Law Council
OF AUSTRALIA

Legal Practice Section

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Retirement Income and Superannuation Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: superannuation@treasury.gov.au

Dear Treasury

Enhancing member protections in the superannuation system

The Legal Practice Section of the Law Council of Australia welcomes the opportunity to respond to the Treasury's Consultation Paper titled *Enhancing member protections in the superannuation system.* This submission is informed by contributions from the Legal Practice Section's Superannuation Committee and Consumer Law Committee.

The Consultation Paper seeks feedback on proposals for enhancing member protections in the superannuation system. These proposals are being considered in the context of the Shield Master Fund and First Guardian Master Fund matters.

This submission addresses each consultation question in sequence. Where the Legal Practice Section does not consider a question to be applicable, or considers that it raises primarily a policy matter beyond the scope of this submission, that position is identified expressly.

The majority of this submission reflects the views of the Legal Practice Section's Superannuation Committee. However, additional comments from the Consumer Law Committee are included and attributed accordingly. This is particularly the case in the response to Question 38 below.

General remarks from the Superannuation Committee

The Superannuation Committee's view is that the policy objective of improving member protection is important, but that the reforms should be directed to demonstrated deficiencies in in the current legal framework. Law reform should not be implemented to address gaps in compliance, supervision and/or enforcement. This approach may create a risk of overlapping, platform-specific or model-specific obligations where existing trustee duties and prudential standards already address the relevant risks. The existing framework already contains significant obligations relevant to investment due diligence, monitoring and trustee governance, including trustee duties under the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**), APRA Prudential Standard SPS 530 and related guidance.

Telephone +61 2 6246 3788 • *Email* mail@lawcouncil.au
PO Box 5350, Braddon ACT 2612 • Level 1, MODE3, 24 Lonsdale Street, Braddon ACT 2612
Law Council of Australia Limited ABN 85 005 260 622
www.lawcouncil.au

The Superannuation Committee also considers that any reforms should preserve member choice, avoid unnecessary compliance costs, and maintain a level playing field across superannuation trustees and products. The risks identified in the consultation appear to arise principally from the nature of particular investment options, advice practices or conduct failures, rather than from the legal characterisation of a trustee as a platform trustee or from a particular trustee operating model.

General remarks from the Consumer Law Committee

The Consumer Law Committee notes that consumers have suffered astronomical losses as a consequence of the Shield and First Guardian collapses, as well as the collapse of Australian Fiduciaries Limited. Those losses were for many people suffered shortly prior to retirement.

It is the view of the Consumer Law Committee that many of the losses were avoidable or recoverable with better oversight from superannuation trustees and more appropriate and simple redress/compensation pathways.

The Consumer Law Committee notes that unregulated lead generators have had a substantial role to play in encouraging and enticing super fund members to switch their investments from their existing superannuation funds into high-risk, poorly diversified investments.

The Consumer Law Committee encourages strong regulation to protect the interests of consumers and encourages broadening of compensation/redress pathways.

Proposal 1: Strengthening governance requirements for Platform Trustees

Question 1: How should a "Platform RSE" and a "Platform Trustee" be defined?

The Superannuation Committee recommends against the introduction of bespoke statutory definitions of "Platform RSE" or "Platform Trustee" for the purpose of imposing a separate governance regime for platforms. The preferable approach is to maintain a standard set of rules applying across APRA-regulated superannuation funds, because the relevant governance risks concern the investment option offered to members and the trustee's conduct in relation to that option, rather than the label attached to the trustee or product.

Creating a separate regulatory category for platform arrangements would be likely to introduce significant complexity. For example:

- a superannuation trustee may offer both platform and non-platform products, and creating a separate governance regime for the platform products only increases operational complexity and ultimately impacts costs charged to members;
- some products which would not normally be regarded as platform products nevertheless have a platform-like investment option which permits member selection of individual ASX-listed securities or term deposits; and
- some platform products include investment options developed by the trustee itself.

In each of these examples, a platform-specific regime risks drawing distinctions that do not map readily to trustees, products or the risk profile of an investment option.

Another area of complexity is whether the proposed definitions would be introduced to the *Corporations Act 2001* (Cth), the SIS Act, or both. The complexity arises by the fact that the two principal statutory frameworks regulating superannuation use different terminology. The SIS Act refers to concepts such as superannuation interests, choice products, classes of product and trustee-directed products, while the Corporations Act refers to superannuation products and (in the FOFA context) super and non-super platform operators. A single statutory definition intended to operate across those frameworks may therefore be difficult to draft with precision and may generate uncertainty.

