members is prudent? Are they perhaps also responsible for ensuring that the flexibility afforded to members to tailor their strategies does not expose those members to ‘unacceptable’ risks (however those might be defined). In other words, to what extent does the paternalistic spirit permeate the trustee’s obligations when, on the face of it, responsibility for the investment decision has been handed over to members. Opinions on this vary, but it remains a live, and

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27 Mihlenstedt v Barclays Bank [1989] IRLR 522; Imperial Group Pension Trust v Imperial Tobacco [1991] 2 All ER 597. In Australia see Dillon v Burns Philp Finance Ltd above at n 26; Minehan v AGL Employees Superannuation Pty Ltd (1998) 134 ACTR 1; Telstra Super v Flegeltaub (2000) 2 VR 276 at 286. This contribution has inspired some writers to describe the members as being settlers of the trust; Dimity Kingsford Smith, ‘Who Knows Best? Review of Discretionary Powers in Superannuation Funds’, (2000) 28 ABLR 428. It is not obvious that such a characterization achieves much, and in so far as the contributing members have no ability to influence the terms of the trust, such an appellation does as much to mislead as to inform.
28 Of course there are exceptions and exemptions, especially for workers younger than 18 or older than 70, or earning below a threshold amount per week.
29 SIS Act, s52(2)(c).
30 SIS Act, s52(2)(b).
31 A more thorough discussion of this issues is presented in M Scott Donald, ‘The prudent eunuch: Superannuation trusteeship and member investment choice’ (2008) 19 JBFLP 5.
very practical, illustration of the tension between the paternalistic tenor of trust law and the commercial context in which superannuation now exists.

The member as ‘employee’

The fact that the courts will also have regard to the context in which the superannuation entitlement arises in defining the obligations of the trustee and legitimate expectations of the members is consistent with the general principle that the courts will have regard to relevant context, the ‘matrix of fact’ to borrow Lord Wilberforce’s phrase,32 in interpreting contractual provisions. In effect the status of the member as an ‘employee’ is recognised.33

The characterisation of the member as an employee most often strengthens the member’s position. It was noted above that the courts have been prepared to recognise that superannuation being a component of the employment contract means that members are not volunteers. The members’ status as employees has also been held relevant where the employer has sought to amend the terms of the trust instrument, a power sometimes specifically reserved for the employer in superannuation trust deeds. In that circumstance, the courts have on occasion imposed a duty of good faith on the employer, consistent with the bilateral duty of good faith that is held to exist between employer and employee.34 So for instance in Imperial Group Pension Trust v Imperial Tobacco,35 Browne-Wilkinson V-C found that the obligation of good faith implied in contracts of employment arose also in the trust deed and rules of the company’s pension scheme.36 A similar obligation was found by Waddell CJ in the Supreme Court of NSW in Lock v Westpac37 and by the Australian Industrial Relations Commission in AMWU v Shell.38

Glover, writing in the immediate aftermath of Lock v Westpac,39 saw the encroachment of employment contracts as constituting a near-eclipse of trust law, concluding

‘The law of trusts has a role subordinate to the law of contract, and possibly subordinate to other categories as well, in the regulation of employee superannuation schemes.’40

With respect, that assessment overstated the situation in 1992. However events have caught up with the observation, in the form of the increasingly popular ‘master’ trusts. Master trusts are, to all intents and purposes, unit trusts configured to achieve ‘complying’ status under the SIS Act, s45. They are offered

32 Prenn v Simmonds [1971] 3 All ER 237 per Wilberforce LJ, 239.
33 Re Courage Group, above at n 13. Whether this recognition stretches far enough was questioned by Paatsch and Smith in 1992 but it is at least possible that the subsequent judicial statements quoted above may have quelled the fires of their discontent. Dean Paatsch and Graham Smith., ‘The Regulation of Australian Superannuation: An Industrial Relations Law Perspective’, (1992) 5(2) Corporate and Business Law Journal, 131, 133.
34 Whilst in theory this ‘good faith’ gloss acts both ways, to date at least, it has mostly served to strengthen the position of the member. It is however possible to imagine circumstances, for instance when a member makes a disability claim, where the duty of good faith might be imposed on the member.
35 Above at n 27, 606.
37 Above at n 15.
38 Australian Metal Workers Union v Shell Refining (1993) 27 ATR 195.
39 Above at n 15.
by financial institutions directly to the public and, except to the extent that they are nominated as the default fund by employers, don’t exhibit the employment nexus between member and fund that was customary in ‘occupational’ superannuation funds. More importantly, the rights and expectations of members more closely resemble those inherent in a unit trust than those in a traditional occupational scheme. This circumscribed set of trustee duties, when combined with member investment choice, has inspired the present author in another setting to describe trustees of these funds as ‘prudent eunuchs’ for the peculiar combination of impotence and lack of accountability they enjoy.41

Concluding comments

Whilst the relevance of the traditional trust law characterisation of a ‘beneficiary’ may be diminishing, it is important not to overstate the importance of the contractual context. In important ways, members display the ‘vulnerability’ that attracts fiduciary obligations in other fields. For instance, they have no proprietary interest in the assets of the fund per se.42 Their interest is better described as ‘an expectancy’.43 Also, the preservation rules applying to superannuation balances mean that members have extremely limited ability to gain access to their superannuation balance prior to their reaching retirement age, albeit that Fund Choice legislation now permits them to transfer between funds more easily than was hitherto the case. Members also have limited ability to examine the detailed operation of the fund in which they are invested. Taken together, these vulnerabilities mean that the protections afforded at equity and in the SIS Act are important not just for the actual protection of members’ interests, but for the confidence they inspire in members that their interests will be safeguarded.

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41 Donald, above at n 31.
42 Re HIH Superannuation [2003] NSWSC 65; Baird v Baird [1990] 2 All ER 300, 305 per Oliver L.J.
2. **The Investor Model**

Superannuation funds administer large investment portfolios on behalf of their members. In that sense, superannuation funds are unambiguously ‘investment’ vehicles. However in recent years it has been presumed that this further implies that fund members are properly considered ‘investors’. This section assesses the extent to which this characterisation fundamentally challenges the Traditional Model described in the previous section.

**The Wallis Committee**

The Financial System Inquiry of 1996, (commonly known as the “Wallis Committee” after its chairman, Mr Stan Wallis AO) heralded a new era for superannuation regulation in Australia. Ambitious in scope, the Inquiry was charged with identifying

> ‘the regulatory arrangements that will best ensure an efficient, responsive, competitive and flexible financial system to underpin stronger economic performance, consistent with financial stability, prudence, integrity and fairness.’


Importantly for present purposes, the Committee sought to remove any distinctions between the regulation of superannuation and the regulation of other forms of collective investment. This means that it effectively treated superannuation fund members as ‘investors’, a characterisation quite different from that which prevailed up to that point.

