

ACCC Minute

Office	Darwin and Melbourne
Date	10 September 2020
To	Stewart McKechnie
From	Kerin Callard and Declan Harrington
Subject:	Superannuation industry in Australia – ACSI & common shareholdings

1. Purpose

1.1. The purpose of this minute is to summarise the state of the superannuation industry in Australia. In particular, this minute focuses on the Australian Council of Superannuation Investors (**ACSI**), its membership and its potential use as a vehicle to consolidate separate shareholder interests in ASX-listed companies. This minute also explains concerns around common shareholdings as they may relate to the superannuation industry.

2. Structure

2.1. The structure of this minute is as follows:

- Section 3 provides an overview of the superannuation industry in Australia, including the role of ACSI and its membership.
- Section 4 explains the competitive landscape of the superannuation industry, including levels of market concentration, competition and barriers to entry, as well as the competitive considerations around common shareholdings.
- Section 5 provides an overview of previous government inquiries into the superannuation industry.

3. Background

The superannuation industry in Australia

3.1. As of June 2018, there were 217 institutional superannuation funds in Australia which can be broadly categorised as retail, industry, public sector or corporate funds.[1] While

[1] A retail fund is a superannuation fund that offers superannuation products on a 'for profit' basis; industry funds are funds originally formed to provide access to superannuation for employees working within a particular industry; corporate funds are funds sponsored by a single employer or group of related employers for the benefit of company employees; and public sector funds are funds designed for employees working in the public or government sector.

assets under management are spread fairly evenly across each category of fund, 82 per cent of member accounts reside in retail and industry funds.[2] In total, superannuation funds comprise over 15 million members and collectively own over $2.7 trillion in assets, playing a key role in the funding of Australians' retirement.[3] In December 2017 the superannuation sector was the second-largest sector in the Australian financial system by size.[4]

3.2. The modern superannuation system began with the introduction of the Superannuation Guarantee in 1992, which extended superannuation coverage to 72 per cent of Australian workers and established prescribed contributions for employers. Since 2005, most employees have been able to choose their superannuation fund and, in effect, the product to which they want to direct their superannuation contributions.[5]

3.3. The revenue of superannuation funds is driven by share market performance, which has been strong over recent years. However, the industry is forecast to record a significant loss due to COVID-19.[6]

3.4. The ACCC has had limited previous engagement with the superannuation industry. There have been a small number of superannuation authorisations (in 2016/17) and superannuation scams frequently appear in our Scamwatch work.

3.5. In recent years, a number of government reviews have considered the superannuation industry. These reviews are discussed below at section 5.

ACSI

3.6. ACSI was established in 2001 and its stated aim is to provide a 'strong, collective voice on environmental, social and governance issues on behalf of [its] members'. It engages with companies to influence their environmental, social and governance (**ESG**) performance.

3.7. ACSI's Annual Reports indicate that it undertakes four types of work, being research, engagement, voting advice and advocacy. This work can be summarised as follows:[7]

- Research – ACSI produces reports on ESG issues such as modern slavery, ESG reporting and CEO remuneration.
- Engagement – In FY19 ACSI held 267 meetings with 192 ASX300 companies. These meetings are aimed at enhancing long-term shareholder value[8] and moving beyond 'AGM agendas' to regularly engage on ESG issues.
- Voting Advice – In FY19 ACSI provided 1 711 voting recommendations to its members on resolutions involving 324 meetings across ASX300 companies. These recommendations help its members to exercise their voting rights to align with ACSI's engagement work on ESG issues. ACSI also offers a proxy voting service for certain members.

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[2] Productivity Commission Inquiry Report: 'Superannuation: Assessing Efficiency and Competitiveness', 21 December 2018 (Productivity Commission Inquiry), pp.85-86.

[3] Productivity Commission Inquiry, p.3.

[4] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry: 'Consumer Interactions with the Superannuation Industry', p.6.

[5] Productivity Commission Inquiry, p.92.

[6] IBISWorld: 'Superannuation Funds in Australia' (IBISWorld), p.4.

[7] ACSI: 2019 Annual Report.

[8] ACSI: 'What we do'.

- Advocacy – engaging with government, regulators and other intermediaries on ESG issues.