The Superannuation Committee is also concerned that different obligations for platform and non-platform products would increase costs for members, because trustees offering both types of products may need to maintain separate policies, systems and processes. Regulatory fragmentation of this kind would be difficult to justify where existing trustee duties and prudential obligations already require appropriate due diligence and monitoring of investment options.

We also note that the existing terminology contained in the SIS Act, introduced as part of the Stronger Super reforms and the Your Future Your Super reforms, is not based on trust law concepts despite the SIS Act otherwise being designed along those lines and all superannuation funds being trusts at general law. This means that there is already a degree of uncertainty in the SIS Act, and we caution against compounding this uncertainty with a new regime based on the existing terminology, however, drafting a new regime with its own concepts would also be a source of confusion and complexity.

If the Government is minded to proceed with its proposals, notwithstanding the above, it may wish to consider leveraging the existing definition of platform operator in section 964 of the Corporations Act, which already has specific rules for superannuation in subsection (3). While this definition is not ideal, it is relatively understood within the industry and has been applied for over 10 years. Significantly, this definition illustrates the reality that a superannuation trustee is not a platform operator "at large" but rather only in relation to a particular underlying financial product (offered as an investment option). In this way, the definition reinforces the concerns expressed earlier about attempts to define "Platform RSE", "Platform Trustee" and "Platform product".

Question 2: Is the term pre-mixed trustee-directed product appropriate for capturing the non-platform and non-member directed sub-category of Choice products?

The Superannuation Committee re-iterates its responses to Question 1 that there should be one set of rules for the investment governance for all superannuation trustees and superannuation funds.

However, to assist Treasury in its considerations, we note that:

- products that would not normally be regarded as platform products can nevertheless offer a large number of investment options, many of which may not be developed / mixed by the trustee; and

- a platform-like investment option which permits member selection of individual ASX-listed securities or term deposits will not satisfy the definition of a pre-mixed trustee-directed product.

Further, an exclusion along these lines will not operate to exclude investment options developed by the trustee which are offered on a platform.

Question 3: Would mandatory holding limits be an effective safeguard to promote diversification and reduce overconcentration risk for platform members?

The Superannuation Committee does not support mandatory holding limits as a platform-specific requirement. Any consideration of holding limits should apply, where appropriate, to all trustees and superannuation products, because the relevant risk concerns the particular investment option and the degree of member exposure to that option, rather than whether the investment is offered through a platform.

Further, the Consultation paper does not make it clear if the holding limits are to apply to an initial investment or to the investment on an ongoing basis. Mandatory holding limits may be capable of operating at the point of initial investment, but they create substantial difficulties on an ongoing basis. A member's exposure may later exceed a limit because of market movements, an increase in the value of an investment, withdrawals from other options or other account transactions. An inflexible obligation to enforce a sell-down in all circumstances may be unfair to members who have valid reasons for retaining the relevant exposure and expose trustees to claims for investment losses and taxes incurred by a member due to a forced sell down.

The Superannuation Committee considers that the better course is to require trustees to consider holding limits (and, if so, on what terms) when determining whether to offer an investment option. The law should also clarify that trustees have an ongoing obligation to monitor investment options, including by periodically considering whether holding limits remain appropriate, and to have a framework to notify members if their exposure to an investment increases over time (e.g. where an investment represents a certain percentage of the member's account balance).

In any event, the Superannuation Committee does not consider that holding limits should apply to managed accounts. Managed account arrangements raise different operational and investment-management considerations, and the imposition of mechanical holding limits may not be well suited to those structures.

The Superannuation Committee also notes that existing duties, including the best financial interests duty and the duties reflected in subsection 52(6) of the SIS Act, may already require trustees to consider holding limits when deciding whether to offer an investment option. The focus should therefore be on clarifying and supporting the operation of those existing duties rather than imposing a prescriptive mandatory holding limit regime.
A mandatory holding limit regime prescribed by the Government or a regulator 'at large' would, unavoidably, risk being less appropriate and less adapted to the risks presented by a particular investment option in the context of a particular product or fund, compared with a limit determined by the relevant trustee.

Question 4: What characteristics of investment options should be considered when setting holding limits?

The Superannuation Committee does not support mandatory holding limits and therefore does not consider that the legislation should prescribe detailed characteristics for setting such limits. To the extent further detail is useful, it should be addressed through prudential guidance, including APRA Prudential Practice Guide SPG 530, rather than through rigid legislative rules.