**The member as ‘consumer’**

The Wallis Committee was the first comprehensive review of financial sector regulation in Australia since the Campbell Committee of 1981. It adopted an avowedly econo-centric perspective. Its focus on markets caused ‘efficiency’ to be accorded a pre-eminent position amongst the regulatory objectives. It noted,

> ‘The general case for regulation is founded in market failure, where efficient market outcomes are inhibited.’

The primary mechanism for promoting the efficiency of the system was to be competition. Competition implied a ‘level playing field’ for equivalent financial products and services and this, combined with an implicit assumption that superannuation was simply another form of private saving, saw superannuation more explicitly brought within the realm of financial service regulation.

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47 Wallis above at n 44 at 175.
This had quite profound implications. Regulation of superannuation was to be included alongside other financial intermediaries such as banking, insurance and investment entities in the remit of two new, overarching regulators, the Corporations and Financial Services Commission and the Australian Prudential Regulation Commission (which became ASIC and APRA in 1998).\footnote{Responsibility for self managed superannuation funds moved to the Australian Tax Office in 1999; ATO Media Release - Nat 99/71, available at \url{www.ato.gov.au/corporate/content.asp?doc=/content/mr9971.htm}}

The Wallis Committee’s decision to include superannuation within the ambit of ‘financial product’ brought about a fundamental shift in regulatory policy. Even the words used to characterise the active elements of the superannuation fund changed. Funds became ‘products’ and members became ‘customers’, a change in rhetoric that highlights graphically the quite different way in which they were each perceived by the Wallis Committee. And in 1998, insult was added to injury when the familiar ‘trustee’ was replaced with the ungainly ‘responsible entity’.\footnote{Managed Investment Act 1998, borrowing a phrase first appearing in LRC Report No.59, above at n 16. In the same vein, there is a gentle irony in ASIC’s decision to use the term ‘member’ rather than ‘client’ in the interests of ‘plain language’ in ASIC, PS184: \textit{Superannuation: Delivery of product disclosure for investment strategies} (2006).}

More important perhaps than the terminology, was the implication of this change in perspective for the choice of regulatory strategy. ‘Financial safety’ regulation was to be reserved for situations

‘where promises are judged to be very difficult to honour and assess, and produce highly adverse consequences if breached.’ \footnote{Wallis, above at n 44, 190.}

The payments system was one such situation. Superannuation was not, though the Committee did recognize the ‘implications of compulsory contributions and tax assistance for superannuation’ in intensifying the level of regulatory ‘assurance’.\footnote{Wallis, above at n 44, 193.}

Prudential regulation was therefore relevant to superannuation, but the regulators were to aim for a level of risk in accordance with the ‘reasonable expectations’ of the recipients of the financial promise. What was ‘reasonable’ where the promise was a superannuation fund member was not specified.

Characterising members as ‘customers’ implicitly provided that direction. As a general rule ‘customer’ protection is achieved by ensuring transparency and freedom of choice. This philosophy is sometimes called ‘consumer sovereignty’. It seeks to empower individuals to pursue their own, personal interests, interests of which they themselves are held to be the best judge. CLERP 6 adopted this perspective quite literally.\footnote{CLERP 6, above at n 45, 27.} This emphasis on self-reliance is a world away from the Traditional Model in which the trustee plays a paternalistic (or perhaps avuncular) role in determining the course of action that is in the beneficiaries’ ‘best interests’.

The member as ‘investor’

If the member of a superannuation fund is a ‘consumer’, then they are a very specific type of consumer; a consumer of financial products. And as the Wallis Committee noted, market-linked financial products at that.\footnote{Wallis, above at n 44, 130 and 136. Also Pearson, above at n 7, 106 - 107.} Their exposure to market outcomes means that superannuation fund members are not just consumers, but ‘investors’.
This is an important gloss. Where consumer protection exists to provide redress to consumers for faulty products, investment is by its nature risky and investors are expected to bear the consequences of that risk. CLERP 6 recognised that reality when it noted.

‘Risk taking is a central component of financial markets. Market regulation is not intended to guarantee the success of a particular investment decision.’

Moreover whilst individuals may, through good luck or good management, avoid losses, not all investors can enjoy this good fortune. Losses will be experienced by some investors somewhere in the population. Finance theory makes it clear that some investments must fail - it is the sine qua non of the equity risk premium and the credit spread on non-sovereign debt securities. Implicit, then, in characterising members as ‘investors’ is an acceptance that the superannuation entitlements of some portion of the population will be inadequate, not because of anything in the power of the member, but due to the actuation of adverse investment outcomes. Put bluntly, investment markets inevitably have ‘losers’ as well as winners.

Such an outcome may be acceptable to a neo-classical economist, but it does not fit as well in a social policy context. Pearson puts the question well,

‘Collectively we are asking the question of what is an acceptable risk to the financial system? We are barely asking the question of what is an acceptable risk for each individual who contributes to that system’

The likelihood that a significant number of participants will have to rely on the ‘safety net’ of the government’s Age Pension is a problem that ought not be ignored. For one thing, this transfer of risk places a great deal of pressure on that safety net to provide for a dignified retirement for those whose investment outcomes prove inadequate. There is an important moral hazard issue at play here. As Bellis notes, the safety net of the Aged Pension provides workers with a ‘free’ option, the value of which depends on where the safety net is set. Set the safety net too high and members may be inclined to ‘gamble’ with their superannuation investment strategies, knowing they can fall back on the government pension if it all goes horribly wrong. On the other hand, set it too low and members who have high expected superannuation balances will choose low volatility strategies (because the government pension is not worth falling back on) and those with low expected superannuation balances will have to gamble (because the combination of a low government pension and a low superannuation balance will be inadequate).

Implications on the choice of regulatory instruments

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55 CLERP 6, above at n 45, 28.
56 The term losses here is to be interpreted loosely. Whilst the actuation of risk may cause actual financial loss of capital, loss in this context also connotes investment outcomes where the rate of return is positive but unexpectedly low.
57 Pearson, above at n 7, 101
Characterising members as ‘investors’ also exerts a strong influence on the regulatory instruments that are appropriate. The model was most clearly articulated in CLERP 6,

‘Regulation is aimed at ensuring that retail investors:

- Are provided with adequate information to make informed investment decisions ...
- Understand their obligations and the risks involved ...
- Have confidence in the standard and qualifications [of advisers and dealers]; and
- Are provided with appropriate avenues of redress in the event of fraud or negligence by financial intermediaries’

Disclosure thus becomes an important element of the regulatory mix, as does licensing of ‘product’ providers. Less attention was paid in the superannuation context to the need for avenues of redress. Disclosure is aimed at improving transparency. Few today would argue that transparency in the context of a superannuation fund is not a good thing. The concerns expressed as recently as 1965 in Re Londonderry’s Settlement about the impact on family harmony of exposing the decisions of trustees to scrutiny seem more relevant to the novels of Trollope and Austen than to the operation of a modern financial institution such as a superannuation fund. However relying on disclosure has some unique consequences in the superannuation context.

