

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry
 – HESTA Submission 29 January 2018

Attention: Commissioner Kenneth Hayne

29 January 2018

BY EMAIL: FSRCSolicitor@royalcommission.gov.au

Dear Commissioner,

I write in response to your letter addressed to me, as Chief Executive Officer of HESTA, dated 15 December 2017. You invited in your letter responses to questions you have posed in respect of HESTA as part of the *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* ("Royal Commission").

We welcome the opportunity to make an early written submission to the Royal Commission and commit to engaging openly in keeping with our organisational culture and values, and advocating for the welfare of our members. To ensure we are able to assist the Commission in its inquiries as best as we can, we have engaged external advisers to provide us with guidance in addressing your queries.

Our external legal representatives are Philip Solomon, QC and Mark Irving SC instructed by Michael do Rozario and Michael Chaaya of Corrs Chambers Westgarth.

I have taken the liberty of providing some brief background to HESTA for context, and have then set out our response to each of your questions.

About HESTA

Health Employees Superannuation Trust Australia ("Fund") was established in 1987 as an industry superannuation fund to provide retirement benefits for workers principally in the health and community services sector.

The Fund is a profit-to-members fund that currently has more than 840,000 members, over 70,000 contributing employers and manages over \$41 billion of members' assets. Approximately 80% of HESTA members are women.

The Fund is managed and operated by a corporate trustee, H.E.S.T. Australia Ltd ("Trustee") – a public company limited by guarantee and regulated by various sources of legislative, regulatory and prudential obligations. The Trustee's current guarantors consist of 10 Employer Guarantors and 5 Employee Guarantors from the health and community services sector. HESTA¹ is structured under the equal representative trustee model, with its affairs governed by a Board of Directors consisting of representatives nominated by eligible guarantor organisations. This ensures that voices of both employers and members are heard as decisions are made in the best interests of members.

There are 14 Trustee Directors on the Board, with an Independent Chair, and an Independent Director who serves as the Chair of the Investment Committee.

HESTA is dedicated to preparing and empowering members for wellbeing in retirement and focused on growing the benefits delivered to members and employers. This is done by achieving strong, competitive long-term investment performance and providing value for money on fees, insurance coverage that is appropriate to members and advice and education services.

HESTA members work across the health and community services sector, which includes:

- nursing and midwifery
- early childhood education
- community services
- aged care
- primary health care.

¹ The Fund and Trustee are hereafter collectively or interchangeably as appropriate, referred to as "HESTA" for ease of reference.

HESTA's products and engagement model are specifically tailored to address the needs of members in the health and community services sector.

The unique characteristics of HESTA members, such as broken work patterns, lower salaries and higher incidences of casual or contract-based employment, play a pertinent role in and influence how HESTA's service model is customised for members to ensure HESTA achieves its mission to make a real difference in the retirement outcome of every member.

The size and potential growth of the sector means that competition for superannuation funds is strong with many funds active in the sector. This along with a diverse workforce has resulted in a market that is multi-faceted, complex and highly contested.

Question 1

Excluding cases of theft from the entity itself, or from an associated entity, has the entity identified any misconduct by the entity (including by its directors, officers or employees, or by anyone otherwise acting on its behalf) which occurred at any time since 1 January 2008? If so, what is the nature, extent and effect of that misconduct?

Definition and guiding principles

HESTA notes the definition of misconduct under the Terms of Reference includes conduct that;

- a) *Constitutes an offence against a Commonwealth, State or Territory Law, as in force, at the time of the alleged misconduct;*
- b) *Is misleading, deceptive, or both;*
- c) *Is a breach of trust, breach of duty or unconscionable conduct; or*
- d) *Breaches a professional standard or a recognised and widely adopted benchmark for conduct.*

The following matters have been reviewed since 1 January 2008 ("relevant date") against the definition of misconduct above:

1. Communications with regulatory bodies
2. Complaints
3. Audit Findings
4. Compliances breaches
5. Tribunal matters
6. Litigated matters
7. Human resource matters
8. Governance matters

HESTA has conducted a detailed assessment as outlined below, and has not identified instances of misconduct, however, discloses two matters.

