

# Keeping Super Safe

A call for greater transparency from superannuation funds

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## **About the author**

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## Executive Summary

Disclosure levels by Australian superannuation funds are inadequate. Disclosure levels should meet international benchmarks to adequately protect Australians' superannuation savings.

The role of some Australian superannuation industry funds as 'default' funds in Australia's industry relations system constitutes government-granted special financial privileges. While customers can opt-out of industry funds defaulted by the industrial award system, few do so.

The poor disclosure means that Australians who have their retirement funds tied up in superannuation funds do not have access to information necessary to understand where their money is invested and what expenses are being paid from their superannuation savings. This lessens competition in the sector.

There is strong international and domestic evidence to show that superannuation funds and/or trust arrangements can be subject to abuse. There is nothing inherently 'safe' about the trust arrangements under which superannuation funds are managed.

Particular attention must be paid to situations where financial power is concentrated. Safeguards must be inbuilt to minimise the ability of well-connected political players to manipulate the system to favour particular investment funds, managers or individuals. A basic safeguard is enforced high-level disclosure of how Australians' superannuation moneys are used.

This report calls for new laws that will force Australian Prudential Regulation Authority (APRA) regulated superannuation funds to comply with extremely high standards of disclosure and transparency.

A fund member, investment advisor, or member of the public, should be able go into the website of any retail or industry superannuation fund and obtain enough information so they can understand where their money is invested, how it is performing relative to similar funds, who gets paid to manage and administer the fund, and how much is paid, and whether the fund's trustees have any cross-directorships.

## Introduction

No Australian should automatically accept that their superannuation retirement nest-egg is safe. As in all things financial, a healthy level of scepticism is warranted and needed when other people have control of money. The greatest safeguard that individuals have over their money is that the people who control their money disclose precisely what they are doing with it. There must also be full disclosure of fees and commissions that superannuation investment controllers receive.

This is a report into the disclosure and transparency levels of Australian superannuation funds. We find that the disclosure levels are inadequate to allow members to understand where their money is invested and what expenses are being paid from their superannuation savings. Superannuation fund transparency is not good enough.

This report does not allege that the financial results claimed and reported by Australian superannuation funds are false or in any way inaccurate. Neither does this report allege any wrongdoing, malpractice or poor decisions of any sort, by any of the persons or organisations responsible for, or managing, superannuation fund money. This report is entirely focused on disclosure and transparency.

This report calls for new laws that will force superannuation funds to comply with extremely high standards of disclosure and transparency.

This report is focused on the transparency and disclosure practices and outcomes of industry and retail superannuation funds only, with a heavier emphasis on industry funds. For this research exercise we have not investigated non-industry public sector funds, corporate or SMSFs.<sup>1</sup>

The reasons for the focus on just these two types of funds are as follows:

- Industry and retail funds exercise control over half of all fund assets (\$548 billion) and have by far the largest number of fund members (27 million accounts).
- Old style public service and corporate pension funds (defined benefit funds) are largely closed to new members.
- In most cases industry and retail fund members do not have any control over the people who manage their money. Usually members do not elect managers/trustees and cannot dismiss them. Their only power is to remove their money and place it in another (similar) fund structure. This compares starkly with SMSFs where (mostly) the people who control the funds (trustees) are also the fund members. That is, SMSF arrangements allow fund members to directly control their money through the trust arrangement.
- The retail and industry funds control the assets of some 27 million fund holders, which is by far the largest bulk of fund members. Industry funds are the predominant default funds (see Table 5 and Table 6 below). That is, if workers do not choose their own fund, the industrial relations system requires their

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<sup>1</sup> Public sector funds are often now closed to new members and are sometimes 'unfunded', i.e. the governments pay benefits from consolidated revenue as they arise rather than accumulating investment funds that then pay out benefits.

money to go to specific funds. This gives the default funds massive institutional market power and advantage over non-default funds. In many respects the default-fund process creates and sanctifies anti-competitive, oligopoly-like market power in superannuation.

Each of these reasons—size of the funds, fund member power imbalance and government mandated anti-competitive arrangements—provides enough cause for high levels of disclosure and transparency. This should be mandatory as a ‘first base’ protective mechanism for Australians’ retirement savings.

# The Australian superannuation system

## Overview

In 1992, the Keating Government introduced compulsory superannuation for all Australian employees. Originally set at 3 per cent, since 2002 employers have been required to pay an additional 9 per cent of the wages they pay employees into superannuation funds.

The money is not the employers' money. It is employees' money that would have been paid to workers as part of higher wages if compulsory superannuation did not exist.

Workers are banned from touching their superannuation money until they retire or part-retire (usually only after someone is 55 years or older). There are laws about how and when workers can receive their superannuation money.

Superannuation funds are approved and regulated by the federal government. Funds are set up under, and must comply with, the *Superannuation Industry (Supervision) Act*. Superannuation funds must operate under 'trust' arrangements.

Trusts are legal 'business' structures commonly in use and subject to federal 'trust' laws. Trusts are controlled by 'trustees' who have a legal duty to run the trust entirely for the benefit of the people who have their money in the trust. An example would be where orphaned children may have money left to them from their deceased parents' estate which is held in a trust. The trustee must manage the money for the benefit of the children, although the trustee is permitted to take a fee for doing this.

Superannuation funds operate in much the same way. The fund trustees are appointed by the organisation/s that set up the trust. The fund members are the beneficiaries of the trust. A very small number of superannuation funds have elections for some trustees however most industry fund trustees are appointed by union and employer groups.

Since the *Superannuation Guarantee Act (SGA)* was introduced in 1992 (which made superannuation compulsory), superannuation funds have grown enormously. As of June 2009, total assets were around \$A1.1 trillion.<sup>2</sup> This is close to the size of Australia's economy (in terms of annual GDP). Contributions to the funds were \$112.2 billion in the year to June 2009.<sup>3</sup> The size of super fund assets is expected to exceed the size of the Australian economy by 2015.<sup>4</sup>

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<sup>2</sup> Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (Cooper Review). "Clearer Super Choices: Matching Governance Solutions." 2009, p. 4.

<sup>3</sup> Australian Prudential Regulation Authority (APRA). "Annual Superannuation Bulletin "as at June 2009, 2010, p. 6.

<sup>4</sup> Association of Superannuation Funds of Australia (ASFA). "Superannuation Statistics - March 2010." 2010.

## Fund types

There are 5 major types of superannuation funds, with assets of \$1.1 trillion and 32.7 million member accounts.<sup>5</sup>

### Retail Funds:

These were usually set up and run by major financial institutions such as AMP for example. Many of these funds were operating well before compulsory superannuation was instituted in 1992. At December 2009 there were 154 retail funds, with combined assets of \$346 billion and 16.6 million members.<sup>6</sup>

**Table 1: Top 5 Retail Fund Managers**

Name	Funds Size	Members
<b>AMP</b>	\$49.2bn	3,200,000
<b>ASGARD</b>	\$20.0bn	376,000
<b>MLC</b>	\$37.3bn	1,237,000
<b>Colonial First State</b>	\$34.9bn	588,000
<b>ING</b>	\$25.3bn	939,000

*Source APRA Statistics Superannuation Fund-Level Rates of Return, issued 20 August 2009*

### Industry Funds:

These were set up jointly by unions and employer associations—usually after 1992. Half of the trustees are appointed by unions and the other half by employer associations. Some funds also have one or two “independent” trustees. At December 2009 there were 65 industry funds with combined assets of \$219 billion and 11.6 million members.<sup>7</sup>

**Table 2: Top 10 Industry Funds by Size**

Name	Funds Size (\$m)	Members ('000)
<b>Australian Super</b>	29,623.9	1,427.9
<b>Unisuper</b>	24,448.6	419.6
<b>REST</b>	15,324.6	1,899.8
<b>Sunsuper</b>	13,559.3	1,167.3
<b>HESTA</b>	13,542.9	641.4
<b>Cbus</b>	12,920.2	561.9
<b>Health Super</b>	7,818.3	210.6
<b>HOST Plus</b>	6,986.2	884.2
<b>MTAA</b>	6,275.0	281.5
<b>Vic Super</b>	6,250.1	237.9

*Source APRA Statistics Superannuation Fund-Level Rates of Return, issued 20 August 2009*

### Self Managed Super Funds (SMSFs):

These are small funds with four or fewer members. Mostly the trustees are the fund members. Almost 70% of SMSF have 2 members. There are 420,000 SMSFs, with combined assets of \$386 billion and 800,000 members.<sup>8</sup>

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<sup>5</sup> Note: the number of fund members significantly exceeds the size of the Australian workforce (about 10.5 million) and the Australian population (21.8 million). The disparity simply reflects the fact that many Australians have money in several superannuation funds.

<sup>6</sup> ASFA. "Superannuation Statistics - March 2010." 2010.

<sup>7</sup> Ibid.

<sup>8</sup> Ibid.

### Corporate Funds:

These are typically run by large businesses for their employees. At December 2009 there were 171 corporate funds, with combined assets of \$60 billion and 650,000 members.<sup>9</sup>

**Table 3: Top 10 Corporate Funds by Size**

Name	Funds Size (\$m)	Members ('000)
Telstra	10,660.6	94.9
Commonwealth Bank	6,978.9	61.0
Qantas	5,873.5	32.3
NAB	3,102.6	30.5
Westpac	2,603.5	33.8
Rio Tinto	2,404.8	23.1
BHP Billiton	2,162.9	18.6
ANZ	1,771.8	29.9
Bluescope Steel	1,660.2	9.6
CSR	1,222.9	13.1

*Source APRA Statistics Superannuation Fund-Level Rates of Return, issued 20 August 2009*

### Government funds:

Government funds are run for public servants. At December 2009 there were 39 government funds with combined assets of \$173 billion and 3.1 million members.<sup>10</sup>

**Table 4: Top 6 Government Funds by Size**

Name	Funds Size (\$m)	Members ('000)
ARIA	18,491	471.5
First State	15,889	515.5
Local Gov Super	7,142	121.2
Australia Post	6,885	49.0
QLD Local Gov	4,041	72.7
Vision Super	4,000	102.8

*Source APRA Statistics Superannuation Fund-Level Rates of Return, issued 20 August 2009*

## Regulatory Structure

Three government bodies oversee and regulate the superannuation funds:

- The Australian Prudential Regulatory Authority (APRA)
- Australian Securities and Investment Commission (ASIC)
- Australian Taxation Office (ATO)

APRA approves the setup of superannuation funds. Both APRA and ASIC have statutory responsibilities to oversee the operation of superannuation funds. This is a part of their general oversight of the total financial system. They do not oversee self-managed super funds (SMSFs). This is undertaken by the ATO.

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<sup>9</sup> Ibid.

<sup>10</sup> Ibid.

## What are 'default' funds?

Since 2006, the law has required employers to give employees the right to choose the superannuation fund into which their money will go. However, under Australia's award and enterprise agreement system, if an employee does not make a choice, the contributions must be paid to the superannuation fund stipulated in the appropriate award or enterprise agreement. The award/agreement funds are known as default funds. The overwhelming majority of compulsory superannuation contributions are allocated to the default fund and within that to the default investment option.

Most of the so-called 'modern' awards include default superannuation fund clauses. The number of default funds varies between 1 and about 5 in each award (although the Educational Services General Staff Award manages to mandate 18 default funds). Each award superannuation clause also has a provision for existing employers to continue to pay into any fund they were already paying into as at September 2008.

An analysis of 166 'modern' awards highlights the dominance of Industry Superannuation as the default option.