The first is that disclosure relies on members being capable of using the information they are provided to make appropriate decisions. It is troubling therefore that there is widespread acceptance of the proposition that many superannuation fund members are ill-equipped to make the decisions expected of them. It is even more troubling that this belief is supported by an accumulating body of empirical research demonstrating that superannuation fund members do in

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59 CLERP 6, above at n 45, 27 – 28.
60 The Superannuation Complaints Tribunal has provided avenues of redress for individual superannuation fund members in respect of certain grievances (primarily those related to decisions of the trustee) since 1994. See Carol Foley, ‘The Role of the Superannuation Complaints Tribunal’ in Susan Kneebone, (ed) Administrative law and the rule of law: still part of the same package?, (Australian Institute of Administrative Law, Canberra, 1998) Members also have access to the remedial provisions of the SIS Act and the Corporations Act.
62 For further discussion, see below in Part 3.
63 The discussion here does not directly address the problems identified by Gallery and Gallery in a series of papers concerning the quality and relevance of the financial information actually provided in superannuation fund disclosures. Unless those shortcomings are deemed unavoidable, they stem from poor implementation of the regulatory policy rather than shortcomings of disclosure as a regulatory instrument per se. See for instance, Gerry Gallery and Natalie Gallery, ‘Inadequacies and Inconsistencies in Superannuation Fund Financial Disclosure: The Need for a Principles-Based Approach’, (2003), Australian Economic Review, 36(1), 89.
fact make poor choices in regards the disposition of their superannuation funds assets. 65

Ironically, the Wallis Committee recognised this problem. It noted,

‘In a market economy, consumers are assumed, for the most part, to be the best judges of their own interests. In such cases, disclosure requirements play an important role in assisting consumers to make informed judgments. However, disclosure is not always sufficient. For many financial products, consumers lack (and cannot efficiently obtain) the knowledge, experience or judgment required to make informed decisions ...’ 66

Remarkably, it did not address this market failing, beyond recognising that in many cases third parties or, as a last resort, the government would provide assistance.

Some argue that poor decision-making on the part of superannuation fund members reflects inadequate financial literacy and that a program of education could address this problem. 67 There is no doubt that some education is likely to improve the general level of financial decision-making. However it would be naïve to assume financial literacy programmes can solve the problem entirely. For a start, there is there is a problem around what constitutes financial literacy: what sorts of knowledge and skills does a person need to be able to participate in the decision processes implied in the regulatory regime, and how does the acquisition of that knowledge and those skills fit into the financial literacy ‘curriculum’? 68 More fundamentally, there are both psychologists 69 and experienced market practitioners 70 who argue that members’ decisions reflect ‘irrational’ biases innate to human decision-making and cannot therefore be ‘educated’ away.

The apparent ‘irrationality’ may also reflect institutional factors, including problems in the incentive structure of the industry. Consider, for a moment, the life-cycle of a superannuation fund member. Making relatively uncontroversial

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66 Wallis above at n 45, 192.


68 The Australian government-sponsored Financial Literacy Foundation has identified superannuation as one of nine topic areas relevant to personal financial literacy, but there is an interdependence across the topics which mean that mastery of the superannuation section also requires mastery of other areas, such as investment and saving. The Foundation’s consumer website can be found at www.understandingmoney.gov.au


70 See for instance Arun Abey and Andrew Ford, How much is enough?, (A&B, Sydney, 2007) and the research cited therein.
assumptions about the pattern of their contributions and of investment returns, each contribution will make approximately the same contribution to the terminal value of their superannuation balance on retirement. Getting it right early matters. However research shows that younger members are typically less engaged in making decisions concerning the disposition of their superannuation entitlements, partly because retirement is perceived to be a distant issue and partly because their accumulated balance is comparatively small. Moreover, education can be expected to have less impact when the subject matter is believed to be irrelevant. Direct intervention in the form of personal financial advice might be more effective, but advice is typically only realistically available towards the end of the life-cycle, at a point where the accumulated balance has reached a quantum such that the commission earned by an adviser is attractive. Ideally, mechanisms would exist to ensure the advice was available at the start of the life-cycle, where it could be expected to have greatest impact on the investment strategy pursued over the life of the member. The structure and operation of today’s industry mitigate against this. It is perhaps not surprising that addressing this problem was one of the key recommendations of the Parliamentary Joint Committee’s on Corporations and Financial Services report into superannuation in 2007.

However, there is an even more fundamental problem with relying on disclosure in the superannuation context. Investors are expected to judge for themselves whether they understand the information being disclosed to them. If they don’t understand the information, they can choose not to invest. However ‘not investing’ is not an option for the majority of superannuation fund members. For them, some level of superannuation contribution is compulsory. If, as seems to be the case, the failure of disclosure is systemic (though undoubtedly more severe in some cases than others), the absence of this crucial ‘safety’ valve is very serious.

Finally, there is no distinction between the regulatory treatment given to different financial products. As the Parliamentary Joint Committee noted,

‘Finding a one-size-fits-all model that could be practically used by product issuers offering a diverse array of financial products could potentially create more problems than it solves.’

It is also not obvious that the same treatment should be accorded even within the superannuation arena. Should for instance the same reliance be placed on disclosure for those ‘products’ designed for discretionary superannuation investment and the ‘products’ used to accommodate the compulsory contributions

71 Simplistically, that salary growth and net investment returns (after fees and taxes) are paced at similar levels over the life of the member, allowing for the impact of the greater volatility of investment returns on compounding. Note this is equivalent to saying that the future value of all contributions is approximately equal under the simple assumptions outlined.

72 Finsia, above at n 64.

73 Parliamentary Joint Committee on Corporations and Financial Services, The structure and operation of the superannuation industry, 2007

74 The Parliamentary Joint Committee report came to the damning conclusion that,

‘it [is] widely acknowledged through the inquiry that product disclosure statements (PDS) are often not suitable for general consumption ... Although they may be legally compliant, PDS that are long, complex, difficult to compare and have key information lacking prominence, do not serve the purpose of communicating effectively with consumers. The public is overwhelmingly put off by such material and anecdotal evidence conveyed to the committee suggested that they ordinarily do not read it.’

Parliamentary Joint Committee, above at n 74, 6.119 - 6.120.

75 Parliamentary Joint Committee, above at n 74, 6.143
required under the superannuation guarantee levy? It seems, for instance, more acceptable to characterise the member as an ‘investor’ in the first instance than it is in the second.