Matter 1 (Trust Deed): Having regard to the decision in *Retail Employer Superannuation Pty Ltd v Paine*², HESTA believes that it is in a similar position to the Applicant in that case. As a result of the potential inconsistency between the trust deed's provisions in relation to amendment, there is a potential that certain amendments are inconsistent with the trust deed and depending on the view taken by the Commissioner potentially within the scope of paragraph (c) of the definition above. HESTA has commenced proceedings in a matter currently before the Supreme Court of South Australia, seeking similar relief to that sought by *Retail Employer Superannuation Pty Limited*.

Matter 2 (Custodian Account): In April 2010, HESTA's Registrable Superannuation Entity ("RSE") Licence contained a condition that all assets be custodially held. At that time, HESTA identified that an account relating to an investment option that many members had invested in was in fact held in HESTA's name directly, and not custodially. HESTA self-reported this matter to APRA and rectified the error. There was no loss or other detriment to members. It is noted that HESTA's RSE licence no longer requires that assets be held custodially.

In the 10 year period, there have been no other matters that fall within the definition of misconduct.

It is not clear to us whether the Commissioner considers that the matters disclosed above constitute misconduct as defined in the terms of reference. HESTA does not consider that either matter constitutes misconduct as that would ordinarily be understood. Neither of the matters disclosed under this heading involved any dishonesty or deliberate action to benefit any person to the

² [2016] SASC 121 (hereafter *REST v Paine*).

detriment of HESTA's members. Both matters are of the nature of inadvertent errors that HESTA has identified and sought to correct. In each case HESTA confirms that no losses to members arose as a result of the issue disclosed.

We have set out below the process that HESTA has taken to respond to this question and more details in relation to the two matters disclosed in response to it.

Assessment

In reviewing its conduct (including that of its Directors, Officers and employees, and those otherwise acting on its behalf) HESTA has considered the following matters since 1 January 2008 ("the relevant date").

1. Communications with regulatory bodies

HESTA holds an RSE Licence which is subject to ongoing supervision by the APRA including regular prudential supervision, consultations, and thematic reviews. HESTA has assessed the findings of these supervision activities since the relevant date against the definition and guiding principles, and has not identified any misconduct.

HESTA is an Australian Financial Service Licensee and its conduct in relation to products and services is regulated by ASIC. Since the relevant date HESTA has infrequently been requested to provide information to Australian Securities and Investment Commission ("ASIC") in relation to its conduct under ASIC's powers in 912E of the Corporations Act. HESTA has assessed the findings of these surveillance activities against the definition and guiding principles, and has not identified any misconduct.

HESTA is a taxed entity regulated by the Australian Taxation Office ("ATO"). Since the relevant date, HESTA has had infrequent communications with the ATO outside of ongoing statutory reporting obligations. HESTA has assessed these dealings with the ATO on tax matters against the definition and guiding principles, and has not identified any misconduct.

HESTA is a registered tax (financial) adviser and its conduct in relation to tax (financial) advice services are regulated by the Tax Practitioners Board ("TPB"). Other than registration, renewal of registration and maintaining registration details, HESTA has had no communications with the TPB regarding its conduct.

HESTA is an APP entity under the Privacy Act 1988, and its conduct in relation to the collection, use and disclosure of personal information is regulated by the Office of the Australian Information Commissioner ("OAIC"). Since the relevant date HESTA has had no communications with the OAIC regarding its conduct.

HESTA is a reporting entity under the Anti-Money Laundering and Counter-Terrorism Financial Act 2006, and provides designated services that are regulated by AUSTRAC. Since the relevant date, HESTA has had infrequent communications with AUSTRAC outside of ongoing statutory reporting obligations. HESTA has assessed these dealings with AUSTRAC in relation to designated services against the definition and guiding principles, and has not identified any misconduct.

2. Complaints

HESTA has an internal dispute resolution process designed to deal with any expression of dissatisfaction with products and services.