**Table 5: Default Funds by Type**

Fund Type	Total Funds identified	Total times listed as default fund
<b>Industry</b>	66	477
<b>Retail</b>	16	38
<b>Public</b>	14	36
<b>Corporate</b>	2	3
<b>Unidentified</b>	9	12

*Source IPA analysis of 166 'modern' awards*

**Table 6: Major Default Super Funds**

Fund Type	Fund	Times listed as default fund
<b>Industry</b>	Australian Super	68
<b>Industry</b>	Sun Super	56
<b>Industry</b>	Asset Super	47
<b>Industry</b>	Tas Plan	44
<b>Industry</b>	Westscheme	26
<b>Industry</b>	State Wide	24
<b>Industry</b>	LUCRF	16
<b>Industry</b>	HOST-PLUS	14
<b>Industry</b>	HESTA	13
<b>Industry</b>	AustSafe	13
<b>Industry</b>	First State	12
<b>Industry</b>	REST	10
<b>Retail</b>	AMP Super Savings	15
<b>Public Sector</b>	Australian Public	6
<b>Corporate</b>	BHP	1

*Source: IPA analysis of 166 'modern' awards*

When the Senate Standing Committee on Education, Employment and Workplace Relations took testimony on the question of default funds strong concerns were expressed as to the lack of transparency in the process of choosing which funds gain the privileged positions as default funds.

For example, Mr Richard Gilbert, CEO of Investment and Financial Services Association (ISFA), put on record,

"IFSA's ... concern is the lack of fair and transparent process in the selection of default funds. A range of super funds made submissions to the commission to be included as default funds in a particular industry. This includes both industry and retail corporate master trust funds. In many cases, the commission has not agreed to their inclusion. This could have a substantial impact on the viability of these funds. IFSA is not aware of any rationale for the decisions by the commission. IFSA is not aware of any scope for excluded funds to appeal the decision of the commission.

The successor body to the commission, created by this bill, is Fair Work Australia. Division 3E of part 5-1 of the bill appears to prohibit appeals of decisions by the full bench of Fair Work Australia. The only review mechanism IFSA is aware of is the requirement that Fair Work Australia review the awards every four years."<sup>11</sup>

The Investment and Financial Services Association (IFSA) represents 145 financial organisations with more than \$1 trillion under management.

### ***Default funds – A concentration of financial power***

The number of industry and retail funds is expected to decline considerably in the medium term while the asset bases expand.

By 2025, total superannuation assets are expected to grow to \$2.2 trillion. The number of industry funds is expected to decline to 21, and the number of retail funds is expected to decline to 47.<sup>12</sup>

This will result in a heavier concentration of workers' money being controlled by a smaller number of financial managers and fund trustees in the retail and industry funds sectors.

There are concerns about the concentration of Australians' superannuation fund assets in a small numbers of hands. For example, Mr Gilbert, the CEO of IFSA argues:

... one of the strengths of the Paul Keating SG agenda was that diversification was critical to it. If we narrow where the money is, yes, there are more risks of systemic failure. <sup>13</sup>

IFSA expresses concern about "... concentrating monopolies in single-administrations systems." It gives the example of Japan "...where recent record-keeping errors by the centralized administrator of the pension system have caused havoc, to the extent that they have lost 50 million records, going back 20 to 30 years."<sup>14</sup>

These sorts of warnings strengthen the need for full disclosure systems by superannuation funds. Disclosure diminishes the opportunity of monopolies to behave inappropriately and increases the capacity for administrative error to be found early.

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<sup>11</sup> Senate Standing Committee on Education, Employment and Workplace Relations (EEWR). Fair Work Bill 2008 Hearings. Sydney, 18 February 2009, p. 50.

<sup>12</sup> Cooper Review. "Clearer Super Choices: Matching Governance Solutions." 2009, Appendix 1, p. 19.

<sup>13</sup> Senate EEWR. Fair Work Bill 2008 Hearings. Sydney, 18 February 2009, p. 52.

<sup>14</sup> Ibid, p. 50.

## The Industry Funds industry

### *A tangled web of control*

Industry funds are a special case. They make up 84 per cent of award default funds putting them in a privileged and powerful financial position in the Australian finance sector. It should be expected that their levels of disclosure is extremely high.

However the structure and interrelationships of the funds and their fund managers is little understood. What is disclosed through their websites and free public publications is relatively superficial. It required ASIC searches to reveal much of the following information.

As at 31 December 2009 the 65 industry superannuation funds controlled \$219 billion in Australians' retirement savings. The 10 largest industry super funds controlled over 70 per cent of that \$219 billion. The men and women who are the trustees and executives of these 10 largest funds are therefore in an extremely powerful position given they choose where over \$155 billion of workers money is invested.

Industry funds have spun off a web of interlocking companies and trusts that undertake much of superannuation administration and management.

At the heart of this web is an entity called Industry Super Holdings Pty Ltd (ISH) which is owned by a clutch of industry funds. In its last set of financial statements (available from ASIC) ISH declared it controlled over \$37.7bn in assets. Figure 2 below shows, who owns ISH and what ISH owns. ISH owns 100% of:

- Industry Funds Management (funds under management \$19.5bn)
- ME Bank (worth \$1.4bn)
- ME Investments (funds under management \$756m)
- IRIS (worth \$643m)
- AusFund (funds under management \$575m) and
- Industry Funds Services (a provider of membership management, financial planning and other services).

Each of these entities provides funds management and other services back to industry funds as 'outsourced' providers. But each of these service providers are owned by a corporate structure (ISH) which is in turn owned by industry funds. This makes for a highly complex and confusing disclosure regime.

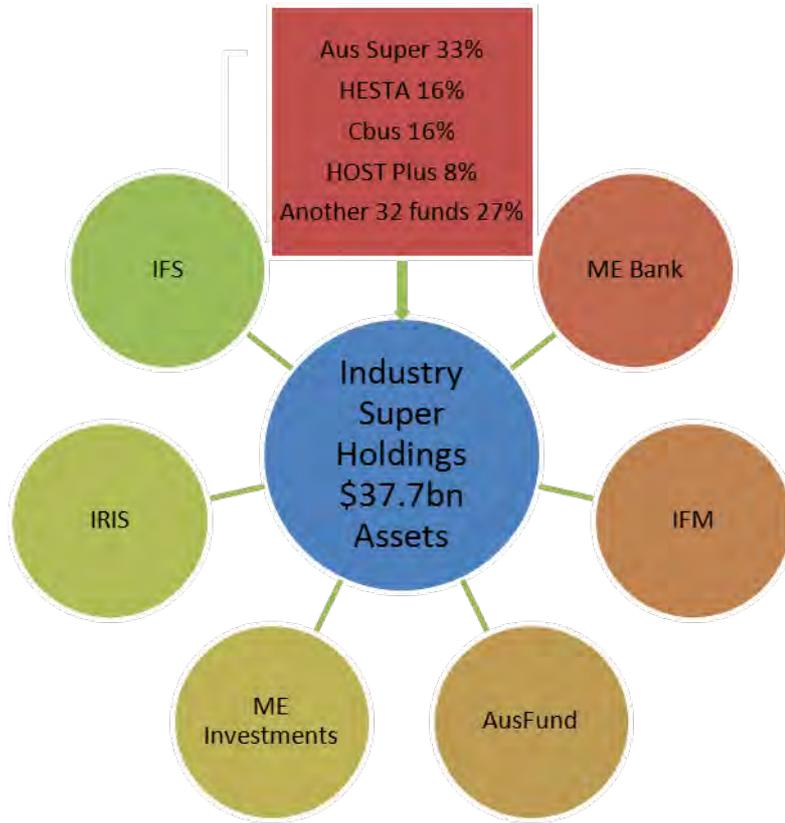
#### **A note on associated entities**

All external investment types whether listed or unlisted, managed or direct, have two characteristics. First, they are purchased in the expectation of a measurable investment return, either from income (dividends, interest, rental income) or capital growth. Second, the assets are managed and controlled external to the fund on commercial terms.

Thirty-six industry funds are shareholders in ISH. The group of investments associated with Industry Funds Holdings (ISH) as associated entities because of the overlapping

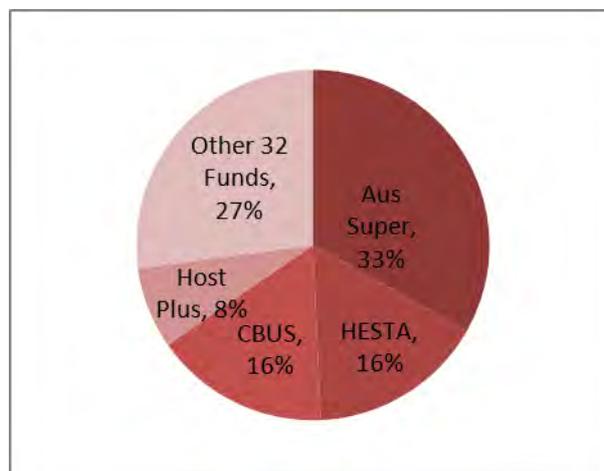
webs of control and directors. Industry funds also invest in administration companies, promotion companies, financial planners and training organisations controlled by industry funds or the ACTU. Some retail managers may have similar investments in associated financial planning networks, foreign subsidiaries or other associated entities. Many of these assets pay no dividends and their return potential is difficult to assess.

**Figure 1: Interlocking shareholdings & relationships**



Sources: ASIC filings, annual reports

**Figure 2 Who owns ISH**



Source ASIC current extract

Industry Super Holdings is owned by 36 super funds. However, just as the ten largest super funds control over 70 per cent of industry fund assets, the top four funds in ISH control 73 per cent of ISH. However it is not the largest of the industry funds which have the largest shareholdings in ISH. Four industry funds have taken large shareholdings in ISH at levels way beyond their overall market share.

**Table 7: The largest Industry Funds and their investment in ISH**

<b>Fund Name</b>	<b>Funds Size December 2008(\$m)</b>	<b>Approximate Fund Size as % of Industry Funds</b>	<b>Investment in ISH February 2009 (%)</b>
<b>Australian Super</b>	29,623.9	15%	33%
<b>Unisuper</b>	24,448.6	12%	2%
<b>REST</b>	15,324.6	8%	0%
<b>Sunsuper</b>	13,559.3	7%	2%
<b>HESTA</b>	13,542.9	7%	16%
<b>Cbus</b>	12,920.2	7%	16%
<b>Health Super</b>	7,818.3	4%	0%
<b>HOST-Plus</b>	6,986.2	4%	8%

*Source: ASIC & APRA, IPA calculations*

In observing the web of cross shareholdings in ISH, its subsidiaries as well as the associated Industry Super Property Trust (ISPT,) issues arise about concentration of control and disclosure. The corporate and personal interconnections suggest significant concentration of financial control.

Table 9 details the cross directorships and background of the twelve most powerful people controlling industry funds.

The power concentration necessitates high levels of disclosure to maintain confidence in the overall superannuation system. Given the industry funds also receive financial privilege through default provisions the highest level of disclosure should be required of these funds as to their investments in such shareholdings and funds.

### **Cross Investments & Shareholdings – First Super v Unisuper**

First Super is a mid-tier industry fund with \$1.26 billion in funds under management (30 June 2009) ranking it about 25<sup>th</sup> in industry fund size. First Super was formed in July 2008 from the amalgamation of three smaller funds covering furniture workers, the timber industry and pulp and paper workers. First Super has somewhat less than 1% market share of the industry funds.

According to First Super they have outsourced and spread their members' monies as follows

**Table 8: First Super assets**

<b>Asset</b>	<b>Value</b>
IFM Enhanced Index Fund	\$81,148,229
IFM Global Equities Trust	\$6,061,220
IFM Australian Infrastructure Fund	\$47,788,444
IFM International Infrastructure Fund	\$26,304,950
Super Loans Trust (Members Equity)	\$12,579,611
ISH/Members Equity (Direct Investment)	\$16,470,720
Super Benefits Administration Pty Ltd	\$755,909
ISPT Core Fund	\$83,274,086
<b>Total Industry Fund Entities</b>	<b>\$274,383,169</b>
All Other Assets	\$990,586,657
<b>Total Fund</b>	<b>\$1,264,969,826</b>

*Source First Super Annual Report 2009*

First Super's 2009 annual report shows that 20% of First Super funds are invested in funds run by Industry Funds Management, Industry Super Property Trust and Members Equity.