This is not to be critical of the PDS regime as means of achieving adequate disclosure. There was considerable criticism of the prospectus regime it replaced. It would be hard to find fault with ASIC’s ‘Good Disclosure Principles’. Instead of providing formal rules of inclusion, definition, presentation or exclusion, ASIC requires that information be presented in a clear, concise and effective manner and that it be timely, relevant and complete, promote product understanding and comparison, highlight important information and have regard to consumer’s needs. This approach gives trustees considerable scope to assess the needs of their members and to tailor the content and form of their PDS appropriately.

Rather the argument here has to do with the over-reliance on disclosure as a regulatory instrument in the superannuation context. Analysis of the effectiveness of the FSR reforms has tended to focus on the content of the disclosure, and on whether it has been cost-effective. Less attention has been placed on whether the regime has been effective in reducing the risk to the consumer. Unfortunately the empirical research described above, and also anecdotal evidence arising from the failures of Fincorp, Westpoint and Australian Capital Reserve, suggests that it has not been wholly effective.

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76  Kingsford Smith, above at n 48.


79  In some cases this has been because artful structuring of the investments (eg as promissory notes in the case of Westpoint, debentures in the case of Fincorp) allowed the PDS disclosure regime to be bypassed. In others, it appears there were deficiencies in the information originally disclosed in prospectuses (e.g. Australian Capital Reserve). Statement by Tony D’Aloisio, Chairman of ASIC to the Senate Standing Committee on Economics, 30 May 2007, available at http://www.asic.gov.au. ASIC has recently moved to address these examples in Regulatory Guide 69: Debentures—improving disclosure for retail investors, October 2007, but this does not address the broader problem.
3. **The Public Model**

The past twenty years have seen superannuation assume an ever greater ‘public’ nature. Within ten years most retirees will derive a material part of their post-retirement income from their superannuation ‘nest egg’, a major ‘privatisation’ of the welfare system in Australia. The ‘compulsory’ nature of superannuation is important also, and in a number of ways. It distinguishes the Australian system from others, such as the US and UK, where coverage may be widespread but is not mandated universally by government. Further, it consolidates the argument that superannuation fund members are not volunteers, and deserve different treatment to that traditionally accorded beneficiaries under trust law. It also influences the intensity of focus expected by Parliament of its appointed regulators, such as APRA and ASIC. As the Wallis Committee noted,

> ‘compulsory contributions and tax assistance for superannuation … arguably combine to imply that government should provide greater regulatory assurance in relation to superannuation than would normally apply for market linked investments’.

With superannuation’s public nature comes the prospect of a set of principles quite distinct from those present in the Traditional and Public Models. There can be little doubt about the existence of a contest between the Traditional and Investor models. There is however an open question whether the Public Model has earned a place in this contest, or whether it remains peripheral and of little relevance to the broader question of characterising the superannuation fund member.

**The member as ‘citizen’**

It seems obvious that the trustees of superannuation funds have been delegated significant responsibility for the administration of two of the three ‘Pillars’ of the government’s retirement incomes policy. If so, trustees of superannuation funds are, collectively, playing a role that includes a public nature. Ought they not therefore be subject to some extent to the principles that govern public officials? Does this in turn, give members a different set of rights than would otherwise accrue under traditional trust law? Professor Kingsford Smith has suggested as much,

> ‘the superannuation trust has a significant public nature despite its legal form … Should fund trustees remain unaccountable and unsupervised in the exercise of discretions … when superannuation has become a privatised version of some aspects of social security?’

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81 Minister’s Introduction in *Options for Improving the Safety of Superannuation; Issues Paper*, 2001, iii, and *Options for Improving the Safety of Superannuation; Background Issues*, 2001, 2.

82 Wallis, above at n 44, 193.

83 They are both regulated entities and prudential guardians. This makes them an interesting example of what Professor Black has termed ‘de-centred’ regulation. Julia Black, ‘Mapping the Contours of Contemporary Financial Services Regulation’, (2002) 2 Journal of Corporate Law Studies 253.

84 Above at n 27, 434. Cf Senate Select Committee on Superannuation and Financial Services, *Prudential Supervision and Consumer Protection for Superannuation, Banking and Financial Services, First Report*, (Senate Printing Unit, Canberra, 2001), where the Senate Select Committee concluded that,

> ‘in most cases, there are already sufficient mechanisms in place for fund members to hold trustees accountable for their actions.’
As we shall see below, the courts have been reluctant to extend the types of accountability to stakeholders found in administrative law into the superannuation arena. In particular they have so far been unimpressed by the argument that they should apply administrative law principles such as ‘procedural fairness’ and ‘reasonableness’ to the exercises of discretion by trustees of superannuation funds. They have preferred instead to apply traditional trust law obligations on trustees, albeit having regard to the context in which those obligations arise. The SIS Act does not remedy the situation.

There are however two areas in which the Public Model does appear to be evident. The first is in the way the SIS Act operates. The second is the presence of a requirement for ‘equal representation’ of members and employers on the boards of superannuation funds. Whether these factors influence courts in the future to look upon the public nature of the trustee’s role more favourably remains to be seen. Certainly neither have had a decisive impact thus far. However, it is worth noting that the Administrative Appeals Tribunal has recently taken cognisance of the unique context in which superannuation trustees operate to apply principles of statutory construction of a more administrative law flavour to the interpretation of key provisions of the SIS Act in re VBN and APRA.\(^{85}\)

**The impact of administrative law on the exercise of discretion by superannuation trustees**

Administrative law attempts to regulate the behaviour of bodies that exercise public responsibilities. It emphasises procedural fairness in decision-making by public bodies as a way to promote their accountability. There is no equivalent requirement in trust law. Nor can superannuation’s statutory regime supply the deficiency. Indeed the impetus in trust law for holding trustees accountable for their decisions is weak indeed. This weakness belies the public nature of superannuation.

A number of commentators have seen an appeal to administrative law principles as a way around the restrictive approach of trust law.\(^{86}\) Administrative law has a similar focus on the exercise of discretion by an individual (or body). Not surprisingly therefore, there are a great many parallels. Like trust law, administrative law proscribes acting for an improper purpose,\(^{87}\) acting otherwise than in good faith,\(^{88}\) and acting under dictation.\(^{89}\) However administrative law has two other broad themes that are attractive to those who would seek to employ it in a superannuation trust context. Procedural fairness,\(^{90}\) sometimes summarised as ‘natural justice’, is a priority of administrative law. So too is the requirement of ‘reasonableness’.