The key themes of HESTA complaints experience are individual dissatisfaction with:

- administration issues; such as processing delays, duplicate accounts, and timing of transactions
- insurance arrangements; such as unwanted default cover, death benefit distribution decisions, declined insurance claims, and underwriting decisions
- HESTA complying with the superannuation administration law; such as financial hardship rules, lost member rules, and contribution tax deduction rules
- the application of HESTA's fees and costs.

When a complaint is received it is investigated by HESTA's outsourced administrator in accordance with HESTA's dispute resolution process and the relevant legislative requirements applicable to the subject matter of the complaint. The response to the complainant is subject to approval of HESTA's internal complaints team. Where a complainant is dissatisfied with HESTA's response, the complainant may escalate the matter

further to an external dispute resolution scheme. A vast majority of HESTA's complaints do not progress to external dispute resolution.

Complaints are reported to the Board on a quarterly basis.

HESTA has assessed all complaints received since the relevant date against the definition and guiding principles, and has not identified any misconduct.

3. Audit findings

Since the relevant date HESTA has engaged an external auditor. PwC is the current external auditor and EY acted in this capacity to the end of the 2012/13 financial year. Since 1 July 2013, HESTA has also had an internal audit function, which is performed by KPMG.

The External Auditor and internal audit function report directly to the Audit and Risk Committee – a subcommittee of the Board.

All external audits have returned unqualified audit opinions to date. HESTA has assessed the findings of audit reports since the relevant date against the definition and guiding principles and has not identified any misconduct.

4. Compliance breaches

HESTA has an internal compliance team with responsibility for the identification, management and resolution of compliance breaches.

The vast majority of HESTA's compliance breaches occur from errors in the administration of member accounts which generally result in breaches of privacy, disclosure or superannuation laws.

Under HESTA's Incident Management Policy every breach is assessed for materiality by an internal Incident Review Panel consisting of members of the management team from compliance, risk and the impacted business unit. The assessment considers factors including the number of members impacted, the number of previous similar incidents, the number of other obligations unable to be fulfilled, the length of time taken to detect the breach, the systemic nature of the breach and any actual or potential loss to members or HESTA. HESTA's Incident Management Policy, including the assessment process, has been provided to APRA and ASIC during supervision or surveillance activities noted in (1). All but one of HESTA's breaches since the relevant date have been determined to be not significant for the purposes of regulated reporting requirements.³

The one significant breach was identified in April 2010 and related to a condition of HESTA's RSE license that required all assets to be "custodially held". It was identified that an account was erroneously established by the custodian which held assets directly in the name of HESTA. Although the assets in the account were minimal and there was no financial impact on HESTA or members, the breach was deemed significant as the assets were of an investment option in which a significant number of members are invested. The breach was reported to APRA and they required no further action from HESTA. It is noted that the requirement for assets to be "custodially held" is no longer a requirement of the RSE licence.

HESTA has assessed compliance breaches since the relevant date against the definition and guiding principles, and has not identified any misconduct.

5. Tribunal matters

HESTA is a member of the Superannuation Complaints Tribunal ("SCT") and Financial Services Ombudsman ("FOS"). Since the relevant date HESTA has been involved in matters which primarily relate to administration delays and errors, insurance coverage or determinations, and death insurance beneficiary disputes. In 2017 the Federal Government announced the establishment of the Australian Financial Complaints Authority ("AFCA") to replace the SCT, FOS and Credit and Investments Ombudsman. HESTA is currently preparing for its transition to the new AFCA regime.

HESTA has assessed these matters against the definition and guiding principles and has not identified any misconduct.

³ Section 29JA of Superannuation Industry Supervision Act 1993 and section 912D of Corporations Act 2001.

6. Litigated matters

Since the relevant date HESTA has been involved in litigated matters pertaining to superannuation and insurance complaints as detailed at point 5 above. Of those matters a limited number have escalated to proceedings commenced in the relevant courts. None of these court related matters have resulted in any findings of wrongdoing on HESTA's part.

In addition, HESTA on occasion participates in class actions typically via a class action funder in respect of its investments.