A guidance-based approach would allow trustees and regulators to consider relevant factors in a manner that is responsive to the characteristics of particular investment options. This is preferable to a statutory formula that may not accommodate differences between asset classes, liquidity profiles, valuation methodologies, member circumstances and product structures.

Question 5: Should codified due diligence obligations be introduced?

Consistent with comments above, the Superannuation Committee does not support codifying due diligence obligations for one sector of the superannuation industry. Platform arrangements may offer a broad range of asset types, and a single codified due diligence obligation may be inappropriate for some assets, may be insufficient for others, and may inhibit trustees from offering new forms of investment exposure where member interests would otherwise support doing so.

The Superannuation Committee instead supports more detailed industry and regulator guidance on due diligence. Such guidance can assist trustees to understand regulatory expectations while preserving sufficient flexibility for trustees to tailor their due diligence and monitoring processes to the nature, scale, complexity and risk profile of the relevant investment option.

This position reflects the broader point that the current framework already includes significant trustee duties relevant to investment due diligence and monitoring. We maintain that the issue is better understood as one of compliance and enforcement rather than a gap requiring a platform-specific codified due diligence regime.

Question 6: What minimum elements should be specified as part of a codified due diligence obligation?

If further detail is to be provided, the Superannuation Committee considers that it should be provided by way of guidance rather than codified legislative requirements. The starting point for any such guidance should be the factors currently identified in SPG 530, supplemented where appropriate to address issues that have arisen in recent matters such as First Guardian and Shield. We note that guidance is already emerging from APRA's recent thematic review of investment governance, the related work APRA that is currently requiring a number of trustees to carry out (via licence conditions or enforceable undertaking) and the lessons for the broader industry that have flowed, and will continue to flow, from those developments.

Any guidance should cover both upfront due diligence before an investment is made available on an investment menu and ongoing due diligence while the investment remains

on the investment menu. It should also emphasise that trustees must identify and manage conflicts that may arise in the due diligence process.

The Superannuation Committee cautions against mandatory detailed rules that attempt to specify every element of due diligence in all circumstances. Such rules cannot realistically be designed to apply appropriately to every entity, asset class and factual context, and they may encourage a "tick the box" approach rather than substantive trustee assessment.

Question 7: Are platform-specific restrictions needed to address conflicted payments or benefits linked to product listing, preferred placement, continued availability or member flows?

The Superannuation Committee considers that further platform-specific bans on conflicted payments are not required. Volume-based shelf space fees are already prohibited under Part 7.7A of the Corporations Act, and the matters identified in relation to Shield and First Guardian do not demonstrate a need for additional platform-specific prohibitions.

The regulatory focus should instead be directed to ensuring that trustee investment governance settings are aligned with member interests. For example, key performance indicators and incentives for due diligence teams should be structured so that they support proper assessment, monitoring and escalation of investment-option risks.

Question 7.1: If so, which types of payments or arrangements pose the greatest risk of undermining a Platform Trustee's independence?

Because the Superannuation Committee does not support the introduction of further platform-specific restrictions, it does not identify a separate category of payments or arrangements requiring additional prohibition under this proposal. To the extent that Treasury is concerned about harmful incentives, the more direct regulatory focus should be on lead generation revenue proposals and related misconduct risks addressed in the separate consultation process.

Question 8: How can restrictions be designed to stop harmful incentives without restricting legitimate operational arrangements?

The Superannuation Committee considers that reforms should target poor conduct and harmful incentives directly rather than restrict legitimate operational arrangements that may support efficient product administration, member access and trustee operations. The Superannuation Committee therefore supports focusing on lead generation revenue issues, where those issues are the relevant source of risk, rather than imposing broad restrictions on platform arrangements more generally.

Question 9: What features of an outsourced model may reduce governance effectiveness?

The Superannuation Committee does not support a regulatory approach that targets any particular trustee business model. The current superannuation framework imposes a high barrier to entry, and the relevant question should be whether each trustee has a proper operating model, appropriate resources and effective governance arrangements.

Outsourcing can present governance risks if the trustee lacks sufficient capability, oversight, information flows or accountability mechanisms. However, those risks are not unique to any one model and should be addressed through generally applicable requirements concerning trustee capacity, resources, oversight and accountability.

The Superannuation Committee also notes that 'external' or 'independent' trustee models may promote innovation and access by new market entrants. A model-specific restriction could therefore reduce competition and innovation without necessarily improving member outcomes.

Question 10: What characteristics could be reflected when differentiating between varying trustee business models, to ensure governance obligations are appropriately calibrated to Platform Trustee environments?