A further \$17.2 million is invested directly in ISH and Super Benefits Administration. Analysis of the current ISH shareholders suggests First Super's shareholding in ISH had increased since its annual report. In February 2010 First Super has a 4.8% shareholding in ISH at a cost of \$32,986,060 (see note below). This compares to First Super's market share of less than 1% of industry funds. ISH has not paid a dividend in the past two years.

By contrast, the same analysis for Unisuper shows a different picture. Unisuper is the second largest industry fund with about a 12% market share and \$21.77 billion in funds under management. Unisuper is also a shareholder in ISH with a 1.9% shareholding, considerably below their overall market share of 12%. Unisuper's investments in IFM, ISH and ISPT only total 1.2% of funds under management.

*[Nb: The shareholding in ISH may have increased since June as the current ISH top-20 shareholding report shows Timber Industry Super Scheme with 14,305,806 fully paid shares and First Super Pty Ltd with a further 20,377,306 partly paid shares.]*

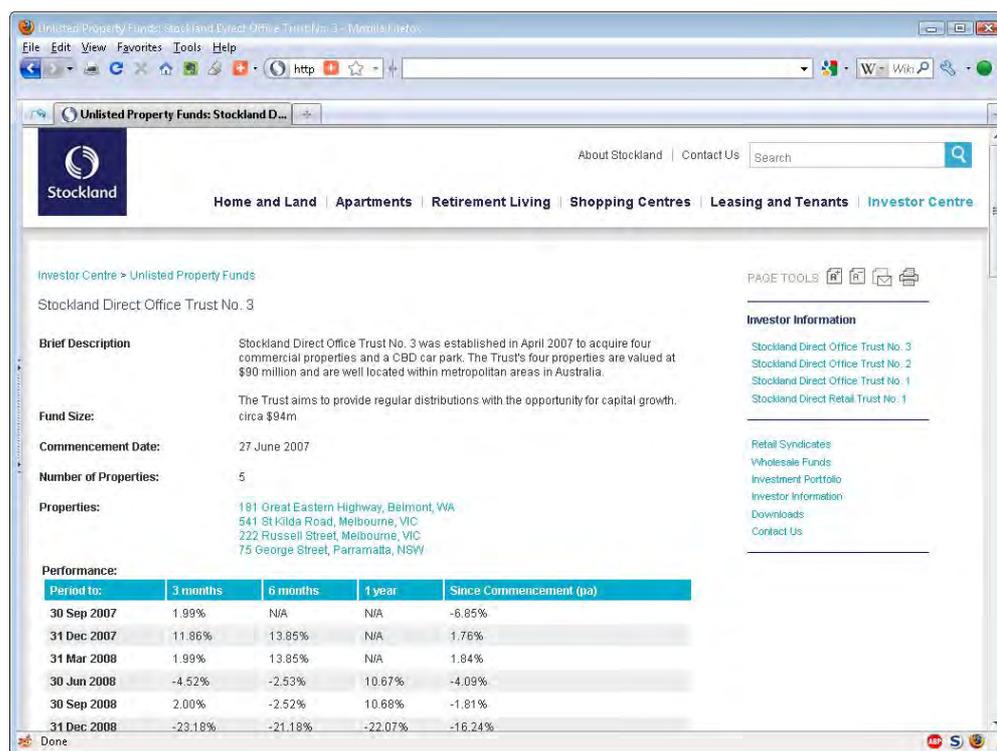
### **Industry funds disclose less than other funds**

Information on the ownership structure and directors of the group of companies comprising the Industry Super Holdings Group and ISPT is not freely available. The

shareholdings and directors information presented in this report was purchased from an approved ASIC information broker.

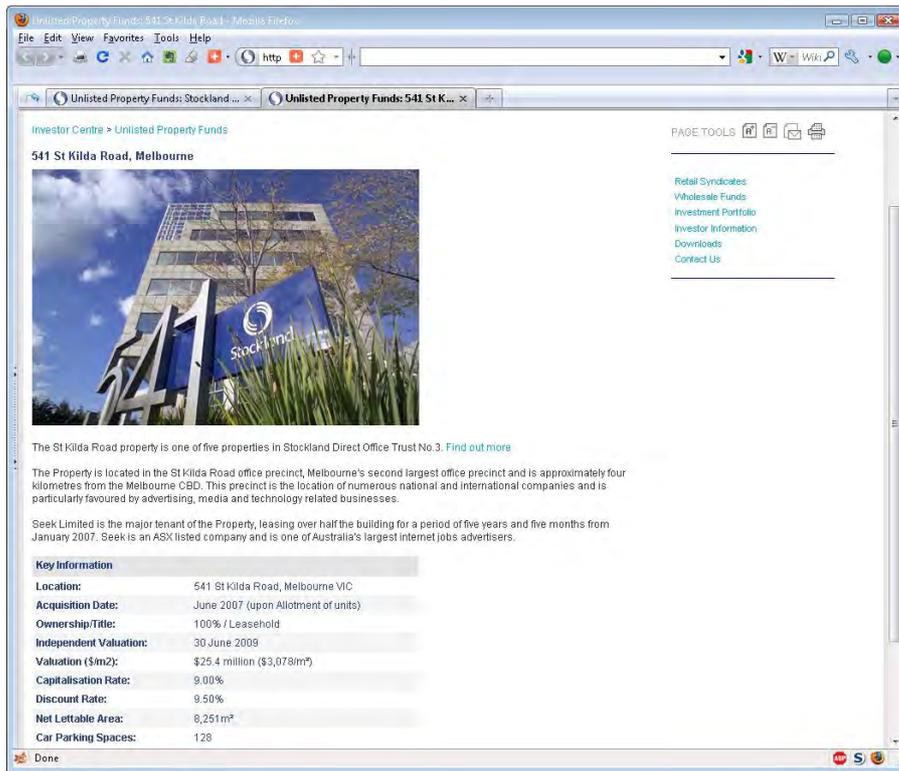
Investing members of the ISH group such as IFM and also ISPT also disclosed significantly less information about the investments under their control than independent investment managers also used by industry superannuation funds.

For example, and by comparison, the screen shots below<sup>15</sup> are from the Stockland Group website and show information for the Stockland Direct Office Trust No.3. Stockland is a high profile property investment fund that is directly comparable to ISPT. The first shot details the purpose of the Stockland fund,

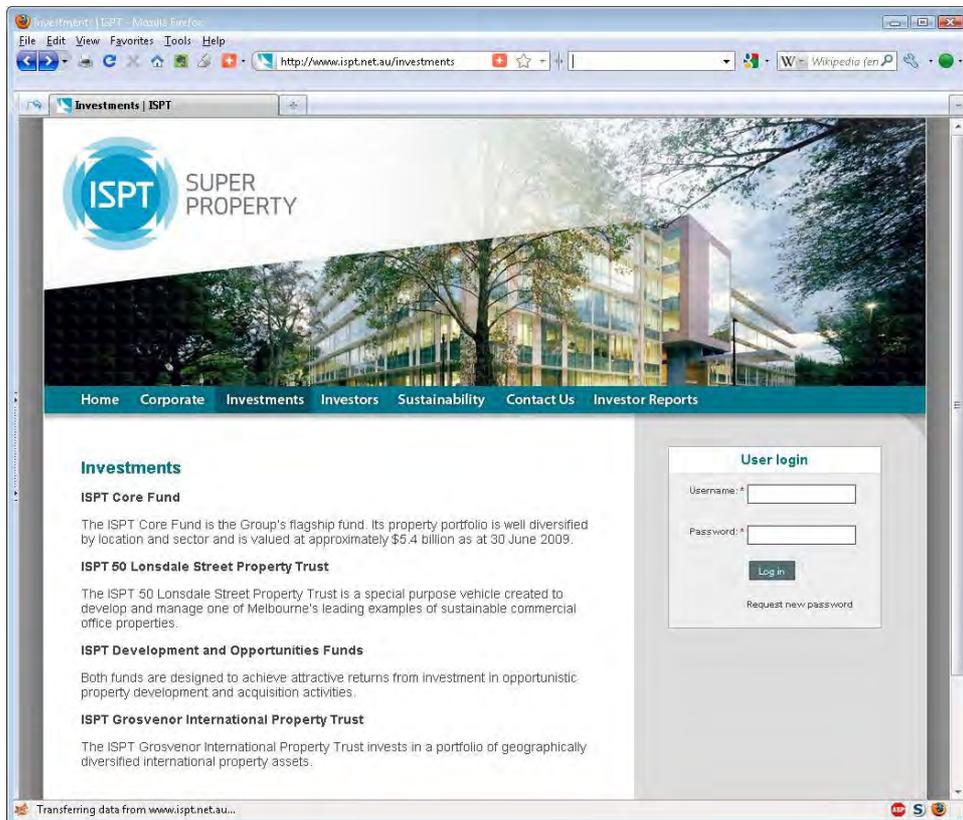


The second screen shot is a click through from the properties list in the first shot to 541 St Kilda Road Melbourne. This has a picture of the building, its address, purchase date, valuation and key details about the property. This shows a high level of disclosure by Stockland.

<sup>15</sup> All screen shots taken 22 February 2010. Media coverage calling for additional disclosure in the Age and Sydney Morning Herald appeared on March 20, 2010. As at 2 April 2010, a link to the ISPT 2009 Annual report was included.

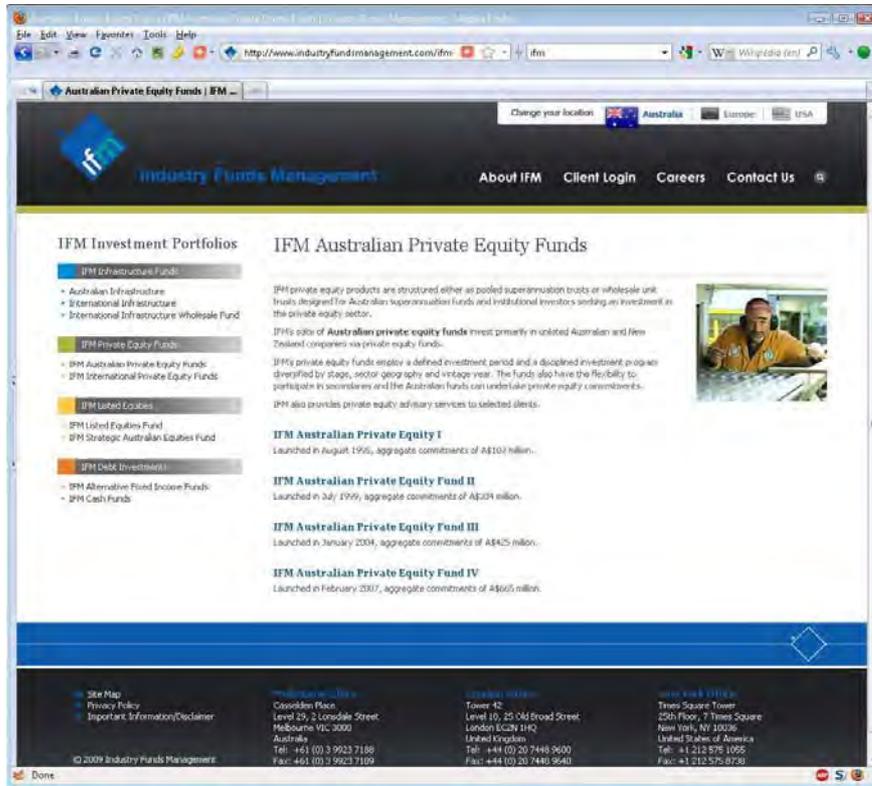


Below is the corresponding screen shot from ISPT, the Industry Funds property trust.