3.8. By working collectively, ACSI members aim to achieve material outcomes for their beneficiaries and deliver genuine and permanent improvements to the ESG practices of the companies in which they invest. ACSI has 38 members, 31 of which are Australian superannuation funds.[9] These superannuation funds are:

- Australian Catholic Superannuation Retirement Fund
- AustralianSuper
- CareSuper
- Catholic Super
- CBUS
- Club Plus Super
- Christian Super
- EnergySuper
- Equipsuper
- First State Super
- First Super
- HESTA Super Fund
- Hostplus
- Legalsuper
- Local Government Super
- LUCRF Super
- Maritime Super
- Media Super
- Mine Super
- MTAA Super
- NGS Super
- Qantas Super
- QSuper
- REST
- State Super
- Statewide Super
- Tasplan Super
- TelstraSuper
- TWUSuper
- UniSuper
- VicSuper
- Vision Super

3.9. These superannuation funds include some of Australia's largest (by funds under management).[10] ACSI estimates that its members collectively own on average 10% of every ASX200 company.[11]

3.10. ACSI is one of four major proxy advisers in Australia. In 2018 ASIC released a report on proxy adviser engagement practices in Australia.[12] In its report ASIC found that institutional investors considered proxy advisers as just one input in their voting decisions and that concerns about the amount of weight institutional investors give to proxy advisers were overstated.[13] ASIC's media release states that proxy advisers are a useful way of investors obtaining more information about their voting decisions.

3.11. ASIC's report contained a number of good practice recommendations for proxy advisers and companies including a recommendation that companies should ensure

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[9] The remaining seven members are Australian and international asset owners and institutional investors (Australian Institute of Superannuation Trustees, APG, IFM Investors, NZ Super Fund, RPMI Railpen, Universities Superannuation Scheme Limited and VFMC).

[10] ACSI: 'Who our members are'; SuperGuide: 'Comparing super funds'.

[11] ACSI: 'Who our members are'.

[12] ASIC: 'ASIC review of proxy adviser engagement practices', June 2018 (ASIC review).

[13] ASIC review, p.4.

that confidential, price-sensitive information is not selectively disclosed to proxy advisers during engagement.

3.12. The three other proxy adviser firms, Glass Lewis, Ownership Matters and ISS Australia, do not list on their websites who they advise but do not appear to have a similar focus on superannuation.

4. Competition in the Australian superannuation industry

Market concentration

4.1. The Australian superannuation industry has low market concentration with the top four superannuation funds accounting for less than 20% of industry assets.[14] These major players are Australian Super (6.4%), AMP Limited (4.3%), QSuper (4.1%) and First State Super (4%).

4.2. The number of superannuation funds has decreased over the last five years due to an increase in mergers. This is driven by a desire to reduce fees and offer a greater range of products.[15] However, it is anticipated that the benefits obtained by market consolidation will be offset by increased regulation.[16]

4.3. In addition, the Productivity Commission has noted that while market concentration is low, it is sometimes superficial and that this affects smaller funds, which pay higher fees, disproportionately.[17] Despite the market consolidation which has already occurred, substantial unrealised scale economies remain.[18]

Competition

4.4. The Productivity Commission concluded that competition in the superannuation industry is not being fully harnessed due to a lack of engaged membership and rivalry between funds to attract and retain members. In addition, poor comparability of options and other factors indicate a lack of healthy competition.[19] This is amplified by the lack of competition in the ‘default’ market, by which up to two-thirds of new job entrants do not choose their own fund but instead are subscribed to a fund of their employer’s choosing.[20]

4.5. IBIS World indicates that within the market, superannuation funds compete on their performance and fees charged to consumers. They also compete with other investment related products such as property and financial markets.

Barriers to entry

4.6. There are high barriers to entry due to high regulation, high costs and the already large number of competing funds in the market. However, individuals are able to start

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[14] IBISWorld, p.26.
[15] IBISWorld, p.13.
[16] IBISWorld, p.16.
[17] Productivity Commission Inquiry, pp.58, 325-7.
[18] Productivity Commission Inquiry, p.22.
[19] Productivity Commission Inquiry, p.515-16.
[20] Productivity Commission Inquiry, pp.528, 576-7.

a self-managed superannuation fund with assets exceeding $200,000. Such funds are unlikely to have a significant impact on large superannuation funds.[21]

Common ownership of firms through investment funds

4.7. Common ownership refers to the simultaneous ownership of shares in competing firms by institutional investors, below the level of control. These institutional investors (which may be banks, pension funds, insurance companies, mutual investment funds or other) are normally passive investors; that is, their shareholdings are 5 per cent or less and they typically do not have board representation.[22]

4.8. Globally, there are only some jurisdictions where acquisitions of non-controlling minority shareholdings are subject to review. For example under the EU merger review regime, only transactions which lead to the acquisition of control or to a meaningful change in the nature of control are subject to review. In the US, however, any acquisition of 10 per cent or more of the voting securities of another firm is subject to review unless that acquisition is solely for the purpose of investment.[23]