In 2016, prompted by the judgment handed down in *REST v Paine*, HESTA identified potential concerns pertaining to the trustee powers under the HESTA Trust Deed and undertook a review of the Deed and its historical amendments. As a result of this review, it was identified that there were a number of historical amendments to HESTA's Deed that could be considered to have been made outside the trustee's powers to make amendments. HESTA engaged external lawyers to provide advice on and undertake detailed analysis of its Deed which resulted in HESTA conducting a review of members' accounts to determine whether members had been adversely impacted. It was confirmed in this review that no members suffered actual loss or were disadvantaged as a result of those amendments in question.

Further to this, HESTA has now lodged an application in the Supreme Court of South Australia to have this matter considered, and its Deed formally revised and approved by the Court. APRA have been advised of this matter and intend to request to be joined as an intervener to the proceedings.

7. Human resource matters

HESTA has 184 employees across Australia and occasionally experiences human resource issues relating to employee performance or behaviour.

These matters generally relate to inappropriate behaviour towards other employees and performance issues relating to failure to meet internal standards.

In assessing these matters against the definition and guiding principles, HESTA has not identified any misconduct.

8. Governance matters

HESTA has a Governance Framework in accordance with Prudential Standard SPS 510 Governance.

The Governance Framework covers matters relating to the Board such as director appointment and removal, tenure, training, performance, code of conduct, remuneration and whistleblowing.

HESTA has not identified any misconduct in relation to governance matters.

HESTA has raised two matters above. As identified, HESTA does not consider either of those matters to comprise misconduct as it would ordinarily be understood. Accordingly, HESTA has not identified any misconduct at any time since 1 January 2008.

Question 2

Has the entity identified any conduct, practice, behaviour or business activity it has engaged in (including by its directors, officers or employees, or by anyone otherwise acting on its behalf) since 1 January 2008, which it considers has fallen below community standards and expectations? If so, what is the nature, extent and effect of that conduct, practice, behaviour or activity?

Definition and guiding principles

In answering this question, the term "community standards and expectations" has been considered and has been guided by the Commission's Terms of Reference ("ToR"), in particular the following statement:

All Australians have the right to be treated honestly and fairly in their dealings with banking, superannuation and financial services providers. The highest standards of conduct are critical to the good governance and corporate culture of those providers.

The same matters were reviewed at Question 1 against the above guidance on community standards and expectations.

HESTA discloses one instance that it believes may have fallen beneath community standards and expectations.

Matter 3 (CommInsure):

Between December 2011 and February 2018, CommInsure has been engaged by HESTA to provide group life and income protection insurance to HESTA members. As is notorious, it was identified in 2016 that CommInsure policies contained clauses that were identified as being inconsistent with acceptable practice in the insurance industry. As described in detail below, HESTA undertook a process of engagement with affected members. Whilst satisfied that all member issues have now been satisfactorily resolved, HESTA accepts that the CommInsure policies previously offered by it in certain respects did not meet community standards and expectations.

Background to HESTA's insurance claims process

HESTA offers its members group life and income protection insurance through an external insurer. HESTA's group insurance policies for its members are held with CommInsure.⁴

Where a member seeks to make an insurance claim, they will directly contact HESTA to initiate the claim and obtain the necessary forms to complete. The member then submits the relevant forms together with supporting evidence directly to the insurer who will assess the members' eligibility under the terms of the insurance policy. The insurer may then either request further information, for example medical evidence from the member's treating medical practitioner, make a determination to accept and pay the claim, or decline the claim.

For insurance claims arising as a result of a member's death, HESTA liaises with the late member's beneficiaries while the insurer assesses the late member's entitlements which, if accepted, are then paid into the late member's HESTA account while HESTA makes a determination as to which beneficiaries the late member's benefits are payable to.

When an insurance claim is declined, HESTA's internal Claims Review Committee ("CRC") reviews each and every one of these declined claims, to ensure HESTA agrees that the decision made by the insurer to decline the claim is correct, in accordance with the terms and conditions of the insurance policy, and is fair and reasonable. The CRC is comprised of qualified insurance experts and similarly trained insurance professionals from HESTA's external administrator. The CRC meets regularly to review and discuss each claim. The CRC advises the insurer whether the Trustee might expect they obtain further information before declining, or should in fact continue to pay the member entitled benefits where appropriate, or whether the Trustee agrees with the position taken by the insurer to decline the claim.