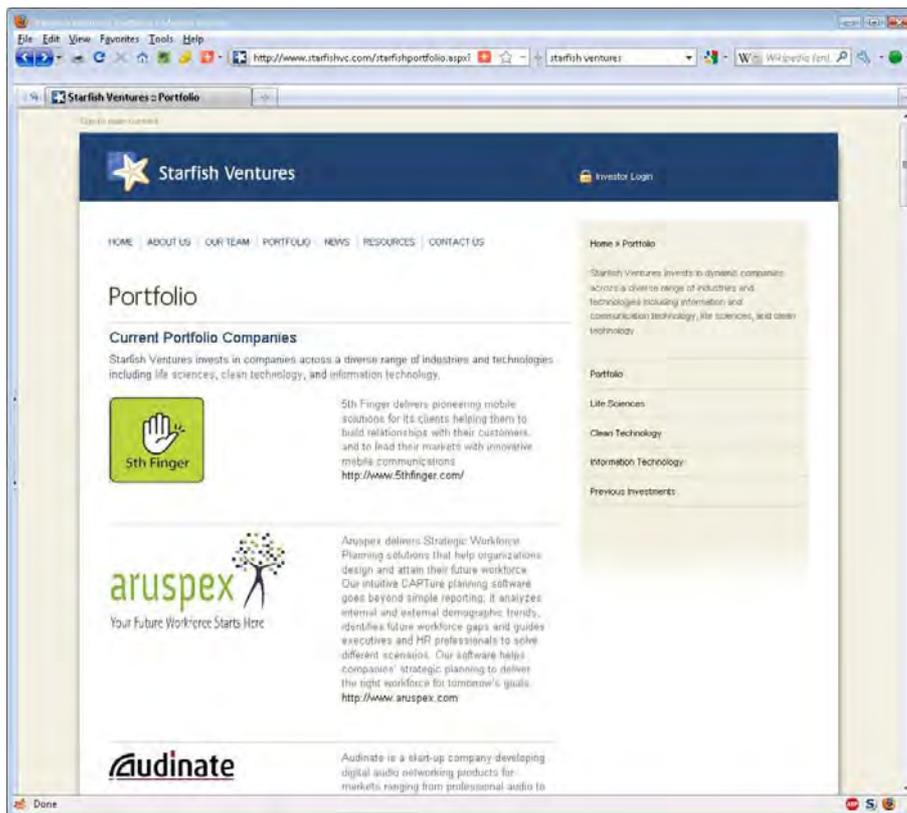


For the main fund, the IPST Core Fund, the only information available is the total value of the fund as at 30 June 2009. No individual properties are listed, no property details are provided and none of the type or level of information available from the Stockland Property Trust is made available by ISPT.

Similar results occur with disclosure of private equity investments. We compared a private fund, Starfish Ventures to the industry management fund IFM. IFM provides no information as to the assets making up their private equity funds or their current valuations.



By contrast Starfish Ventures, a much smaller private equity firm, provides considerable detail on their website of the investments in their funds, including links to the websites of their investments. Starfish is a small fund. If Starfish can provide high level of disclosure surely superannuation funds can do the same.



***Industry funds are controlled by an extremely small number of individuals.***

Twelve people across the industry funds industry hold directorships or executive positions where they control \$188 billion of financial assets.

As shown earlier, at the heart of the web of cross shareholdings and cross directorships is Industry Super Holdings (ISH) and the largest industry super fund Australian Super.

The largest shareholder in ISH is Australian Super (a \$29 billion dollar fund). Australian Super has 13 trustees of whom four hold cross directorships on other ISH related companies or are on ISPT the industry funds property trust that has \$7 billion invested in it.

**Table 9: The twelve most powerful people in superannuation**

	<b>Superannuation Industry Positions Held</b>	<b>Background &amp; Qualifications</b>
<b>Anna Booth</b>	Director of IFM (\$19.5bn), ME Bank, Industry Super Holdings (\$37.7bn). <b>Total \$58.5 bn.</b>	Formerly National Secretary of the Textile, Clothing and Footwear Union of Australia and Junior Vice President of the ACTU.
<b>Cath Bowtell</b>	Director of Australian Super (\$29bn) and AGEST (\$3.5bn). <b>Total \$32.5 bn.</b>	ACTU Senior Industrial Officer (resigned 16 March 2010).
<b>Brian Daley</b>	Director of Australian Super (\$29bn), ARIA (\$11.5bn), HOST Plus (\$7bn), and ISPT (\$7bn +). <b>Total \$54.5bn.</b>	National President of the Liquor, Hospitality and Miscellaneous Union (LHMU).
<b>Anne De Salis</b>	Director of NSW State Super (\$38bn), Industry Super Holdings (\$37.7bn), ME Bank (\$1.3bn) and Funds SA (\$14bn). <b>Total \$91bn.</b>	Senior Advisor to Paul Keating then career financial services professional. Has held senior management positions with AMP and MBF.
<b>Mark Delaney</b>	Chief Investment Officer Australian Super (\$29bn) and Director ISPT (\$7bn). Member Australian Council of Super Investors Committee of Management. <b>Total \$36bn.</b>	Career funds management professional. Has held senior positions with AXA and Federal Treasury.
<b>Angela Emslie</b>	Chair HESTA (\$13.5bn), Care Super (\$3.6bn), Vision Super (\$4bn) and Australian Institute of Superannuation Trustees. <b>Total \$21.1bn.</b>	Consultant in the health, community services and government sectors. VECCI background in OHS.
<b>Bernie Fraser</b>	Chairman of ME Bank and Industry Super Holdings (\$37.7bn). Director of Australian Super (\$29bn) and Cbus (\$13bn). <b>Total \$81bn.</b>	Governor of the Reserve Bank of Australia 1989 to 1996. Secretary to the Treasury 1984 to 1989.
<b>Sandy Grant</b>	Director of Industry Super Holdings (\$37.7bn), ME Bank, Super Members Investments Ltd (\$0.8bn), IRIS, Superpartners (\$75bn) and Care Super (\$3.6bn). <b>Total \$42.6bn.</b>	Career superannuation management professional. Has held senior positions with Colonial and been CEO of IFS and Cbus.
<b>Brian Pollock</b>	Director of IFM (\$19.5bn), ME Bank and Industry Super Holdings (\$37.7bn). <b>Total \$58.5bn.</b>	Career funds management professional. Formerly Executive Director Property and Lending with AXA.
<b>Elana Rubin</b>	Chair of Australian Super (\$29bn). Director of ISPT (\$7bn +) and Tower Australia. <b>Total \$36bn.</b>	ACTU background in OHS, industrial work, superannuation policy and advocacy. Was CEO of ARF.
<b>Ian Silk</b>	CEO of Australian Super (\$29bn) and alternate director of ISPT (\$7bn). <b>Total \$29bn.</b>	Advisor to Cain/Kirner governments. Has held senior positions in the superannuation industry for 14 years.
<b>Garry Weaven</b>	Chair of IFM (\$19.5bn). Director of ME Bank and Industry Super Holdings (\$37.7bn). <b>Total \$58.5bn.</b>	Former Assistant Secretary of the ACTU. Founded Industry Fund Services in 1994.

*Source: Directorships from ASIC extracts as at 12 Feb 201 and, annual reports. Biographies from annual reports & online searches.*

## **Inadequate transparency causes problems**

### ***Confidence in the system is put at risk***

Fortunately, the Australian financial system has proven stronger than most international systems in the global financial crisis. Despite this, the Australian superannuation sector has concerning features:

1. There is a heavy concentration of control of other people's money in a comparatively small number of hands.
2. There is a reliance on process alone to ensure integrity.
3. Disclosure of transactions is low or masked.

### ***Low disclosure means fund members are uninterested in the operation of their funds***

It is recognised that many Australians are disengaged from, or uninterested in, the financial affairs of the super funds in which they have their money.

Australians have their income compulsorily taken from and placed in superannuation funds and are institutionally discouraged by the superannuation funds because of poor disclosure. Effective comparisons between funds cannot be made because of poor disclosure. Inadequate disclosure is the main reason that Australians are disengaged from the use of their compulsory superannuation contributions.

Australians must be given the opportunity to be engaged and interested in how their superannuation nest eggs are being used. The basic step to achieving this is to require the superannuation funds to disclose the necessary information in full.

### ***Disclosure works: The CalPERS case***

The California Public Employee's Retirement System (CalPERS) is one of the largest superannuation funds in the world, with assets of some \$US200 billion (2009) covering 1.6 million workers and retirees. Its assets are larger than all of the Australian industry superannuation funds combined. It is a government-sector fund and, as such, should have been expected to have the highest of governance standards.

CalPERS has been plagued by scandal over the scale of fees paid to outsourced investment managers and 'placement agencies' (intermediaries who pitch their products).<sup>16</sup> There is concern about 'political fixers' and 'peddlers masquerading as placement agents' resulting in calls for intermediaries to register as lobbyists. The troubles were triggered by revelations of huge fees paid—in one instance \$US70 million to a former CalPERS board member turned agent. The former board member had used his political connections to help private fund managers gain billions in business.

CalPERS provides outstanding disclosure of assets, expenses, fees and commissions paid. This level of disclosure is far beyond any Australian super fund yet CalPERS still fell afoul of good governance. It was only through the level of disclosure of CalPERS that

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<sup>16</sup> Lifsher, Marc. "CalPERS, CalSTRS See Long-Term Credit Ratings Lowered." Los Angeles Times, 11 December 2009. (and) "CalPERS to consider stiffer rules." Los Angeles Times, 16 November 2009.

investigators were able to piece together the money trail to the ‘political fixers’ and ‘peddlers masquerading as placement agents.’ High levels of disclosure and transparency are not in themselves inoculation against malfeasance but they are a powerful shield.

CalPERS provides a powerful lesson for Australian superannuation funds. Like any financial institution, superannuation funds can be subject to misuse of the members’ funds. Particular attention must be paid to situations where strong political connections exist. Safeguards must be built to minimise the ability of well-connected political players to manipulate the system to favour particular investment funds, managers or individuals.

### ***Lessons from the Cole Royal Commission***

There is strong evidence in Australia that fiduciary trust arrangements have been abused. The 2003 Cole Royal Commission<sup>17</sup> into the building and construction industry provided damning evidence that workers’ money held in trusts was being misused in the construction sector.

The Royal Commission into the Building and Construction Industry (the Cole Commission) was a highly controversial investigation. Building unions claim that it was a political set-up intended to harm Australian unions. Whether this is true or not is irrelevant to the issue of security of workers’ money.

The Cole Commission found major misuse of member funds in trusts (redundancy, long service leave, and training) where the structure, control and governance arrangements were/are almost identical to those for the industry superannuation funds. That is, the funds are controlled by a ‘partnership’ of unions and employer associations.

The operations and governance of the superannuation funds did not receive adverse findings. This is welcome. This should not, however, result in complacency.

Volume Ten of the Cole Commission Report presents the outcome of the Commission’s investigations into trust funds operating within the construction sector. There were four types of funds investigated. In each instance the funds obtain their income and assets from compulsory employer contributions paid on behalf of employees.

The four trust fund types investigated were:

- *Superannuation funds*
- *Redundancy funds:* Where money is held in trust for employees who suffer redundancy and is paid to them to compensate for redundancy. In 2001 there are eight construction-sector redundancy funds with assets exceeding \$500 million.
- *Long Service Leave funds:* Where employees’ money is held in trust and paid to them after long service in the industry.
- *Training Funds*

The funds are controlled by trustees appointed by unions and employer associations.

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<sup>17</sup> [www.royalcombcgi.gov.au](http://www.royalcombcgi.gov.au)

The significance of the Cole investigation was that the Commission was able to compulsorily acquire all the financial records of the trust funds and conduct an exhaustive forensic investigation of the accounts. Probably never before have any superannuation funds in Australia been so thoroughly and publicly investigated as to their internal governance standards and practices. The Commission was not interested in the funds' financial performance but whether funds were being used for the exclusive benefit of members.