The Superannuation Committee notes its above position that governance obligations should not be calibrated by reference to a platform-trustee category or a particular trustee business model. The preferable approach is to apply robust trustee duties and prudential requirements across the industry, while assessing each trustee's operating model, resources and governance arrangements on their merits.

Question 11: What would the impact be of banning the trustee-for-hire model?

The Superannuation Committee does not support banning the so-called 'trustee-for-hire' model. Such a ban would be likely to reduce innovation, create barriers to access for disruptors and adversely affect members and small businesses that rely on this model.

The Superannuation Committee considers that the policy objective should be to ensure that any trustee using an 'external' or 'independent' trustee model has adequate resources, expertise, governance and oversight arrangements. That approach addresses the underlying regulatory concern without excluding business models that may deliver legitimate benefits to members and the market.

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

Question 14: What length of waiting period would ensure consumers have time to reflect on information before they make a decision?

The Superannuation Committee does not support the introduction of an additional waiting period for inter-fund superannuation switches. The existing rollover and transfer regime is already complex, including different rules for transfers from choice products, illiquid investments and transfers to self-managed superannuation funds.

Adding a further waiting period that applies only in certain circumstances would increase complexity and compliance costs. The transferring fund may need to verify that a member's instruction is genuine, but it should not seek to influence the member to remain in the fund once the member has made a decision.

The Superannuation Committee considers that the existing cooling-off regime in section 1019A of the Corporations Act is designed for and already provides a suitable mechanism for member reflection. That regime provides a 14-day timeframe, which is longer than the period contemplated by some waiting-period models.

The Superannuation Committee recommends that, instead of introducing a new waiting period, Treasury consider clarifying the operation of the cooling-off regime, including the obligation to pay under cooling-off regardless of the liquidity of investments at the relevant time. A simpler and more effective model would be for cooling-off to apply from the date of the welcome letter, with that letter containing the relevant warnings.

The Superannuation Committee also notes that transfers from choice products are not always required to be rolled over within three business days and may occur within a period of up to 30 days—or longer for illiquid investments. This existing timing structure further reduces the case for an additional waiting-period mechanism. It is also unclear how the proposed additional timeframe set out in the Consultation paper would apply when this timing applies to a superannuation switch.

Question 15: Should members switching superannuation funds be required to reconfirm their choice following a waiting period?

We note the Superannuation Committee's position that an additional waiting period should not be introduced. Reconfirmation would add further procedural complexity without addressing the underlying causes of poor switching outcomes. Trustees are also very likely to receive a significant volume of complaints from members who are compelled to give the same instruction twice (at different times) in order to rollover their superannuation savings to the fund of their choice.

Question 16: Would a waiting period have any negative impacts on consumers?

We note the Superannuation Committee's opposition to a waiting period. These concerns include additional complexity, increased compliance costs and the risk of interfering with members' ability to implement legitimate decisions about their superannuation.

Question 18: What challenges may funds face in implementing a waiting period, and how could these challenges be mitigated?

A waiting-period regime would present practical implementation challenges for trustees and administrators. A transferring trustee or its administrator may not know which investment option or options the member is transferring into.

The transferring trustee may also not know the type of product into which the member is transferring, except where the transfer is to an SMSF. This is particularly important because some superannuation funds offer both platform and non-platform products, making it difficult to determine whether the proposed regime applies in a given case.

These operational difficulties reinforce the Superannuation Committee's view that a simpler cooling-off and warning-based model is preferable to an additional waiting-period regime.

Question 19: Should restrictions apply on communications between a financial adviser and the member after the onset of the waiting period?

The Superannuation Committee does not support restrictions on communications between a financial adviser and the member after the onset of a waiting period. There may be many legitimate reasons for continuing communications, including urgent circumstances arising from market disruption, financial instability, geopolitical events or other emergencies.

Restricting adviser-member communications could impair the member's ability to obtain timely advice and make informed decisions. This would be inconsistent with the objective of protecting members' interests.

Question 20: Should consideration be given to a mandatory waiting period applied between the provision of super switching-related financial advice and the acceptance of such advice?

The Superannuation Committee does not support a mandatory waiting period between the provision and acceptance of switching-related financial advice. Such a rule would be difficult to operationalise, particularly where advice is provided as part of a broader advice engagement and where the timing of advice, acceptance, implementation and fee consent may vary between advice models.

Question 21: Should a waiting period apply to all switches, or to a prescribed subset?

We note the Superannuation Committee's position that a waiting period should not be introduced. The Superannuation Committee considers that member protection would be better advanced by warnings, cooling-off settings and targeted action against poor conduct.