Turning first to procedural fairness, it is important to note that though the lay meaning of the term is potentially quite wide-ranging, the sense in which it is used

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85. [2006] AATA 710.
86. Kingsford Smith, D., above at n 27; Sir Robert Walker, above at n 18, 131. Indeed some commentators have even returned the favour, couching the duties of public officials as akin to ‘trusteeship’. See for instance, Paul Finn, ‘Public Trust and Public Accountability’ (1994) 3 Griffith Law Review 224, 228.
89. R v Stepney Corp [1902] 1 KB 317.
in administrative law in Australia is not. It refers primarily to the operation of two rules; the ‘hearing’ rule and the ‘bias’ rule.\textsuperscript{92} The requirement that a decision-maker provide a person who will be affected by the decision an opportunity to be heard prior to the decision being taken is quite foreign to traditional trust law.\textsuperscript{93} A trustee can solicit and receive input from beneficiaries but there is no obligation to do so, absent a provision in the trust instrument to that effect. All that a member can expect is that the trustee will give real and genuine consideration to the matter,\textsuperscript{94} which may in some cases require the trustee to seek information from the member. The ‘bias’ rule is even more problematic for superannuation trustees. As Sir Robert Walker has pointed out,\textsuperscript{95} conflicts of interest are endemic in superannuation trusts. Indeed as a later section highlights, the statutory requirement for ‘equal representation’ actually creates conflicts in Australia in many cases.

The requirement for ‘reasonableness’ in administrative law is often linked to Lord Greene MR’s statement in \textit{Associated Provincial Picture Houses v Wednesbury}\textsuperscript{96} that:

\begin{quote}
`The court is entitled to investigate ... whether [the decision-maker] has taken into account matters which they ought not to have taken into account, or conversely, have refused to take into account or neglected to take into account matters which they ought to have taken into account ... [or has] come to a conclusion so unreasonable that no reasonable [person] could have come to it.'\textsuperscript{97}
\end{quote}

Courts in the UK, have expressly endorsed this bi-furcated principle (often termed the \textit{Wednesbury principles}) in the pension context\textsuperscript{98} and in trust law generally.\textsuperscript{99}

The situation is not so clear in Australia. The courts in Australia have adhered to the grounds identified in \textit{Karger v Paul}\textsuperscript{100} for judicial review of a trustee’s exercise of discretion: if the trustee failed to act in good faith, acted for an ulterior purpose or failed to give real and genuine consideration to the matter.\textsuperscript{101} The court may also intervene if, the trustee having disclosed reasons, those reasons are not sound.\textsuperscript{102} The courts, reluctantly it seems at times, also recognise the ability of settlors to include provisions in the trust instruments that expressly limit or preclude the provision of information to members.\textsuperscript{103}

\begin{footnotesize}
\begin{itemize}
\item\textsuperscript{92} Mark Aronson, Bruce Dyer and Mathew Groves, \textit{Judicial Review of Administrative Action}, 3\textsuperscript{rd} edn, (Lawbook Co., Sydney 2004) at 370.
\item\textsuperscript{93} \textit{Karger v Paul} [1984] VR 161.
\item\textsuperscript{94} \textit{Partridge v Equity Trustees Executors and Agency Co} (1947) 75 CLR 149; \textit{Karger v Paul}, above at n 93.
\item Walker, above at n 18.
\item \textit{Associated Provincial Picture Houses}, above at n 91.
\item \textit{Associated Provincial Picture Houses}, above at n 91, per Lord Greene MR, 234.
\item \textit{Edge v Pensions Ombudsman} [1999] 4 All ER 546.
\item \textit{Sieff v Fox} [2005] EWHC1312.
\item Above at n 93.
\item \textit{Telstra Super}, above at n 27; \textit{Asea Brown Boveri Superannuation v Asea Brown Boveri} [1999] 1 VR 144.
\item \textit{Rapa v Patience} (1985), (unreported, Supreme Court, NSW, McLelland J, No 2112 of 1981, 4 April 1985).
\item \textit{Tierney v King} [1983] 2 Qd R 580; \textit{Hartigan Nominees v Rydge} (1992) 29 NSWLR 405, per Sheller JA, 446.
\end{itemize}
\end{footnotesize}
What then of the Wednesbury principles? In Maciejewski v Telstra Super,¹⁰⁴ Windeyer J held that the decision of a trustee could be reviewed if the trustee could be shown to have come

’to a conclusion which no reasonable person could have come to on the material which was before it.’¹⁰⁵

This position appears now to be well accepted.¹⁰⁶ However in Telstra Super v Flegeltaub, Batt JA expressly distinguished what might be termed the ‘manifestly unreasonable’ ground from the ‘Hastings-Bass’ element of Lord Greene’s formulation. He said,

’I would reserve for another day the question whether the decision of a trustee of a superannuation fund … can be challenged on any grounds other than those stated in Karger v Paul, such as failure to direct itself correctly in law over and above addressing itself to the correct question, failure to take into account all relevant factors and taking into account an irrelevant factor. Such grounds smack very much of administrative law. That is an area of law far removed from the law of trusts.’¹⁰⁷

This reservation was echoed by Justice Barrett, speaking extra-curially. He professed the view that,

’any attempt to introduce Hastings-Bass thinking into this arena would … be to inject an entirely foreign and chaotic influence.’¹⁰⁸

It seems, then, that in Australia there remains a gap between the trust law and administrative law grounds for review of a decision-maker’s exercise of discretion. As McAlister concludes,

’It remains to be seen whether the groundswell experienced in the English courts will eventually capture us in its wake’.¹⁰⁹

The impact of the SIS Act on procedural fairness and reasonableness

The position just described would matter less if the statutory regime applying to superannuation supplied mechanisms for achieving the same ends. Unfortunately (for those who would seek administrative law-style accountabilities) the statutory regime does not require procedural fairness nor ‘reasonableness’, at least not directly.

Whilst not requiring procedural fairness per se, the SIS Act does provide for an enhanced level of transparency over that required by trust law generally. As noted in Part 2, the regulatory regime requires that superannuation fund members (and would-be members) receive certain prescribed information relating to their fund.

¹⁰⁴ Maciejewski v Telstra Super Pty Ltd (No 2) [1999] NSWSC 341

¹⁰⁵ Above at n104, at [21]. But cf, Meagher and Gummow who argue that unreasonableness may provide evidence of mala fides or a failure to exercise the discretion but is not of itself grounds for interference by a court. Rodderick Meagher and William Gummow, Jacobs Law of Trusts, (6th edn, Butterworths, Sydney, 1997), 1616.

¹⁰⁶ See for instance Sayseng v Kellogg Superannuation [2003] NSWSC 945 per Bryson J at [62]; Telstra Super, above at n 27, 284; Asea Brown Boveri, above at n 101. Also re HIH Superannuation, above at n 42, citing the High Court of Australia in Attorney-General v Breckler (1999) 197 CLR 83, which itself had cited Clerical Administrative and Related Employees Superannuation v Bishop, above at n 20 and Wilkinson v Clerical Administrative and Related Employees Superannuation (1997) 7 FCR 469.