The Commission investigated the following superannuation funds

- Allied Unions Superannuation Trust (Queensland) Building
- Unions Superannuation Scheme (Queensland)
- CONNECT Construction and Building Unions Superannuation Fund
- New South Wales Electrical Superannuation Scheme
- Superannuation Plan for Electrical Contractors (Qld)
- Westscheme Superannuation Scheme

There were no findings by the Cole Commission that any of the superannuation funds used members' money for any purpose other than the benefit of the members. Findings were made about unions acting as 'enforcers' to require moneys to be paid to these superannuation funds. However, that does not go to the question of the internal operation of the funds themselves.

The same cannot be said of the redundancy and long service leave funds. The Commission found systemic misappropriation of member's funds including:

- (a) the making of payments by industry redundancy funds to members in circumstances not authorized by the trust deed;
- (b) the provision of welfare benefits by an industry fund exclusively for those of its members who were financial members of a union, thereby discriminating against members of the fund who were not union members; ...
- (i) the receipt by a trust controlled by a branch of a union, of the proceeds of part of a commission paid on an annuity purchased by a trustee of an industry redundancy fund;
- (j) the receipt by a trust controlled by a branch of a union, of distributions from a trustee of an industry redundancy fund, the source of such distributions being interest earned on payments made by employers for the benefit of employees; ...
- (s) the distribution by an industry training fund of most of its general purpose funding to unions or union-controlled bodies rather than to 'bipartite' bodies as contemplated by the fund's objects; ...
- (v) the approval by the board of an industry training fund of funding for a scheme to which discriminatory conditions of participation, favouring the sons and daughters of trade unionists, apply;
- (w) the approval by the board of an industry training fund of a grant to a union for a 'safety and training officer' in circumstances where that officer in fact engaged in numerous tasks not related to training; with the result that the funding was expended for purposes not authorised by the trust deed;

(x) the repeated renewal by the board of an industry training fund of a grant to a union for a 'safety and training officer' despite failing to receive acquittal of moneys provided ...<sup>18</sup>

In other words, interest from trust funds was paid to unions, thereby breaching the purpose of the trust. Union officials' children received privileged access to trust training moneys. Training trust moneys were used by unions to fund their own activities. Money was taken from trust funds for non-trust member uses. Trust benefits were paid to union members and not to non-union members.

Examples of allegations of misuse of construction industry trust fund moneys have continued since the Cole Commission Report. These include the use of funds to pay for international travel 'junkets'.<sup>19</sup>

The Cole Royal Commission demonstrated that there is nothing inherently 'safe' about trust arrangements. They do not guarantee that fund moneys are used entirely for the benefit of members and that funds are not misappropriated for other purposes. Many other layers of oversight and protection are needed, including high-level disclosure of the details of how fund moneys are used.

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<sup>18</sup> Cole Commission Report, Volume 10, pages 8–10.

<sup>19</sup> Masanauskas, John. "Revealed: Union Boss's \$80,000 Luxury Junket." Herald Sun, 13 November 2008, p. 1.

## Current Superannuation Fund Transparency

### *The policy environment*

In mid-2009 the Federal government commissioned an inquiry, called the *Review into the Governance, Efficiency, Structure and Operations of Australia's Superannuation System* (the Cooper Review).<sup>20</sup> The Cooper Review reports and submissions to it give a good insight into the thinking of the superannuation and financial industry on the governance levels required of superannuation. The Review is being conducted by a panel with considerable experience in the financial and superannuation sectors. Around 190 submissions were sent to the Review by organisations and individuals involved and/or interested in superannuation. A Preliminary Report was released on 14 December 2009.

The 'government has articulated four principles that will guide its assessment': 'Simplicity', 'Efficiency', 'Equity', and 'Adequacy'.<sup>21</sup> Glaringly absent is the word 'transparency'. This omission is, unfortunately, consistent with the style and approach of the governing Act, the *Superannuation Industry (Supervision) Act*. It's also consistent with the regulatory oversight apparent from APRA and ASIC and with which those operating in the superannuation industry seem comfortable.

Neither APRA nor ASIC appear to undertake any form of direct auditing of the superannuation funds.

APRA publishes a summary of all superannuation fund performances online. However, this summarises the returns supplied to APRA by the funds.<sup>22</sup> It is not an independent assessment of the funds' performance. That is, under current legislative requirements, APRA reports what the funds are reporting.

APRA appears to rely on governance processes stipulated under the superannuation Act to satisfy its integrity requirements. That is, APRA assumes that the superannuation funds keep accurate financial records in line with standard accounting practices and have these accurately audited. However, it is not possible to assess if the fund performance comparisons supplied to APRA enable accurate 'apples with apples' comparisons of performance to be made. It is unknown if funds have differences in valuation methods. For example, what is the timing of real estate valuations? If some funds revalue their real estate holdings on a constantly rotating basis and others revalue property holdings on a set date in a year, performance results can be markedly different.

ASIC's available online information on superannuation funds is also scant, relating mostly to advice on process. ASIC does provide general information on how to compare funds and funds' performance and supplies some general tables.<sup>23</sup>

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<sup>20</sup><http://www.supersystemreview.gov.au>

<sup>21</sup> Cooper Review. "Clearer Super Choices: Matching Governance Solutions." 2009, p. 3.

<sup>22</sup> See <http://www.apra.gov.au/Statistics/Superannuation-Fund-level-Publications.cfm> "Data in this publication has been prepared from the superannuation returns submitted to APRA under the *Financial Sector (Collection of Data) Act 2001*."

<sup>23</sup> See <http://www.fido.gov.au/fido/fido.nsf/byheadline/Long-term+performance+figures+for+typical+super+fund+investment+options?openDocument>

However, ASIC makes it clear that it bears no responsibility for the accuracy of the data it supplies, stating 'ASIC acknowledges with thanks data supplied by the following agencies that rate super funds: Morningstar, SelectingSuper and SuperRatings. These agencies remain responsible for the data and we have not independently verified it.'

As ASIC makes clear, the real external performance oversight of superannuation funds' performance (other than their required audit processes) is done by three private ratings agencies.

- Morningstar is an international ratings agency.
- Selecting Super is a privately owned Australian entity.
- Super Ratings is a privately owned Australian entity.

What we conclude is that the official regulatory oversight of superannuation is focused on *governance processes*. It is assumed that if the process of 'Trust' and statutory governance is adequate, that the superannuation system will have integrity, that transparency will occur and that potential for misappropriation or misuse of members' funds can be minimised. This can be true to a point. Proper governance process is essential to a superannuation system for it to have integrity.

But governance processes on their own do not give sufficient protection to fund members. Instead the regulatory assumption ought to be that when the control of large sums of other people's money is put in the hands of comparatively small numbers of people that the capacity for maladministration, diversion of funds to other (non-member purposes) and fraud is ever-present. This is not to suggest that this is happening in the superannuation sector at the moment. However, it is irresponsible of the regulatory framework to operate on any assumption other than that risk is ever-present. Operating on the regulatory assumption that governance processes themselves will guarantee transparency and protection equates to low-level regulatory oversight.

What would put an additional brake on the potential for misuse of superannuation member funds is the enforced disclosure of all asset listings, movements in values and fees and commissions. That is, to require not only disclosure through governance process, but also disclosure of detailed, tangible facts and financial outcomes.

## **A model for transparency: best practice disclosure**

The Panel views disclosure as one important way in which trustees can be made accountable to members: that is, specific information must be given to members.<sup>24</sup>

APRA regulated superannuation funds should be required to conform to high mandated disclosure standards.

A fund member, investment advisor, or member of the public, should be able go into the website of any retail or industry superannuation fund and obtain enough information so they can understand where their money is invested, how it is performing relative to similar funds, who gets paid to manage and administer the fund, and how much is paid, and whether the fund's trustees have any cross-directorships.

These full disclosure and transparency declarations should be posted on superannuation websites every quarter. By posting declarations quarterly, reflecting the previous quarter's activity and position, this would protect the confidentiality required in relation to funds' forward investment strategies.

This disclosure should be mandatory. The law should require all superannuation funds to report these financial facts in a standard format. Similar information should be supplied by outsourced fund managers and made available on the superannuation fund websites.

Full disclosure will not provide a guarantee against poor fund performance, misappropriation of funds, or fraud, but it is a basic essential step needed to manage and minimise the risks.

Default award funds, whether industry, corporate, retail or government must be held to a higher standard than those actively chosen. As the Cooper Review notes, these are the funds the least sophisticated investors belong to and they are there under legislated mandate. AMP also makes this point in their submission to the Cooper Review.

Increasingly, the ownership or legal structure of a fund is less relevant to the product design, pricing and other features offered to consumers. The governance of the superannuation industry needs to reflect these developments, and while high regulatory standards should apply to protect all members of superannuation funds, arguably higher standards should apply to the "default" market where members do not make an active choice.<sup>25</sup>

It is an important operational principle to accept that default funds are a special superannuation case requiring the highest levels of disclosure.

### ***Standard Reporting Format***

Morningstar is a large international ratings agency providing independent assessments on the performance of Australian superannuation funds. We believe it is worth citing in detail aspects of Morningstar's submission to the Cooper Review of Superannuation.

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<sup>24</sup> Cooper Review. "Clearer Super Choices: Matching Governance Solutions," 2009, p. 14.

<sup>25</sup> AMP. "Response to the Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System, Phase 1 - Governance." 2009, p. 6.

They paint a damning picture of poor disclosure in the Australian superannuation industry and are specific about what should be required to fix the situation.

The requirement should be for investment managers to publish quarterly asset allocations at a minimum. Many investment managers currently disclose this information to Morningstar voluntarily on a monthly basis, and we advocate regular, comprehensive disclosure of portfolio holdings more generally (refer section 8.2.6 below).

8.2.6 Measures such as publishing trust deeds, offer documents, and related materials on websites are effective and economical ways of increasing transparency and member engagement. ...

It is, however, our view that the key disclosure issue for superannuation and funds management is the comprehensive, periodic disclosure of portfolio holdings (the stocks, bonds, and other securities which constitute the portfolios of superannuation funds and other pooled investment vehicles).

Australia lags global best practice in this area. In a Morningstar study of global fund investor experiences published earlier this year, Australia and New Zealand were the only countries among the 16 assessed which do not require regular, full portfolio holdings disclosure.

Australian superannuation scheme providers and fund managers currently have a mish-mash of approaches to holdings disclosure. Some disclose information on a monthly basis, some quarterly, and some not at all. Some disclose their top 10 holdings only, and some nothing.

Superannuation and managed funds disclosure in Australia is also poor when compared with the extensive mandatory disclosure requirements for listed securities.

Regular, comprehensive holdings disclosure would also provide greater opportunity for detection of undesirable behaviours such as excessive turnover and 'window-dressing' (the practice of turning over a fund's portfolio holdings close to a reporting period, selling poorly-performing companies and buying strongly-performing ones, to make the fund's performance look better).

Additionally, there is little uniformity or consistency in other key information such as the identity of the people managing the money. Product disclosure statements for superannuation funds and other pooled investment vehicles should disclose information such as the key individuals responsible for investment management.<sup>26</sup>

The law should require all superannuation funds to disclose financial facts in a standard format. We agree with the position of Morningstar.

The following is the minimum we advocate should be disclosed and updated quarterly. See Appendix A for definitions and characteristics of each asset class described in this section.

### **Fund Assets**

#### **Best Practice Reporting: Traditional Exchange-Traded Asset Classes**

- Top 20 Australian shareholdings by name, number and value.
- Top 20 International shareholdings by name, number and value.
- Country allocation for international shares
- Any substantial shareholdings notified to the exchange
- Fixed interest by portfolio maturity length and yield.
- Cash deposits held and with whom.

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<sup>26</sup> Morningstar. "Submission to Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System, Phase Two: Operation and Efficiency." 2009, p. 4, 5-6 .

- External managers by asset class, name and value of funds managed with links to fund descriptions on the managers' websites.

These assets are generally re-valued at least daily by fund managers as standard operating procedure. If the fund manager utilises daily unit pricing then the value of these assets is transmitted from the fund manager to the overall fund daily.