⁴ HESTA's insurance policy arrangements with CommInsure expire on 28 February 2018, after which its group insurance policies will be held with AIA Group.

Business activity and practices in question

In 2016 CommInsure's practices in dealing with insurance claims were investigated and widely reported in the media. As a result of the allegations made against CommInsure around inappropriately declining insurance claims, the insurer commissioned an independent review by external experts of declined claims, amongst other processes and practices. These allegations gave rise to HESTA seeking a review of insurance claims made by HESTA members that were declined by CommInsure. In particular, HESTA reviewed, together with the claims team at CommInsure, claims where:

- a CommInsure Medical Officer had been involved in the assessment of the claims (Death and Income Protection)
- HESTA's internal Claims Review Committee had initially disagreed with CommInsure's decisions to decline the claims, but ultimately agreed with CommInsure's assessment to decline
- HESTA members had escalated their claim through the escalation process as informed by CommInsure at the time.

Of the above claims reviewed during September to December 2016, it was found that 9 of those claims required a reassessment by CommInsure. These were subsequently re-reviewed by HESTA and determined to be incorrectly declined or managed claims. All 9 of those claims were appropriately remedied by July 2017. For context, 4225 claims were made by HESTA members in 2016. This is generally reflective of the annual volume of claims HESTA receives.

In addition to the above categories of claims reviewed, HESTA undertook reviews for two specific categories of claims that had emerged from industry investigations as having a higher likelihood of being declined:

- Claims subject to the medical condition defined under the policy documents as "Severe Rheumatoid Arthritis" – to ensure that members were being assessed under a revised definition (and old if this was more beneficial to member)

1 claim was found to have been incorrectly paid as a temporary incapacity, however on review it was converted to permanent incapacity. This did not result in any change to insurance benefits payable to the member but rather removed the requirement for the member to undertake ongoing medical assessments to confirm their eligibility to be paid

- Declined terminal illness (or where initially declined and then admitted but paid a lesser amount due to change of age)

No claims were found to have been incorrectly determined.

Further to the above, HESTA also undertook a review of its own internal processes and policies concerning the management of insurance claims. HESTA determined these processes and policies incorporated sound practices that were routinely adhered to by its internal team. On that basis and the outcomes of the claims review described above, HESTA did not identify any necessary changes to its processes or policies.

Conclusion

HESTA has not identified any conduct, practice, behaviour or business activity since 1 January 2008 that has fallen short of community standards and expectations, subject to the abovementioned matter.

Question 3

If yes to either or both of questions one and two:

a) Is the identified conduct, practice, behaviour or activity the subject of another inquiry or investigation, or a criminal or civil proceeding?

Matter 1 (Trust Deed): As identified above, HESTA has commenced proceedings in the Supreme Court of South Australia seeking orders similar to those sought in *REST v Paine*.

Matter 2 (Custodian Account): No

Matter 3 (CommInsure): Yes. ASIC conducted extensive investigation and examination of CommInsure's practices, including reviewing over 60,000 documents and interviewing staff. ASIC obtained files from dispute resolution schemes, spoke to consumer advocacy organisations and obtained independent medical and legal advice. ASIC released a public report on this investigation on the 23rd March 2017.

b) Does the entity consider that the identified conduct, practice, behaviour or activity to the particular culture or governance practices of the entity? If so, describe that culture or governance practice.

Matter 1 and Matter 2: No.

Matter 3: In relation to issues arising from the practices and business activities of HESTA's external insurer, HESTA does not consider that this matter was attributable to the culture or governance practices of HESTA as an organisation. From a HESTA perspective, the outcomes of the review and inquiries made when the concerns arose demonstrated that HESTA has a robust framework for reviewing and assessing insurance claims. It was prevalent in the review outcomes that HESTA's governance practices and cultural behaviours in this area are rightly focussed on achieving positive outcomes for members.

c) Does the entity attribute any of the identified conduct, practice, behaviour or activity to some broader cultural or governance practices in the industry or sector of the industry in which the entity operates? If so, describe those cultural or governance practices.