Question 22: How should "higher-risk product" be defined?

We note the Superannuation Committee's position that a waiting-period regime should not be introduced. The Superannuation Committee also notes that attempts to define product categories by reference to broad legal labels may create complexity and uncertainty where risk is more closely connected with the conduct surrounding an investment option.

Question 23: Are there exemptions which should be considered so as not to unduly restrict member choice?

We note the Superannuation Committee's opposition to a waiting-period regime. The Superannuation Committee's preferred approach is to avoid introducing a regime that would require exemptions to mitigate undue restrictions on member choice.

Question 24: What content should be included in notifications to consumers switching to a platform RSE or SMSF?

The Superannuation Committee supports warnings that are general, simple and capable of being understood by members. Overly detailed warnings are less likely to be read or understood, and may therefore be less effective in improving member decision-making.

Warnings should focus on poor behaviours and relevant risks rather than imply that SMSFs or platform products are inherently problematic. SMSFs and platform products can provide positive benefits for members, including choice, control and access to a wider range of investment options.

The content of any warning should therefore be directed to matters such as understanding the product, the consequences of switching, fees and costs, investment risks, liquidity, insurance implications and the importance of receiving appropriate advice where relevant. Those matters are consistent with a simple warning model that supports informed choice without discouraging legitimate member decisions.

Question 25: Are regulators or members' current funds more appropriate to provide these warnings?

The Superannuation Committee considers that warnings could be provided as part of the process by which members give rollover instructions, regardless of whether those instructions are given to the transferring fund or receiving fund. This would place the warning at a point where the member is actively considering or implementing the transfer.

Warnings could also be included in the welcome letter issued by the APRA-regulated receiving fund. This is consistent with the Superannuation Committee's preferred model under which cooling-off would apply from the date of the welcome letter and that letter would contain the relevant warnings.

Question 26: Would implementation of this proposal result in significant compliance costs for trustees?

Yes. The Superannuation Committee considers that implementation of a waiting-period proposal would result in significant compliance costs because of the complexity of the existing rollover framework and the practical difficulties in identifying when and how the proposed regime applies.

Question 27: Would there be benefit from requiring receiving funds to collect and provide information on flows into higher-risk products?

The Superannuation Committee refers to its comments on high-risk superannuation switching in the previous consultation. Any additional reporting obligation should be assessed by reference to its utility for regulatory supervision, its proportionality and its compliance burden on trustees.

If Treasury pursues enhanced visibility of fund flows, the Superannuation Committee considers that the reporting framework should be targeted, standardised and designed to avoid duplicative obligations. The objective should be to give regulators actionable information about poor conduct or emerging systemic risks, rather than to require broad reporting that does not materially improve supervisory outcomes.

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

Question 31: Would prohibiting fee deductions for switching-related advice meaningfully reduce harmful or inappropriate switching and improve member outcomes?

The Superannuation Committee does not support prohibiting advice fee deductions for switching-related advice. Existing law already imposes heightened obligations when advice involves superannuation switching and rollovers.

A prohibition would override a member's consent to pay for advice from their superannuation interest and would be likely to reduce access to advice. This is particularly problematic because recommending a more appropriate superannuation product is often a core part of initial financial advice.

The proposal would also be difficult to implement in practice. Advice may cover a range of topics, with superannuation switching being only one recommendation within a broader statement of advice. It would therefore be difficult to determine what proportion of the advice fee relates to switching-related advice.

The advice process may involve the member entering into an advice agreement, receiving switching advice and fee-consent documentation, implementing the advice through a switch to a new fund, and then having the agreed advice fee deducted. In that sequence, the member's agreement to pay for advice may already have been made before the deduction occurs.

The Superannuation Committee is also concerned that the proposal would place trustees in the role of advice regulator. Trustees currently conduct spot checks of statements of advice for compliance with the sole purpose test, but they should not be required to check all statements of advice for new members for compliance with a fee-deduction prohibition.

Requiring trustees to obtain and review advice provided before a person became a member would increase compliance costs and create privacy issues. It would also shift regulatory responsibility away from the appropriate focus on adviser conduct and licensee supervision.

The Superannuation Committee notes that there is no evidence that superannuation switching advice is inappropriate or harmful in most cases. If the policy concern is poor sales tactics or poor advice, the regulatory response should target those matters directly rather than restrict legitimate member access to advice.

The Superannuation Committee supports stronger adviser governance. In particular, a regime under which ASIC identifies and publishes poor actors would give trustees reliable information on which they could act, as occurred where trustees recently cut ties with advice licensees that ASIC identified as being involved in poor lead generation tactics.