¹⁰⁷ Telstra Super v Flegeltaub, above at n 27 at 285.


However disclosure of this type is a one-way communication. Decisions about how much and when to disclose are subject to the regulatory requirements, but much discretion is left in the hands of the trustee. Worryingly, the regulatory framework contains inconsistencies and lacunae that commentators have suggested ‘presents scope for trustees to manipulate disclosures, thus potentially misleading fund members and adversely affecting their decisions’.

The obvious way for a member to address any perceived deficiencies in the information they have received is to pose questions to the trustee. On the face of it, members can expect answers to questions they have about the fund and their interests therein. Section 52(2)(h) of the SIS Act, as amplified by reg 4.01 of the SIS Regulations, invokes s1017C of the Corporations Act 2001. Section 1017C provides that a concerned person (defined to include a member) has the right to request and then receive such information as might reasonably be required to understand the main features and investments of the superannuation fund and to make an informed judgment about the management, financial condition and investment performance of the superannuation fund of which they are a member, as well as their personal benefit entitlements. This provision is fortified by s101 of the SIS Act which requires trustees to have a procedure in place to ensure any complaints or enquiries are ‘properly considered’ within 90 days.

The problem is that reg 4.02 of the SIS Regulations notes that internal working documents of the trustee are not included in the definition of the information that must be provided. The practical effect of that limitation is that members have little opportunity to seek information not contained in the standard disclosures. A brooding silence is thus almost guaranteed except where there is a material event to act as a catalyst, justifying recourse to an external party, such as a contested disability claim or an industrial dispute.

This situation contrasts quite markedly with the comments of the then Treasurer, the Honourable John Dawkins MP, when introducing the SIS Bill to parliament, ‘The disclosure of adequate and appropriate information to members is a critical element in the prudential arrangements if members are to be in a position to exercise influence over the direction their fund takes’ (italics added).

The democratic timbre of these words finds an uncanny echo in the next section, in which the requirement for ‘equal representation’ is discussed.

‘Equal representation’ as evidence of public policy

Part 9 of the SIS Act provides for equal numbers of member and employer representatives on the trustee boards of superannuation funds. The requirement has a very ‘public’ flavour. Slightly tongue-in-cheek, it carries flavours of the ‘no tax without representation’ principle attributed to Bostonians in the era of the Boston Tea Party. Perhaps, as Paatsch and Smith conclude, it was simply a political accommodation required to secure employer and union support.

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114 The exceptions are public offer funds, small superannuation funds (between 4 and 50 members) and certain public sector schemes. Public offer superannuation funds are required to have either equal representation or an independent trustee; s93 SIS. Small superannuation schemes can choose amongst a range of options similar in effect to equal representation; s92 SIS.
for the precursor to the SIS Act, rather than a deliberate attempt to embed
democracy into superannuation fund governance.115 In any case, it projects a
democratic ideology that is not present in trust law (which is highly paternalistic)
nor in financial regulation (which is highly individualistic).

Such ‘representation’ is quite foreign to trust law. At trust law, beneficiaries of a
trust ordinarily have only very limited ability to influence the identity (or
membership, if a board) of the trustee of their fund, unless it is provided for in the
trust instrument. Absent some wrongdoing on the part of the trustee, the courts
have been reluctant to accede to beneficiaries’ requests to have a trustee
removed. 116 Beneficiaries also appear to have no grounds at general law to
nominate a person or persons to be trustee of their fund.

The situation in the arena of financial regulation is slightly different. The
constitutive documents of unit trusts usually provide limited rights to unitholders
to vote on the appointment or removal of the entity responsible for the unit trust.
Similarly the constitutive documents of a public company will usually grant
shareholders in the company certain rights related to the election and removal of
its directors. However in neither case does statute impose constraints on the
relative influence of the different stakeholders on the composition of the decision-
making organ(s) of the entity, as occurs with the ‘equal representation’
requirement in the superannuation arena.117

It is also worth noting that the rhetoric of “representation” is antithetical to
traditional notions of board membership. As Street J laid down in Bennetts v Board
of Fire Commissioners of NSW118

“It is entirely foreign to the purpose for which this or any other board exists to
contemplate a member of the board being representative of a particular group or a
particular body. Once a group has elected a member of the board he assumes
office as a member of the board and becomes subject to the overriding and
predominant duty to serve the interests of the board in preference, on every
occasion upon which any conflict might arise, to serving the interests of the group
which appointed him. With this basic proposition there can be no room for
compromise.”119

Like other boards of trustees, trustees of superannuation funds are expected to act
unanimously, unless otherwise specified in the trust instrument.120 The duty
trustees bear to act impartially means that they are also expected to act in the
best interests of the membership as a whole, and not in the interests of some
cohort or faction. This is a recurrent issue for trustees in the superannuation
arena. One needs look no further than Cowan v Scargill121 for a vivid illustration of
the frictions and pressures at play inside a trustee board composed of different
‘factions’.

115  Paatsch and Smith, above at n 33.
116  See Meagher and Gummow, above at n 105, 15.84-85, and cases cited therein.
117  Seen in this light, it is perhaps the presence of the employer representatives on the board of
a superannuation fund that is the anomaly, at least in the case of defined contribution funds.
118  (1967) 87 WN (NSW) 307.
119  Above at n118, 311. See also Cowan v Scargill above at n 24.
120  Luke v South Kensington Hotel Co (1879) 11 Ch D 121; Re Billington [1949] St R Qd 102; Cock
& Howden (Trustee of Cock) v Smith (1909) 9 CLR 773. As noted by Barrett J, in this they
differ from the boards of company directors, above at n 108.
121  Above at n 24.
Evidence of administrative law thinking in the way the SIS Act operates

The idea that, de facto, trustees exercise delegated responsibility for the regulation of superannuation gains some support from the way in which the SIS Act is designed.

As a start, the trustee is very firmly placed in the frame as the primary actor in the regulatory regime. However the SIS Act is very careful about the ways in which it seeks to influence the decisions of trustees. The derivation of an investment strategy for the fund (a key trustee obligation under both general law and the SIS Act) is a good example. The regulatory regime does not dictate the form the strategy will take. Section 52(2)(f) does however provide a set of criteria (a regard for risk, return, liquidity and diversification, and so on) to be applied by trustees in making that decision. Similarly s 52(2)(g) imposes a criterion on the formulation of a reserving policy but does not say what that policy must be. The approach of setting criteria for decision-makers is redolent of administrative law (and to a lesser extent statutory trust law).