Industry superannuation funds make heavy use of fund managers<sup>27</sup>. That is, industry funds decide on the asset allocation of the funds, into for example shares, property, fixed interest and cash then contract out significant portions of funds management to specialist organisations (fund managers) who have expertise. This is sound, sensible practice.

As standard procedure external fund managers provide fully detailed reports to superannuation fund trustees, usually on a monthly basis. However, the use of external fund managers is often used as the excuse for lower levels of disclosure because multi-manager funds (such as Industry super funds and retail master trusts) collate and consolidate their holdings data from a number of sources.

Perhaps surprisingly, the Australian Superannuation Funds Association argues against individual reporting of stocks and even pooled funds.

Reporting from super funds on the individual holdings of stocks, pooled funds, etc. can be very burdensome for super funds and investment managers and in many cases is already provided to individual members if they request it, and also to fund analysts and researchers for analysis of style and other portfolio return factors.<sup>28</sup>

This almost amounts to a plea for secrecy and must be rejected as a flawed policy and wrongly described as burdensome. There is an abundance of software available that can bring together required information. At minimum, it should be a straightforward procedure to report quarterly, in arrears, on a website, the overall holdings of the top 20 domestic and international shares, cash holdings and bonds. Any claimed inability to do this must raise questions about the record keeping capacity and reliability of funds performance.

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<sup>27</sup> Note: Retail funds tend not make heavy use of fund managers, as they generally have investment expertise in-house. In fact, the parent organisations of retail funds are often outsourced fund managers used by industry funds. Hence fund manager disclosure requirements are likely to have a higher impact on industry funds than on retail funds.

<sup>28</sup> ASFA. "Submission - Super System Review – Phase Two: Operation and Efficiency," 2009, p. 40.

**Best Practice Reporting: Unlisted Trusts**

The following also should be reported including infrastructure investments, private equity holdings, total return portfolios and property trusts showing.

- Value of funds managed aggregated by fund manager
- External managers by asset class, name and value of funds managed
- Links to websites of individual funds. E.g. The Stockland Direct Office Trust No. 3 website shows fund size, performance, names of properties with further links for more information<sup>29</sup>
- Links to the underlying investments in associated entity trusts, e.g. Industry Funds Management funds and ISPT for industry funds and other members of the overall group for retail funds

The overall principal for these types of assets is that a super fund member should be able to go directly to a listing of the underlying assets and see the values for any trust from links on the super fund website. As investments in these assets tend to be long-term as do the underlying investments in the trusts, once implemented, maintaining this information should be straightforward and inexpensive.

**Best Practice Reporting: Direct Property, Property Development & Other Direct Investment**

- All properties owned, the address, purchase date, purchase price, most recent valuation and yield.
- Properties leased to associated entities, (defined in the broadest sense) to whom the properties are leased and the rental amounts.

Investments in property developments should have special treatment. This should happen particularly where the workers constructing the properties are also members of the superannuation fund. Additional disclosure in construction was recommended by the Cole Commission. This should include;

- financial or other interests, directly or indirectly, in any of the projects in which the super fund is an investor
- Interests of controllers or managers of outsourced fund managers in any of the projects in which the super fund is an investor
- Interests (including leases) of unions or industry associations who appoint the trustees to the super fund
- Any lobbyists associated with or acting for the super fund or the unions or industry associations who appointed the trustees to the super fund involved in seeking government approvals for projects in which the super fund is an investor?
- Any unions or industry associations who have appointed trustees to the super fund arranged or caused to arrange any arrangements, either commercial or industrial relations arrangements, that give special advantage to projects in which the super fund is an investor?

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<sup>29</sup> [http://www.stockland.com.au/investor-centre/unlisted-property-funds2\\_stockland-direct-office-trust-no-3.htm](http://www.stockland.com.au/investor-centre/unlisted-property-funds2_stockland-direct-office-trust-no-3.htm)

#### **Best Practice Reporting: Other Direct Investments**

Disclosure should list infrastructure, private equity and art investments providing;

- Name, value and size of shareholding for all assets
- Valuer, valuation date, most recent movements in valuation for all assets

#### **Best Practice Reporting: Associated entities & Any Other Assets Not Already Mentioned**

Related party direct investments, such as shareholdings, (as opposed to deposits or investments with) in industry superannuation vehicles such as ME Bank, ISH, ISPT and any other assets or investments not already listed and showing;

- Full list with shares held, amount paid (and any outstanding amounts if partly paid shares), value, valuation date.
- Dividends received

These shareholdings are generally long term in nature. Once posted to the web this should not generally be expected to change much.

### ***Control & Trustees***

Control of super funds is formally vested in the trustees. For industry funds, the majority (often all) trustees are appointed by employer groups and unions. Retail fund trustees are often executives of the firm running the fund although independent directors are becoming more common in these funds. Trust law is very clear as to the duties of trustees to act solely in the interests of the trust beneficiaries.

Because trustees are in such a powerful and responsible position, information about trustees and their capacity to undertake the duties of a superannuation trustee is of direct relevance to super fund members.

There is a complete divergence of views within the industry as to the adequacy of current appointment and suitability requirements for trustees. In summary;

- Industry funds think equal representation of employers and unions is not only a suitable governance model of itself, they argue other models, especially executive or finance industry professionals dominated models are inferior.
- By contrast, retail funds think the qualifications and skills of trustees to discharge their duties are the important criteria.
- One group focuses on who appoints the other group on who is appointed.<sup>30</sup>

The Cooper Review recognizes that competence, rather than provenance, is of utmost importance in the effective supervision of superannuation funds.

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<sup>30</sup> See submissions to the Cooper Review by Industry Funds Forum, Cbus, AMP, AXA, Industry Super Network and Tower for examples of the divergence in views.

Specifically, it believes that while individual trustee directors do not have to be technical experts across all aspects of superannuation, they must be able to understand and address effectively the issues they encounter as trustee directors. They must be capable of setting the business, investment and operational strategies of the fund and overseeing its operation.<sup>31</sup>

Unisuper raised an important and, it appears, untested and evolving area of law in relation to trustee capacity:

UniSuper would also like to see equal representation rules and the 'fit and proper' requirements for directors harmonised to avoid impasses where members elect directors who may not individually have the qualifications that APRA might expect. In the past, it was sufficient if the board, assessed as a whole, met the requirement, whereas now there is a trend towards requiring every director to possess the requisite skills and expertise across all disciplines.<sup>32</sup>

Irrespective of one's view as to whether it is the appointment process or the attributes of the appointees which is important, the appropriate disclosure for all trustees should be:

**Best Practice Reporting: Disclosure of Appointment, Skills and Conflicts**

- Who appointed trustees and when
- Formal qualifications relevant to their role
- Other relevant training completed and when
- All other positions they hold showing by name, other superannuation trusteeships and industry directorships
- Any links to fund managers the trustees may have, especially links to funds in which the superannuation fund has investments
- Any directorships of entities in which the superannuation fund has investments
- Any conflicts of interest

Of great interest in terms of transparency are all fees and other payments to trustees. In general, these are not separately disclosed and the industry appears to have little appetite for full disclosure in the future. The industry superannuation lobby association ASFA argue that only *policies* for remuneration should be disclosed and not the actual amounts paid be disclosed.

ASFA contends that there should not be a requirement to disclose to members the level of remuneration paid to directors and executives of super funds or remuneration arrangements of service providers. ... in the interest of transparency trustees should be required to disclose to members their policies around key governance areas, including remuneration.<sup>33</sup>

Remuneration *policies* are insufficient for adequate disclosure especially when this often means a statement to the effect that trustees also act as directors of the holding

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<sup>31</sup> Cooper Review. "Clearer Super Choices: Matching Governance Solutions," 2009, p. 12.

<sup>32</sup> Unisuper. "Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation Industry, Phase 2: Operation and Efficiency. Unisuper Submission." 2009, p.9.

<sup>33</sup> ASFA. "Submission - Super System Review – Phase Two: Operation and Efficiency," 2009, p. 46.

company of the trust and of this they receive no payment. Such slippery statements hiding the fact the trustees are in fact paid to act as trustees.

A few superannuation funds do disclose actual trustees and executive remuneration, usually in the same way large public companies do i.e. in a table with remuneration bands. Unisuper is a leader in this regard

[Unisuper] believes the industry should not ignore the basic tenet that remuneration is an important element in attracting and retaining talent. Remuneration also sets an expectation that a Board appointment comes with the obligation to make a contribution worthy of payment.<sup>34</sup>

#### **Best Practice Reporting: Disclosure of Remuneration of Trustees and Senior Management**

- Trustee payments, including all expenses should be disclosed in the same manner as listed public companies are required to disclose their payments to directors
- The same disclosure standards for executive remuneration applying to listed public companies should apply to superannuation fund managers.
- Information for the preceding financial year should be posted in html format on the superannuation fund's website.

## ***Fees & Commissions***

### **1. Fees & Commissions to External Service Providers**

The level of fees and commissions paid by super fund members has been the focus of a major marketing campaign by industry super funds for some years. Distrust of commission based remuneration has become so strident within sections of the industry funds segment that the Industry Funds Forum seriously argued commissions should be banned altogether rather than just disclosed and 'representative trustees' i.e. the industry funds model be mandated.

If commissions were banned, the governance arrangements of promoters could more easily be structured to reflect the success and need for a representative Trustee system to protect and grow Australia's retirement and national savings pool.<sup>35</sup>

This is an extraordinary attack on a rival business model. It smacks of self-interest promotion particularly as IFF says all funds should have a "representative Trustee system" as industry funds do.

Industry funds claim that they charge members lower fees than retail funds. This claim has been disputed on the public record by IFSA to the Senate EEWR.<sup>36</sup> At least one industry fund, Cbus, recognises the current reporting of fees does not adequately capture wholesale investment management fees paid by both industry and retail funds.

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<sup>34</sup> Unisuper. "Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation Industry, Phase 2: Operation and Efficiency. Unisuper Submission." 2009, p.9.

<sup>35</sup> Industry Funds Forum (IFF). "Submission to the Australian Government in Response to the Issues Paper "Phase One Governance"." 2009, p. .

<sup>36</sup> Senate Standing Committee on Education, Employment and Workplace Relations (EEWR). Fair Work Bill 2008 Hearings. Sydney, 18 February 2009, p. 50, 53.

Cbus has some concern that most superannuation funds are not currently adequately reporting on the underlying investment fees incurred within fund of fund investments. For a typical default fund investment structure, this can add up to 20 to 30 basis points to the total disclosed fee. Cbus has spent significant effort on ensuring that all such fees are disclosed as part of our fee reporting to members, but we believe that few other superannuation funds are doing so. Cbus would be happy to discuss this in more detail with the Review Panel.<sup>37</sup>

It may be that retail funds' fees are more clearly declared because retail funds tend to manage their investments directly whereas industry funds make heavier use of outsourced fund managers. It may be that the fund managers charge steep fees that do not show up in the industry funds' balance sheets. For example one scenario could be if 'fees' were left undisclosed by offsetting against lower declared investment returns than would otherwise be the case. There is not enough information disclosed by the superannuation funds to make any assessment.

The Association of Superannuation Funds of Australia details a long list of ways expenses can be hidden from members.

Examples of invisible costs are many and varied – including fees in asset swaps, using intermediate company structures, different treatment for different elements of custody costs, soft dollar brokerage, custodians carving out margins for currency transactions etc.

The list is long and can often involve addition of an extra layer of cost in order to make fees appear lower, which is clearly not in the best interests of members.

Both corporate and public sector funds often incur expenses that are not recovered by fees, e.g. the employer (or government in the case of public sector) subsidises some of the costs of administration (e.g. in staff time spent on fund issues). Some investment fees are not currently captured. Some investment products involving multiple layers of fees (that may not be publicly disclosed by the superannuation funds that invest in the products) and performance fees are not consistently disclosed.