Question 32: Under Proposal 4, which option or combination of options would best reduce inappropriate switching while still allowing appropriate access to advice?

We note the Superannuation Committee's position that advice fee deductions for switching-related advice should not be prohibited. The Superannuation Committee considers that reforms should target poor advice, poor sales tactics and poor lead generation practices directly.

Question 33: Should restrictions also be placed on advice fee deductions from SMSFs?

The Superannuation Committee does not support extending restrictions where the underlying case for prohibiting advice fee deductions has not been established.

Question 34: What would be the impact on members' ability to exercise choice and access financial advice?

The Superannuation Committee considers that the impact on members' ability to exercise choice and access financial advice would be significant. Removing the ability to pay for relevant advice from superannuation would exacerbate existing access-to-advice issues.

Reduced access to advice may particularly affect members who need assistance to compare superannuation products, understand investment options, assess insurance consequences or decide whether a rollover is in their interests. This outcome would be inconsistent with a member-protection objective where the advice itself is appropriate and properly provided.

Question 35: If advice fee deduction restrictions were based on a member's total superannuation balance or age, what thresholds would be appropriate?

This question is not applicable in light of Superannuation Committee's position that advice fee deduction restrictions should not be introduced. The Superannuation Committee therefore does not propose balance-based or age-based thresholds.

Question 36: What existing barriers prevent funds from conducting stronger checks before allowing advice-fee deductions?

The Superannuation Committee notes that stronger trustee checks would raise practical concerns, including increased compliance costs, privacy issues and the inappropriate transfer of regulatory responsibility to trustees.

Question 37: How would this proposal interact with a waiting period for switching-related advice?

We note the Superannuation Committee's opposition to both a waiting-period regime and a prohibition on advice fee deductions for switching-related advice. The combination of these measures would increase complexity and may further reduce member access to timely advice.

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

Question 38: Do you consider existing pathways for members to seek redress for financial losses are overly complex and not fit for purpose?

Views of the Superannuation Committee

The Superannuation Committee considers that any compensation regime should be based on fundamental legal principles of fairness and accountability. Where a trustee is at fault, existing mechanisms (including the operational risk financial requirement) already provide a basis for funding compensation.

The Superannuation Committee considers that the focus of reform should be on clarifying the law and strengthening the operation of the operational risk financial requirement (**ORFR**) to ensure these financial resources are available in circumstances involving third-party fraud or fraud in an underlying asset, including matters such as Shield and First Guardian, provided that there is a degree of trustee fault or misconduct.

The ORFR is a prudentially required capital amount that already exists within the regulatory framework and is calibrated to the risk profile of the trustee's operations. The Superannuation Committee considers that ORFR rules could be updated to ensure that the investment profile of a platform—including the nature, complexity and risk characteristics of the investment options offered to members—could inform the assessment underpinning the ORFR and, in turn, the appropriate quantum of ORFR required to be held by a trustee. A trustee that offers higher-risk investment options or options with elevated exposure to third party fraud or operational failure, could be expected to hold a correspondingly higher level of ORFR. This type of risk-calibrated approach could ensure that the protective mechanism is proportionate to the actual risk borne by members without imposing a blanker obligation disconnected from trustee conduct.

The Superannuation Committee also considers it would be beneficial to clarify the permissible uses of the ORFR to ensure that it is available for losses attributed to fraud and other misconduct occurring in an underlying asset provided there is still a degree of fault or misconduct by the trustee.

The Superannuation Committee submits that a strengthened and clarified ORFR framework is preferable to Option 1 or Option 2 below.

The Superannuation Committee has significant concerns with a no-fault compensation regime for platform trustees (or, for that matter, for superannuation trustees of any kind). Such a regime would not be consistent with fairness or accountability if it made trustees liable regardless of whether they caused the loss, could have done anything to prevent it or whether it can recover the loss from others who also caused it.

A no-fault regime would also make trustees liable for losses more directly caused by others and would create an uneven playing field between superannuation and non-superannuation investment structures. It may also create moral hazard, because other participants in the ecosystem may take less care if they are less likely to bear liability for their own conduct.

The Superannuation Committee notes that AFCA already provides a simple and free pathway for members to have issues addressed, and that the large majority of member issues are properly resolved through current pathways. If the proposed regime is fault-based, the Superannuation Committee considers that the essential concept already exists in the current framework.