In other areas the SIS Act is more prescriptive. So for instance Part 12 of the SIS Act imposes a set of very specific duties including a duty to keep minutes and records, to keep reports and to notify regulatory bodies of changes in the fund’s circumstances. These duties seem motivated by a desire on the part of legislature to facilitate regulatory review of the actions of their ‘delegate’ should the need arise. These provisions complement the licensing regime for trustees imposed by the FSR Act.

Other prescriptive duties are designed to ensure funds have minimum governance standards. These include complaints resolution procedures, board composition, and the nature of contractual arrangements with agents, such as investment managers. Again this focus on process, rather than substance, is characteristic of both administrative and trust law. However its prescriptive nature is foreign to trust law.

The thin end of the wedge?

Whilst the courts have been reticent to apply administrative law principles to the decisions of trustees of superannuation funds, in re VBN and APRA the Administrative Appeals Tribunal chose to interpret the provisions of the SIS Act (specifically s52(2)(c)) in the light of administrative law principles. The Tribunal saw the administrative law context of s52(2)(c) as severing the connection between s52(2)(c) and its trust law antecedents, identifying ambiguity in the phrasing used by the Treasurer in introducing the Bill to justify this approach. Several authors

122 See for instance Strengthening Super Security, above at n 113.
123 Re Boston’s Will Trust [1956] Ch 395 per Vaisey J at 405.
124 This is usefully contrasted with the PDS content requirements described briefly in Part 2 above. In that context, the regulator has mixed qualitative guidelines with specific items to be included.
125 Section 103.
126 Section 105.
127 Sections 106 and 106A.
128 For instance Section 101.
129 Sections 107 and 106A. Also the SIS Act Part 9, discussed briefly above.
130 For instance ss116, 124, 125.
131 Above at n 85.
132 Above at n 85, [323].
have voiced concern with this finding 133 and, with respect, the ambiguities identified by the Tribunal are capable of more obvious interpretations.

The Tribunal’s decision has not yet been considered by the courts, but it does contrast the courts’ approach in cases such as Invensys v Austrac Investments,134 Australian Securities Commission v AS Nominees 135 and Knudsen v Kara Kar,136 in which no administrative law gloss was placed on the interpretation of the provisions.

That said, the idea that the interpretation of relevant statutory provisions might be influenced by considerations from administrative law is an interesting one. It would receive support from the ‘purposive’ approach to statutory interpretation required by Section 15AA of the Acts Interpretation Act 1901, but only if the proposition is accepted that superannuation fund trustees are performing quasi-public role.

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134 (2006) 198 FLR 302


4. Risk and the Member

One of the most important ways that the three models outlined above differ is in the way they allocate risk amongst the actors. At first blush the trustee bears much of the risk in the Traditional Model, and the member bears it in the Investor Model. The reality is rather more complex. And in the Public Model regard must be had for exogenous factors.

The Traditional Model

The paternalistic stance of the Traditional Model ostensibly sees much of the financial risk borne by the trustee(s). At its extreme it would see the trustee bear the risk of under-delivery of financial benefit (whether through imprudence, waste or misadventure) personally.

The vast size of many superannuation funds makes the idea of trustee liability, even with trustee insurance, somewhat theoretical save for breaches that are small or affect a relatively narrow cohort of members. This is a reality that even the capital adequacy requirements of the trustee licensing regime cannot address. For example, suppose that the investment policy applied to the default option of a $10bn superannuation fund was implemented with a delay that caused a permanent loss in potential earnings of 2% for members. The amount required to make good the trust would be of the order of $150m, well beyond the capital required under the regulations (and presumably the personal assets of the trustees).

There is a further challenge in this Model; identifying the appropriate measure of recompense. (Risk after all involves not just the incidence of occurrence but its likelihood and magnitude). This is more complicated than it sounds. To establish a good claim against the trustee, the aggrieved member must first show a breach of one or more of the trustee’s obligations. This is an ex ante judgment. That is to say, the breach is not established by the actuation of loss (or disappointment of legitimate expectation) but by some failure in the process by which the investment strategy was decided and implemented. As Lindley LJ noted in Re Chapman, a trustee is not ‘...a surety, nor is he an insurer; he is only liable for some wrong done by himself, and loss of trust money is not per se proof of such wrong’

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137 For the sake of simplicity, the discussion that follows assumes that the funds are defined contributions funds. In the case of a defined benefit fund, the risk may be borne by the sponsoring employer rather than the member, depending on the solvency status of the fund at the time in question. In the US and UK, but not Australia, there may also be pension benefits guarantees to take into account.

138 In practice, of course, most superannuation fund trustees are covered by some form of indemnity, either from the trust or via indemnity insurance, so the extent of their exposure is limited to the mismatch, if any, between the terms of the indemnity and their liability for the breach of trust.

139 Assuming approximately 66% of the assets of the fund were invested in the default option, which is approximately the industry average (excluding retail funds for which choice is a basic design feature); APRA, Annual Superannuation Bulletin 2006, at 31. Note, such a slippage would be relatively easy to incur - a delay in implementing a currency hedge over 20% of the portfolio during which the currency appreciates by 10% would have this impact (ignoring interest rate differentials).


141 [1896] 2 Ch 763
The SIS Act attempts to set out some qualitative standards for trustee actions. Most pertinently, s52(2) codifies some of the general law obligations of trustees, breach of which would ceteris paribus give rise to an action seeking recompense. Section 52(2)(f) in particular would appear to assist members seeking to impugn their trustee for what they deem to be an inappropriate investment strategy. On its face, s 52(2)(f) provides guidelines to assist trustees in the design of their investment strategies. It implies into the constitutive documents of the trust a covenant that requires the trustee to have regard for a variety of factors relevant to the formulation of an appropriate investment strategy, such as risk, return, liquidity and diversification. This would appear to give members some specific indicia they could use to identify a breach. However the drafting specifically requires the investment strategy only ‘to have regard to’ those factors, which is a very low threshold requirement indeed. And the trustee has a statutory defence under s56(5), if they can show that they complied with s52(2)(f) when they formulated the investment strategy. So the member’s task will not necessarily be an easy one, comprising both evidential and legal hurdles.

Moreover, whether the act (or omission) of the trustee constitutes a breach will be judged according to the standards of the time. Thus for instance, in Nestle v National Westminster Bank plc the English Court of Appeal declined to impugn a trustee whose investment strategies over a forty year period failed to deliver the investment performance that a trustee with knowledge of modern investment practices might reasonably be expected to have delivered. Rather, the trustee was expected to apply the thinking relevant at the time. This principle remains good today, even with the intervention of s52(2)(f), because its open-ended nature (it specifically notes the criteria are ‘not limited to’ those listed) anticipates the possibility of other criteria, such as those established as relevant by a new theory of investment, being relevant. So members cannot use hindsight to justify their claims of breach.