Under the current rules investments could be arranged in such a way that the Indirect Cost Ratio (ICR) for many superannuation funds could be legitimately disclosed as zero.<sup>38</sup>

One thing is known: no-one manages money for nothing. Everyone who manages money must gain income from the exercise to continue in the money management business. What is needed is full transparency by superannuation funds so that assessments can be made of fees, commissions and other costs. Then the accuracy of funds claiming to have lower fees can be put to the test.

## **2. Internal Fees & Expenses**

In addition to fees paid to external parties, whether they be commissions to financial planners from retail funds, investment management fees to fund managers or fees to outsourced fund administrators there are also internal fees and costs.

Payments to trustees and senior executives are not the only internal expenses. All expenses to related parties, other administrative costs and profit margin in the case of retail funds should be disclosed in actual dollar amounts and as a percentage of fund assets.

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<sup>37</sup> cbus. "Superannuation System Review, Phase One: Governance - Submission." 2009, p. 5.

<sup>38</sup> ASFA. "Submission - Super System Review – Phase Two: Operation and Efficiency," 2009, p. 37.

## **Performance**

There are a number of issues relating to superannuation performance that arise due to changing policy positions of successive governments and from the differing returns from the various asset classes and investment managers. These issues relate to comparability, timeliness, value added, relevance and actual return. We recognise that investment performance measurement is an area where policy requires trade-offs and that no one model will suit all investors.

Because this is a report about transparency through disclosure, we will highlight only three aspects of performance measurement: timeliness, consistency and investability.

### **1. Timeliness**

Daily unit pricing should be mandated within the industry as the only appropriate standard to ensure fair treatment of all super fund members. While mandating daily unit pricing for multi-manager funds may seem to be costly and difficult, in most cases those managers will either have end of day asset pricing for their listed investment portfolios or will be managers of slow changing unlisted assets. In either case the information is available. ING Australia sums up why daily unit pricing is the only fair investment performance measurement.

INGA is a strong supporter of unit pricing and proposes that it should be the pricing methodology used for ensuring member equity in a superannuation choice environment. The ongoing cost of daily unit pricing is minimal once it has been established. The benefit of member equity outweighs the cost of implementation and administration. The principle of 'member equity' is essential for any pricing methodology and is endorsed under the ASIC and APRA Good Practice Guide to Unit Pricing. In most cases, superannuation investment options that allow members to transact daily should also be required to price daily. In the case of members buying into an investment option, methodologies other than daily unit pricing, for example crediting rates, may give an advantage to some members and a disadvantage to others depending on their point of buy-in since the real price is not known and members may pay a value for the assets substantially more or substantially less than what they are worth. Daily unit prices are designed to ensure that this inequity may be avoided since the unit price of the investment option will reflect its value.<sup>39</sup>

### **2. Consistency**

Consistency should allow meaningful comparisons of all funds and all similar types of funds. As ASFA advocates below, it is imperative that performance data compares like for like, both in terms of fees and taxes but also risk profiles.

Investment returns should be measured on a consistent post tax and post fee basis. There should be standard rules around which fees should be deducted from the investment return (eg. only investment fees as defined on a consistent, mandatory basis).

In order that fund members can be clear about what they are choosing, and so that investments can be fairly compared, investment options within superannuation funds must be measured and disclosed on a compulsory standardised basis in terms of their risk/return profile.

If investment options continue to be categorised in the current way, there needs to be a compulsory standardised way of categorising assets into "growth" and "defensive". There is also a need for compulsory rules for placing investment options into the categories of "growth", "balanced" etc.<sup>40</sup>

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<sup>39</sup> ING Australia. "Submission to the Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (the Cooper Review)." 2009, p. 12.

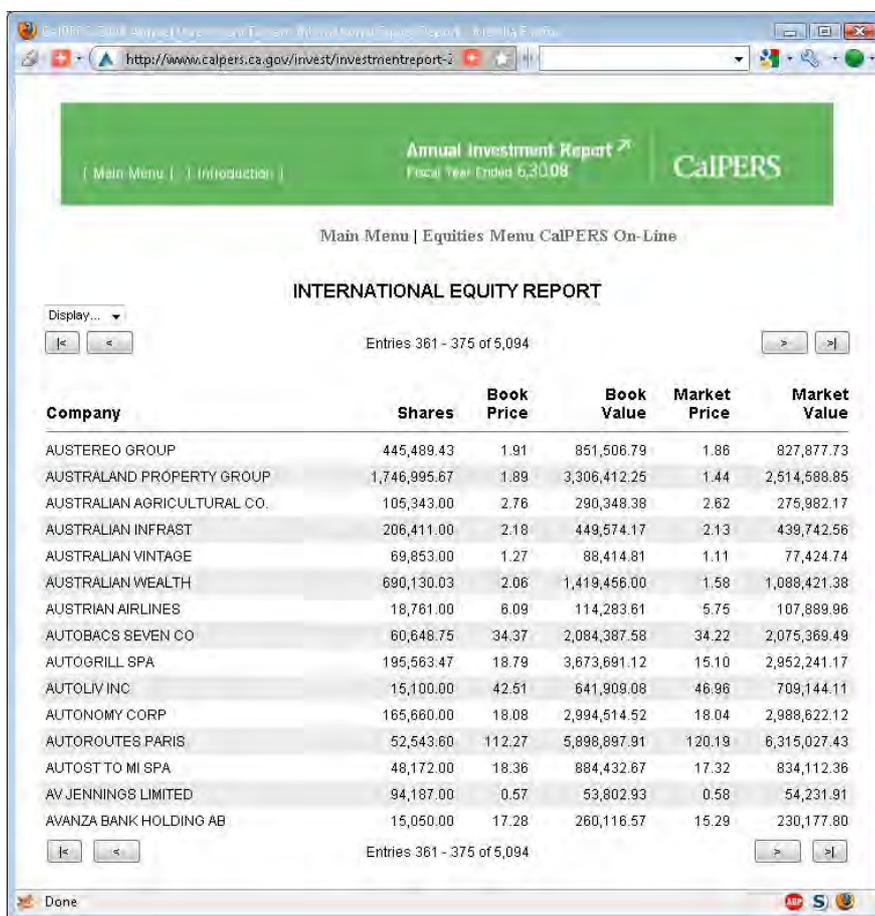
<sup>40</sup> ASFA. "Submission - Super System Review – Phase Two: Operation and Efficiency," 2009, p. 5.

### 3. Investability

A final aspect of performance is mandating what super funds can compare themselves to and related to that, their own benchmarks. At a bare minimum, whatever the fund compares itself to should be something a member could have invested in. Many superannuation funds compare themselves to the CPI which it is impossible to actually invest in. If a fund is not comparing itself to some sort of risk adjusted benchmark based on its own default asset allocation or the industry average asset allocation then an appropriate comparison to use is the cash rate return for the period.

#### **CalPERS: An example of transparency**

The California Public Employee's Retirement System (CalPERS) meets or exceeds the model transparency we advocate. CalPERS lists all shares, both domestic (US) and international, their book value and market value.



The screenshot shows a web browser window displaying the CalPERS Annual Investment Report for the fiscal year ended 6/30/08. The page title is "INTERNATIONAL EQUITY REPORT" and it shows entries 361-375 of 5,094. The table lists various companies with their respective shares, book prices, book values, market prices, and market values.

Company	Shares	Book Price	Book Value	Market Price	Market Value
AUSTERO GROUP	445,489.43	1.91	851,506.79	1.86	827,877.73
AUSTRALAND PROPERTY GROUP	1,746,995.67	1.89	3,306,412.25	1.44	2,514,588.85
AUSTRALIAN AGRICULTURAL CO.	105,343.00	2.76	290,349.39	2.62	275,982.17
AUSTRALIAN INFRAST	206,411.00	2.18	449,574.17	2.13	439,742.56
AUSTRALIAN VINTAGE	89,853.00	1.27	88,414.81	1.11	77,424.74
AUSTRALIAN WEALTH	690,130.03	2.06	1,419,456.00	1.58	1,088,421.38
AUSTRIAN AIRLINES	18,761.00	6.09	114,283.61	5.75	107,889.96
AUTOBACS SEVEN CO	60,648.75	34.37	2,084,387.58	34.22	2,075,369.49
AUTOGRILL SPA	195,563.47	18.79	3,673,691.12	15.10	2,952,241.17
AUTOLIV INC	15,100.00	42.51	641,909.08	46.96	709,144.11
AUTONOMY CORP	165,660.00	18.08	2,994,514.52	18.04	2,988,622.12
AUTOROUTES PARIS	52,543.60	112.27	5,898,897.91	120.19	6,315,027.43
AUTOST TO MI SPA	48,172.00	18.36	884,432.67	17.32	834,112.36
AV JENNINGS LIMITED	94,187.00	0.57	53,802.93	0.58	54,231.91
AVANZA BANK HOLDING AB	15,050.00	17.28	260,116.57	15.29	230,177.80

All unlisted trusts are listed by name, book value and market value. In the example below venture capital funds are presented. It can be clearly seen than all of these investments are valued at below book value, allowing an investor in CalPERS to ask informed questions if that concerns them.

Annual Investment Report  
Fiscal Year Ended 6/30/08  
CalPERS

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VENTURE CAPITAL REPORT

Display... Entries 1 - 15 of 76

Security	Shares	Book Value	Market Value
AACP CHINA VENTURE INVESTORS A LP	812,748.00	812,748.00	716,302.00
AACP INDIA A	1,615,605.00	1,615,605.00	1,366,562.00
AACP INDIA B	2,860,693.00	2,860,693.00	2,845,592.00
ABERDARE VENTURE III	13,500,000.00	13,500,000.00	13,035,036.00
ABS CAPITAL PARTNERS IV	1,517,179.00	-	-
AISLING CAPITAL 11	51,505,790.73	51,505,790.73	47,633,346.00
ALTA BIOPHARMA PARTNERS II LP	26,611,979.68	26,611,979.68	17,279,050.24
ALTA BIOPHARMA PARTNERS LP	22,986,798.74	22,986,798.74	1,125,367.00
ALTA V	11,644,855.56	11,644,855.56	482,142.00
AMERICAN RIVERS VENTURES I LP	12,900,000.00	12,900,000.00	5,077,535.00
APA EXCELSIOR IV	11,153,523.65	11,153,523.65	1,451,802.00
APAX VENTURES IV INAL PARTNERS	2,223,353.39	3,453,974.39	-
APOLLO EURO PRINCIPAL FINANCE	22,333,886.79	35,142,166.54	31,877,385.00
BACHOW INVESTMENT PARTNERS III	19,764,150.38	6,399,498.38	31,477.62
CALIFORNIA EM VENTURES IV LLC	95,725,428.25	95,725,428.25	87,360,957.00

Entries 1 - 15 of 76

In addition to listing all payments of commissions and fees paid to investment managers and stockbrokers CalPERS lists every payment to consultants and professional service firms and also details what the payment was for (see below). These payments range from temporary help for accounts payable through to membership for the Chief Investment Officer at a leadership council.