The Superannuation Committee is firmly of the view that Option 1 should not be pursued. Requiring a superannuation trustee to effectively act as insurer against theft or fraud at the underlying third-party investment level would, with respect, contradict the legal foundational principles of fairness and accountability, and would be particularly egregious in circumstances where the trustee has complied with its duties and obligations at law.

If, however, Option 1 is pursued, the Superannuation Committee considers that it should be triggered only where the platform trustee's misconduct contributed to the loss, so that there is a sufficient link between trustee conduct and member loss. The Superannuation Committee also recommends that any determination of the amount of such a pool should be based on a risk assessment (similar to the approach adopted for operational risk financial resources), noting the difficulty in assessing fraud risk in underlying assets because of a lack of information (that due diligence would be unlikely to identify). Noting that the platform trustee's insurance may not cover losses of this type, the Government should also consider whether the platform trustee should be granted statutory rights to recover loss from others who also contributed to the loss.

If the Government were minded to pursue Option 1, it should also consider platform trustees' liability for levies under the Compensation Scheme of Last Resort given that platform trustees would effectively be underwriting a large proportion of potential loss that the scheme could otherwise ultimately be liable for.

The Superannuation Committee does not support Option 2, under which ASIC would have powers to direct remediation. Remediation obligations agreed in enforceable undertakings with Macquarie and Netwealth illustrate one of the more appropriate pathways for ASIC to pursue remediation. Alternatively, where an organisation does not agree with ASIC's remediation expectations, it is open to ASIC to seek remediation via the Courts, which is precisely what it has done with EQT in the case of Shield, and Diversa in the case of First Guardian. The Superannuation Committee submits that ASIC should not be given powers to direct remediation outcomes that currently require either agreement or resort to the curial process.

If the Government were minded to pursue Option 2, the Superannuation Committee recommends:

- the power only be enlivened if ASIC has reasonable grounds to believe that the AFS licensee has contravened a provision of a law regulated by ASIC and members have suffered loss or other financial detriment due to that contravention; and
- the power be limited to require the AFS licensee to establish a remediation program to rectify the misconduct and remediate clients who have been affected by the misconduct, and to appoint an independent expert to oversee the program.

Views of the Consumer Law Committee

The Consumer Law Committee's view is that the experience of the victims of the Shield and First Guardian collapse demonstrates significant gaps in terms of the redress that is reasonably able to be obtained by consumers.

Existing pathways for members to seek redress for financial losses arising from the collapse of superannuation platform investment products are, in the Consumer Law Committee's view, both overly complex and structurally inadequate. The Consumer Law Committee wishes to direct the Government's attention to a specific dimension of this problem that is not adequately addressed by the proposals in the consultation paper as currently framed: the position of members whose losses are causally linked to a failure by a Trustee to perform adequate due diligence in selecting or retaining a product on its platform.

The AFCA jurisdictional exclusion for management of the fund as a whole

AFCA has rejected most complaints made against Superannuation Trustees in respect of the Shield and First Guardian Collapse, and alleged failures in due diligence made against superannuation trustees. AFCA's rejection of such complaints is on the basis that the complaints are said to be about the management of the fund as a whole, as contemplated by AFCA Rule C.1.5(b).

Importantly, the Corporations Act establishes the AFCA Scheme and defines what constitutes a superannuation complaint.[1] The Corporations Act does not prohibit the consideration of a complaint in relation to the management of a fund as a whole. That exclusion arises only as a consequence of the AFCA Rules.

Prior to AFCA's establishment superannuation complaints were considered by the Superannuation Complaints Tribunal pursuant to the *Superannuation (Resolution of Complaints)* Act 1994 (the **ROC Act**). Subsection 14(6) of the ROC Act provides an express statutory exclusion from consideration of a complaint if the complaint was made in relation to the management of a fund as a whole.

That is, there is no statutory exclusion that would prevent a superannuation fund member from complaining to AFCA in respect of due diligence failures by a super fund trustee. However, the Consumer Law Committee notes that the Shield and First Guardian victims are being turned away by AFCA on the basis of the application of a rule of the AFCA scheme.

The consultation paper itself acknowledges that AFCA has identified that many complaints against superannuation trustees in the Shield and First Guardian context related to the management of the fund as a whole and were therefore outside AFCA's superannuation jurisdiction.