Assuming the existence of a breach is established, then the question of the quantum come into play. The trustee in breach is then required to make good the trust. This in practice means that the court will attempt to identify the position the trust would have been in had the assets not been abused. The trustee may also, if the breach gave rise to a benefit they enjoyed, have to disgorge the profit, notwithstanding that the trust may not have been able to enjoy the benefit.

There is another subtlety to be considered, though in this case it operates in favour of the member. If an investment is found to be in breach of trust (eg for not being a permitted investment under the deed) the loss suffered by the trust on that investment cannot be offset against better than expected performance from another part of the investment portfolio. This is despite the likelihood that the courts would accept the relevance of modern portfolio theory in judging whether a breach had occurred in the first place. The courts will accept that some investments in the portfolio did not perform as well as expected, and that such

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142 Section 56(5). There is however a moot point whether the specific terms of s52(2)(f) eclipse the broader obligations to ‘act in the best interests’ (s52(2)(c)) and to exercise due ‘care, skill and diligence’ (s52(2)(b)).

143 [1994] 1 All ER 118.

144 Unlike in contract, at trust law there is no requirement of causation connecting the breach to the size of the shortfall; liability in that sense at least is strict.


146 Regal (Hastings) Ltd v Gulliver [1967 2 AC 134.
underperformance does not, *ipso facto*, constitute imprudence (or some other breach). However once a breach is established, liability for recompense flows irrespective of the performance of the rest of the portfolio.

Risk, then, in the Traditional Model is not wholly borne by the trustee. The complexities of establishing a breach of trust dilute slightly the otherwise paternalistic assumption of responsibility by the trustee under this model.

**The Investor Model**

In the Investor Model the member ostensibly bears the risk of investment. Only if the trustee breaches a contractual obligation, or breaches a statutory obligation, does the investor have a right to seek recompense. Disclosure of relevant information, so that the investor is in a position to make the best decision, is key for the trustee, but the member bears the risk of assimilating and applying that information to suit their needs. However the open-textured drafting of guidelines in the Corporations Law, and ASIC’s interpretation in relation to PDS and other disclosures in this case arguably operate in favour of disgruntled members. They could, for instance, be interpreted expansively by a court minded to find in favour of a vulnerable member. Moreover the statutory requirement does not require the member to demonstrate that they would have decided differently if they had received the appropriate information, nor that they relied on the information they did receive. So the burden of risk on the member, as investor, may be lighter than appears on the surface.

The ‘individualisation’ inherent in the Investor Model also serves to fragment the experience of superannuation fund members more than is the case in the Traditional Model. The likelihood that some members have inadequate superannuation balances (and no recourse to recompense for the shortfall) is arguably greater in the Investor Model. Against this, Wallis et al would argue that the average balance is higher in the Investor Model because of the efficiency of a more competitive market and economy. The conclusion an individual reaches about whether this is desirable is ultimately an ethical one.

**The Public Model**

The definition of risk in the Public Model is somewhat broader than in the other two Models. The primary concern of the Public Model is that the public policy underlying superannuation be achieved. If, for the sake of simplicity, we assume that the public policy behind superannuation is to provide a vehicle for the accumulation of assets necessary to fund an adequate level of post-retirement income for retirees, then risk is defined in terms of the potential for shortfall relative to this objective.

The factors that constitute risk in this Model are distributed across a variety of actors. The trustees in effect act as guardians of the assets as they accumulate, bear risks in a way that is similar to those under the Traditional Model, albeit with an enhanced level of transparency and accountability. Members, though, bear the risk of under-contribution relative to peers.147 And ultimately, should the retiring cohort on average fall short of adequate provision, the democratic process will see that welfare issue resolved on the political stage through adjustment of factors exogenous to superannuation such as tax rates and the level of the Age Pension.

**Taken Together**

The regulatory scheme affecting superannuation is an amalgam of the three Models. Members are neither fully under the wing of paternalistic trustees securing

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147 M Scott Donald, ‘Comment on Adequacy of Superannuation’ [2007] *Jassa* 25 (Autumn)
their best interests, nor are they forced to fend for themselves amongst the wolves and predators of the market as investors. And, thanks to the public nature of superannuation, they are also inextricably linked to the success of the system as a whole. That the balance currently appears to have swung in favour of the informed, self-reliance stance of the Investor Model is perhaps the result of eleven years of Conservative government in Australia, and perhaps the pendulum will swing back towards more paternalistic models while the Labor government holds sway; time will tell.

**Concluding comments**

Writing in what today seems like the dark ages, before the SIS Act, the FSR Act and Choice of Fund, Paatsch and Smith commented that

‘[T]he change in the raison d’etre for superannuation has resulted in a legislative and regulatory regime which is complex, inequitable and precarious from the point of view of beneficiaries of superannuation schemes’¹⁴⁸

The reforms of the past fifteen years have gone some way to addressing the perceived inequities and the precariousness of the system. That they should have done so at the expense of even greater complexity was perhaps inevitable. What was not inevitable was that the reforms should exacerbate the patchwork appearance of the superannuation regulatory scheme because of the profoundly different way in which the key stakeholder, the member, was characterised.

One result is a situation in which the member could be excused a crisis of identity. There is a pronounced dissonance between the protective, paternalistic rhetoric of “trust”, “trustee” and “beneficiary” and the individualistic, self-sufficiency of “product” and “consumer”. And neither reflect the Orwellian dehumanisation inherent in the term “responsible entity”.

These differences are of more than semantic interest. They fundamentally affect the types and levels of protections available to members. For instance, disclosure, the lynch-pin in the Investor Model, is of less relevance in the Traditional Model because paternalism renders self-reliance by members less important. Similarly, procedural fairness, a central feature of the Public Model, barely features in the Investor Model in which members themselves determine both their fund and the investment strategy within that fund. The allocation of risk across the system is fundamentally affected by these influences.

These illustrations should not be taken to imply that they are the only area where the characterisation matters. The responsibilities of trustees in respect of member investment choice, an issue raised by both APRA and, more recently, the Joint Committee, ¹⁴⁹ is another area. So too is the provision of individual financial advice to members and the overall trend towards ‘corporatisation’ of superannuation fund governance following the advent of Fund Choice.

Nor should the observations in this paper be taken to suggest that any of the characterisations of superannuation fund members, whether as beneficiaries, employees, citizens, consumers or investors, is correct. They each have strengths and weaknesses. Crucially, though, each has contributions to make. It is important, then, that we do not allow any of them to eclipse the others as we seek to find a balance that safeguards the legitimate expectations of all participants in the system.

¹⁴⁸  Paatsch and Smith, above at n 33, 131.
¹⁴⁹  Joint Committee, above at n 73.