(Dollars in Thousands)

Individual or Firm	Fee	Nature of Service
Ogilvy Public Relations	\$55	Communications & Marketing
Bongo Post & Music	50	Video, Multimedia & Production Services
California State Teachers' Retirement System	50	Diversity Conference
Method	50	Leeds Educational Display
Robert Half International, Inc.	50	Temp Help for Accounts Payable
Sapphire Technologies, Inc.	44	FSIP Oracle Database Services
Maximus/Center for Health Dispute Resolution	40	Review Member Medical Claim Appeals
Eaton Interpreting Services	40	Sign Language Interpreting Services
CSUS, College of Continuing Education	35	Training Consultation
Sign Language Interpreting Service Agency	35	Sign Language Interpreting Services
Bedrosian & Associates	32	Writing/Editorial Service
Prosci, Inc.	32	Change Management Training
Evergreen Systems, Inc.	32	Server Implementation
Pacific Business Group on Health	31	Internet-Based Health Plan Chooser Tool Management & Maintenance Serv
Jam Media, LLC	30	Video, Multimedia & Production Support
Forrester Research, Inc.	30	CIO Leadership Council Seat
Lincoln Crow, LLC	29	Communication Services
Interaction Associates	29	Facilitation Training Workshop
Page Design Group	28	Digital Design & Production Services
Entsys Solutions, Inc.	27	Citrix Upgrade Project
Runyon, Saltzman & Elhorn, Inc.	25	Communications & Marketing
Kaleidoscope Group, LLC	25	Diversity Awareness Baseline Survey
Dee Hansford Consulting	24	Customer Service Program; Video, Multimedia & Production Support
Pacific Satellite Connection, Inc.	24	Video Production
Los Rios Community College	22	Medical Terminology Training
Adcom Media	21	Multimedia Communication Services
Suzanne Stone Freelance Services	20	Freelance Services
International Foundation for Retirement Education (InFRE)	20	Certified Retirement Counselor Credential Program
Other	154	
<b>TOTAL CONSULTANT &amp; PROFESSIONAL SERVICES EXPENSES</b>	<b>\$177,123</b>	

There is no transaction or asset of CalPERS which they do not fully disclose. The reports are written in such a way that they can easily be understood by anyone with a basic grasp of financial reporting. For people with high-level financial and analytical skills we believe that the CalPERS information would enable extremely high quality analysis to be carried out.

However, as the CalPERS fraud story related earlier shows, disclosure does not prevent fraud. But it does make fraud and misappropriation of funds much more difficult and, if they do occur, more likely that they will be discovered.

CalPERS provides an example of the minimum disclosure standards that should be applied to Australian APRA-regulated superannuation funds.

## **Our own investigations into Australian superannuation disclosure**

To test disclosure in the Australian superannuation sector, we undertook our own investigations. The results further heighten our concerns.

We selected a list of major Australian superannuation funds and did two things:

- Searched their websites for disclosure information and followed up each fund with phone calls to see if additional information would be supplied on request.
- Undertook an Internet search of all publicly available information on the trustees and managers of the superannuation funds and their outsourced fund managers.

We selected 24 industry funds and 12 retail funds. The industry funds are a mix in size (\$1bn to \$30bn), industry (blue collar, professional, white collar) and geographic spread. The retail funds vary in terms of distribution networks, size, internal management and style.

The list is a selection of funds to give an indication of what an ordinary person doing a search could find.

### ***Our findings: Superannuation disclosure of investments***

We ranked industry and retail funds on the asset disclosure model we advocated earlier. For each type of disclosure we allocated a point, so if for example a fund disclosed its top 20 shareholdings in Australian equities it received a point and if it disclosed both the name of its fund managers and how much money it had with each it received another two points. Not all funds invest in all the asset classes available and it is recognised that this methodology will favour a complex fund with good disclosure over a very simple fund with excellent disclosure. As a result we have not included the actual names and points received of the funds we ranked.

No fund fully met the standard of disclosure advocated in this report however some funds do provide substantial amounts of relatively timely information to members and prospective members.

Below we provide a rating of funds disclosure based on our criteria

5 Stars \*\*\*\*\* Fully meets needed disclosure standard

4 Stars \*\*\*\* Approaches needed disclosure standard – typically discloses some individual investments e.g. top 20 Australian shares, has good disclosure of external fund managers used, may disclose names of direct property or infrastructure holdings.

3 Stars \*\*\* Average for Australia but insufficient disclosure – typically has no details of individual investments and no disclosure of direct shareholdings in associated entities but has relatively good disclosure of external fund managers used.

2 Stars \*\* Inadequate disclosure – this is a diverse group containing funds that are poor on external funds managers (often failing to list amounts held with each) but then manage to disclose one other investment type, i.e. direct investment names or associated entity investments.

1 Star \* Poor disclosure – this group provides very little information with usually their only disclosure (out of greater than 20 possible disclosure points) being the names of some of the external fund managers used but with no listing of amounts held with each.

**Table 10 Industry and Retail funds ranked by level of disclosure**

Disclosure Rating	Percentage & (Number)	Percentage & (Number)
	Industry Funds	Retail Funds
***** Fully meets needed disclosure standard	0	0
**** Approaches needed disclosure standard	21% (5)	42% (5)
*** Average for Australia but insufficient disclosure	46% (11)	33% (4)
** Inadequate disclosure	17% (4)	17% (2)
* Poor disclosure	17% (4)	8% (1)

*Source: annual reports, web pages, IPA analysis*

### Industry Funds

Most Industry funds disclosure was at 30 June 2009. Typical disclosure included a list of investment managers by asset class and how much money is managed by each external fund manager. On contacting the funds there is no more recent information available. There is a legal obligation to disclose assets over 5% of the portfolio and most Industry managers interpreted this to mean by fund manager rather than individual assets.

The best disclosing funds reviewed provided substantially more information than the average. One fund provided the top 20 ASX and international share holdings as at 31 December 2009. Current asset allocation was disclosed and a quarterly stock voting report was posted to the website.

Two other funds invest large amounts of their default portfolio in a type of portfolio which invests in infrastructure, private equity, high yield bonds, property and other assets not traded on exchanges. Both of these funds disclose major investments in actual properties and infrastructure investments.

Other funds were judged as above average. One lists individual properties owned by the fund and provides additional information about its properties. Another has the most detailed information on trustee cross-directorships and trustee remuneration. One fund also discloses large infrastructure investments and individual properties.

The Industry Funds classified as below average in disclosure listed their external managers without disclosing how much was allocated to each manager. With a few exceptions there was no listing of direct investments.

### **Retail Funds**

As a group, the Retail Funds offer more disclosure than the Industry Funds. This is particularly true of funds managed by a single manager although even multi-manager funds – the equivalent of most Industry Funds – disclose allocation by manager as at 30 September 2009. In general the retail funds offer more timely information on their websites.

It is necessary to note that most retail funds are owned and operated by wholesale funds managers – the same managers who manage portfolios for the industry funds. If retail funds are capable of publishing their own asset and performance data it must also be available for the wholesale portfolios they manage for Industry Funds.

The best of the Retail Funds were on a par with the best of the Industry Funds in terms of disclosure. For example one retail fund provides the top 10 stocks for single manager funds as at October 2009 and for multi-manager funds twice a year. Another discloses actual asset allocations to 31 December 2009. And another lists every share held in the fund (although without weights) and asset allocation by sector as at 31 July 2009.

The worst disclosure from Retail Funds mirrored poor disclosure from industry funds. One retail fund for example offers relatively good disclosure of single asset class funds they manage but is entirely lacking on information for multi-manager, multi-asset class funds. Another appears to offer no asset allocation information at all for the general public.

### **General Comment**

This rating of 36 funds represents 35 per cent of industry funds and 7 per cent of retail funds and is a sample only. There may be funds not included in this list that may have disclosure levels that we would consider as meeting the necessary disclosure requirements. However our assessment is consistent with comments made by Morningstar and others referred to previously. The standard should be that 100 per cent of funds meet the disclosure standards necessary for an ordinary person to gain a good understanding of what is happening with their superannuation retirement money. This is clearly not occurring.

## **Conclusions**

Australia leads the world in the non-government management of retirement savings. On the evidence from this report, the level of disclosure from the superannuation funds accorded default (monopoly) status is insufficient.

There is insufficient information available from the superannuation funds to be able to make a full assessment about what is occurring with Australians' retirement nest eggs.

Further, the low levels of disclosure mean that the accuracy or otherwise of superannuation funds performance cannot be tested or verified by fund members themselves or anyone with an interest. The compulsory nature of superannuation, in particular makes the poor disclosure highly unacceptable.

Fixing this problem will require the imposition of the highest levels of disclosure on to the APRA-regulated superannuation sector.

## Appendix A: Definitions to understand Super Fund Assets

Assets are what the fund invests in. Superannuation funds may package these varying asset classes into investment options, known as balanced funds, or they may allow members to invest in single asset classes such as Australian Shares.

### Traditional exchange-traded asset classes

These are listed assets. That means they are traded on stock exchanges or other markets and are highly liquid (i.e. easy and quick to buy and sell). These are the asset classes traditionally invested in by superannuation funds. The asset classes are Australian and international equities, listed property trusts, cash, fixed interest. Equities (shares) and property are regarded as growth assets, while cash and fixed interest are defensive assets. This means equities and property have a higher risk and a higher return profile compared to cash and fixed interest.

Listed equities can be single companies such as BHP Billiton or Woolworths but they can also be listed investment trusts. Listed property trusts are one example but others include listed infrastructure funds such as Challenger Infrastructure Fund or private equity funds such as ING Private Equity Access.

The value of these asset classes fluctuates as much as second by second while the exchange is open. And because they are so easily traded the makeup of a portfolio of these types of assets can vary day by day, or even more. A portfolio of traded assets can be valued in real time with end of day reporting standard.

Most superannuation funds invest in these assets via external managers although occasionally a super fund will make a direct investment in a single company or listed trust.

### Unlisted trusts

Popular unlisted investment categories include property, infrastructure and private equity trusts. Unlisted property trusts and infrastructure trusts invest in property and infrastructure respectively in the same way as those listed on stock exchanges but entry and exit from these funds is via application and redemption rather than buying and selling units on the exchange. As a result unlisted property and infrastructure trusts are less liquid (harder to turn into cash) than listed trusts. For example, investors in The Stockland Direct Office Trust No. 3 can apply to sell their units based on the net tangible asset backing for the last quarter, (less a discount). There is a queuing system and limits on how many can be processed in a quarter.<sup>41</sup>

Private equity funds can be venture capital providers to start-up ventures, concentrated in a single industry e.g. biotechnology, or focussed on companies with distressed assets. The scope is very broad and as a result the risk profile of private equity funds varies.

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<sup>41</sup> [http://www.stockland.com.au/investor-centre/unlisted-property-funds2\\_stockland-direct-office-trust-no-3.htm](http://www.stockland.com.au/investor-centre/unlisted-property-funds2_stockland-direct-office-trust-no-3.htm)

Unlisted funds are a growing asset class for many superannuation funds. Specialist firms create portfolios of assets in many categories. These funds can be either open or closed. Open funds allow new money to be invested which the managers then use to invest in further assets. Closed funds do not permit new investment and hold a fixed portfolio of assets to maturity.

The valuation of these assets changes less often than that of listed assets. However, the makeup of the underlying assets also changes less often than for listed assets. While individual shares can be bought and sold within a day, properties and start-up businesses are often held for years.

Superannuation funds can either invest in these trusts directly or engage an external manager who invests in these funds for a number of clients.

#### **Direct investment (including property)**

Some superannuation funds invest directly in certain assets. As was noted above occasionally a fund will buy and sell its own shares or other listed assets. However, by far the largest category of direct investment is property, with some funds such as Cbus having significant proportions of their funds directly owning entire commercial properties.

Increasingly infrastructure is also seeing direct investment by superannuation funds.

The value of direct investments depends on the valuation policies of the fund and typically changes infrequently, perhaps as little as once a year for property and infrastructure but daily for listed shares. And similar to unlisted trusts referred to above, the assets are often held for long periods of time.

#### **Associated entities**

All of the above investment types whether listed or unlisted, managed or direct, have two characteristics. First, they are purchased in the expectation of a measurable investment return, either from income (dividends, interest, rental income) or capital growth. Second, the assets are managed and controlled external to the fund on commercial terms.

As was detailed in the main body of the report, there is also a large, and growing, group of investments associated with Industry Funds Holdings (ISH) and ISPT. Thirty-six industry funds are shareholders in ISH and 24 are shareholders of ISPT. Industry funds also invest in administration companies, promotion companies, financial planners and training organisations controlled by industry funds or the ACTU. Some retail managers may have similar investments in associated financial planning networks, foreign subsidiaries or other associated entities. Many of these assets pay no dividends and their return potential is difficult to assess.