It is clear at law that where a trustee of a superannuation fund has made a decision in respect of a member that is or was unfair or unreasonable, such a decision is a decision that would enable a member to complain to AFCA and seek redress.[2] Importantly, such a

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1 *Corporations Act 2001* (Cth), s.1053(1)(a).
2 Ibid, s.1053(1)(a).

decision includes a failure to make a decision.[3] In this regard, the Consumer Law Committee suggests that where a trustee, acting in accordance with its fiduciary and statutory obligations, forms the view that its own failures might have caused a member losses, the trustee ought to make a decision to pay compensation to any such member and accordingly the failure to make such a decision is, under the Corporations Act, a relevant decision that enables a consumer access to AFCA for external dispute resolution purposes. However, that is not how the AFCA Rules are being applied by AFCA at present.

The Consumer Law Committee notes that this exclusion has profound consequences for affected members. A Platform Trustee's decision to list an investment product on its platform, and the adequacy of the due diligence process applied before and during that listing, is characterised under AFCA's approach as *management of the fund as a whole*. As a result, an individual member who can demonstrate a direct financial loss caused by a trustee's failure to conduct reasonable due diligence cannot bring that specific complaint before AFCA in the superannuation jurisdiction.

The Consumer Law Committee is of the view that this creates a structurally unjust outcome. The due diligence obligation is imposed precisely to protect individual members. The breach of that obligation directly causes individual financial harm. Where a member asks for compensation and the trustee makes a decision to refuse that request, that should enliven an entitlement to seek redress from AFCA. Yet the mechanism through which the breach is characterised removes the individual member's ability to pursue compensation through the accessible, free, and expert external dispute resolution pathway that the financial services regulatory framework is designed to provide.

Alternative pathways do not adequately fill the gap

The Consumer Law Committee acknowledges that members may have recourse to other avenues, but submits that none adequately substitutes for accessible external dispute resolution in this context.

- **AFCA general jurisdiction:** Where a financial adviser was involved in the member's decision to invest, complaints against that adviser may be considered under AFCA's general jurisdiction. However, this does not assist members who received no personal financial advice (such as the victims of the Australian Fiduciaries Limited collapse), whose adviser is insolvent or cannot be located, or whose losses are attributable primarily to trustee rather than adviser conduct.
- **ASIC enforcement action:** Enforcement action is strategic, discretionary, and cannot serve as a substitute for individual member facing redress. The experience of the court-enforceable undertakings obtained from Macquarie Investment Management and Netwealth, while welcome, demonstrates that compensation through enforcement pathways is available only in a subset of cases, is not automatic, and does not arise within a timeframe that addresses the immediate financial impact on members.
- **Part 23 SIS Act assistance:** This mechanism is discretionary, slow, requires APRA advice, and is subject to a public interest test. It is not a member-initiated pathway and cannot be relied upon as a primary or reliable source of compensation for individual members.

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[3] Ibid, s.1053(5).

- **Litigation:** Individual and class action proceedings are available in principle but are time consuming, costly, and uncertain. Members who have lost substantial retirement savings are frequently not in a position to absorb litigation risk, and the complexity of liability across multiple entities scheme operators, financial advisers, trustees, and responsible entities compounds the difficulty.

The Consumer Law Committee submits that the foundational principle of the Australian financial services consumer protection framework is that regulated entities owe enforceable legal obligations to the consumers they serve, and that consumers should have accessible pathways to enforce those obligations when they are breached. That principle is not currently honoured in the superannuation trustee context, where the very conduct most central to member protection the exercise of investment governance and due diligence—is the conduct least amenable to member-initiated challenge.

The reforms proposed in this consultation offer a genuine opportunity to address this structural deficiency. The Consumer Law Committee urges the Government to ensure that any reformed framework closes, rather than perpetuates, the gap created by the exclusion which currently exists in AFCA's rules in relation to the management of the fund as a whole.

Question 39: Should the requirement to compensate members from trustee capital be pre-funded or post-funded?

The Superannuation Committee's preferred approach is to clarify the operation of existing mechanisms.

Question 40: If a pre-funded requirement were adopted, should it be principles-based or prescriptive?

The Superannuation Committee does not support the creation of a pre-funded no-fault compensation requirement for platform trustees.

Question 41: What criteria and evidentiary threshold should apply to determine that a loss is attributable to external fraud or theft and therefore an "eligible loss"?

The Superannuation Committee's concern is that trustee liability should not arise without a sufficient connection between trustee conduct and the member's loss.

Contact

The Legal Practice Section would welcome the opportunity to discuss this submission. In the first instance, please contact Maged Girgis, Chair of the Superannuation Law Committee [redacted] or Dana Beiglari, Co-Chair of the Consumer Law Committee [redacted].

Yours sincerely



Greg McIntyre SC
Chair, Legal Practice Section