4.9. The OECD, while noting that more research is needed, has recently indicated that common ownership in firms through diversified investment funds may have a detrimental impact on market competition in certain concentrated sectors (particularly airlines and banking). An oligopolistic market where competitors share common shareholders may lead to higher prices, a higher chance of collusion and incentivise management to consider industry or investment fund performance rather than that of the individual firm.[24]

4.10. In particular, the OECD identified that common ownership could incentivise institutional investors to facilitate coordination among portfolio firms. An investor holding shares in multiple firms in an industry may act as a ‘cartel ringmaster’, passing information between the parties and monitoring compliance. This is amplified in a concentrated industry where common owners hold a significant amount of a company.[25]

4.11. The OECD identifies the establishment of voting blocs as the most straightforward mechanism by which this might occur, allowing an institutional investor to exert effective (or at least sufficient) control over voting rights and influence, particularly with respect to governance and ownership structure. Referring to Australia as an example, the OECD noted that the reliance of institutional investors on proxy voting advisers, which analyse shareholder voting decisions and make recommendations, can strengthen the stability of these blocs.[26] However, the extent to which the recommendations of proxy advisers actually distort overall voting results is unclear.[27]

4.12. The OECD report noted that there is growing concern about the concentration of voting rights, and potential conflicts of interest, associated with institutional investors employing proxy advisory firms to analyse shareholder voting decisions. This concentration could be a source of concern from both a corporate governance and competition policy perspective. These proxy services could be a catalyst for common

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[21] IBISWorld, p.30

[22] Kluwer Competition Law Blog: ‘Common ownership – where do we stand?’, 15 April 2019.

[23] OECD: ‘Common Ownership by Institutional Investors and its Impact on Competition’, 5-6 December 2017 (OECD report), pp.7-8.

[24] OECD report, p.5.

[25] OECD report, p.20.

[26] OECD report, pp.22-23.

[27] Muraca and Freeman: ‘Regulation of proxy advisory firms’.

ownership competition impacts, since they could serve to explicitly identify the common interests of institutional investors within an industry and form voting recommendations accordingly.[28]

4.13. Ultimately the OECD indicated that further analysis is needed, and that the application of cartel or merger rules to situations where common ownership may impact competition should be considered. In the meantime, the OECD noted that market studies may be an opportunity to gain visibility into markets with substantial institutional investor ownership.[29]

5. Previous Australian Reviews

5.1. In 2013 the government appointed a committee to conduct the Financial System Inquiry (**the Inquiry**). The final report, which published in November 2014, found that superannuation is not efficient due to a lack of strong price-based competition and, as a result, the benefits of its scale are not being fully realised. It also questioned whether the government's 'MySuper' reforms would improve competitive pressures in the superannuation industry. Those reforms were intended to put in place a set of regulatory standards for default superannuation funds to provide low-cost, transparent and comparable set of products which achieve better outcomes for members which do not choose their own fund or investment strategy.[30]

5.2. The Inquiry made a number of recommendations in relation to setting clear objectives for the superannuation system, improving operational efficiency during accumulation and improving efficiency in retirement. The Inquiry led to the Productivity Commission's 2018 report.

5.3. In June 2018 the Productivity Commission completed a review into the provision of financial services in Australia. While this report touched upon superannuation in its analysis, it did not make any specific findings or recommendations, noting that the Productivity Commission was conducting a separate inquiry into superannuation and the establishment of the Royal Commission.

5.4. In December 2018 the Productivity Commission conducted an inquiry into the efficiency and competitiveness of Australia's superannuation system and whether better ways to reallocate defaults are needed. The Productivity Commission found that structural flaws, such as underperformance and multiple accounts, are harming millions of members and that inadequate competition, governance and regulation led to those outcomes. The Productivity Commission made a number of recommendations to modernise the super system which focused on increased accountability and transparency.

5.5. The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry submitted its final report to government on 1 February 2019. It made a number of recommendations about changes to the superannuation system, including that the regulatory powers of ASIC and APRA be strengthened.

[28] OECD report p36

[29] OECD report, pp.40-41.

[30] Productivity Commission Inquiry, p.80.

5.6. On 27 September 2019 the Treasurer announced a review of the retirement income system in Australia, following a Productivity Commission recommendation (**Review**).[31] The Terms of Reference require the Review to identify:

- how the retirement income system supports Australians in retirement;
- the role of each pillar in supporting Australians through retirement;
- distributional impacts across the population and over time; and
- the impact of current policy settings on public finances.

5.7. The Review was due to report to Government by June 2020, however the report is not publicly available and may have been delayed due to COVID-19.

5.8. None of these inquiries or reviews have raised concerns about common ownership or proxy advisers in relation to superannuation.

[31] Treasury: 'Retirement Income Review'.