HESTA does not consider that the above identified matters are attributable to broader issues or concerns with the cultural or governance practices in the wider industry or sector.

d) What steps has the entity taken to:

i. Remedy the consequences for consumers or other businesses of the identified conduct, practice, behaviour or activity;

Matters 1 and 2: There are no relevant consequences for consumers or other businesses.

Matter 3: As part of the review undertaken with respect to HESTA's appointed insurer CommInsure, it was identified that 9 members were adversely impacted by having their insurance claims incorrectly declined. As outlined earlier, a detailed review process was undertaken by HESTA together with CommInsure and these members have been remediated with their claims being paid. No other businesses were impacted by this matter.

No further remedial actions were considered necessary and HESTA and its members have been satisfied with steps undertaken to resolve this.

ii. Prevent recurrent of conduct, practice, behaviour or activity of the kind identified?

HESTA does not believe that the identification any of Matters 1 to 3 suggests that there are broader systemic issues such that action needs to be taken to prevent any recurrence.

In relation to Matter 3, HESTA works closely and engages regularly with its insurer to work collaboratively in reviewing insurance claims and the efficacy of this process is again demonstrated in the outcomes of the review undertaken with CommInsure.

When HESTA's insurance policies with CommInsure were due to expire, a detailed tender process was undertaken to ensure HESTA's insurance offering remained appropriate to delivering the needs of its members. HESTA's business practices are always under continuous review for improvement, and this business practice provides us with comfort that matters such as those occurring with CommInsure are not systemic.

Question 4

a) During each of the past ten years (according to whatever annual reporting periods the entity has employed in the ordinary course of its operations) to what uses and in what amounts has the entity applied members' funds other than the investment of those funds, the administration of the superannuation fund and the payment of member benefits?

Background to HESTA's fees as and how they relate to expenditures

HESTA charges members two base fees - an administration fee and investment fee. The administration fee comprises of a weekly dollar amount plus an account based percentage; this is deducted monthly from members' accounts and then paid into HESTA's reserve accounts. This is distinct from members' superannuation funds which remain in their accounts and are applied to investments on their behalf or the payment of member benefits.

HESTA's investment fee is an account-based percentage fee that is deducted from investments before earnings are applied to members' accounts. These investment fees are applied to items related to HESTA's investment of members' superannuation funds.

It has been identified that during the relevant period, HESTA has applied funds towards the following categories of expenditures that do not fall within the categories of investment, administration or payment of member benefits:

- Branding
- Industry Super Australia and joint industry campaigns
- Sponsorship
- Business Development.

These expenditures are drawn from funds available in HESTA's reserve accounts, which as mentioned earlier accumulate from the administration fees charged to members. These expenditures are not drawn from members' funds.

HESTA notes that the fee and cost disclosure obligations under Corporations Act 2001 requires the inclusion of all costs incurred in the operation of the fund to be included in the Administration fee. This we believe is distinct from the information being requested in this question, which implies a narrower construction of administration expenses. Therefore, while all costs of operating the fund are funded through the Administration fee, the above expenditures are the part of those costs we believe do not fit the narrower construction of administration.

As a superannuation trustee HESTA is also cognisant of the requirement that the fund must be maintained for the sole purpose defined within section 62 of the Superannuation Industry (Supervision) Act 1993. HESTA's expenditure in the categories noted above are guided by APRA's published materials on the sole purpose test⁵, and have been discussed with APRA as part of HESTA's prudential review consultations over the years. HESTA is not aware of any expenditures that do not satisfy the sole purpose test.

⁵ Letter to all trustees of APRA regulated superannuation funds, APRA, 14 March 2015
Superannuation Circular No III A 4

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Summary of expenditures in the four categories for each year of the relevant period

In a competitive marketplace, the need for investing in scale, innovation and underlying infrastructure has been balanced with meeting member expectations around returns, access, engagement, responsiveness and support.

Operating expenses applied to these areas over the past ten years are broken down as follows*:

	2017 (\$)	2016 (\$)	2015 (\$)	2014 (\$)	2013 (\$)	2012 (\$)	2011 (\$)	2010 (\$)	2009 (\$)	2008 (\$)
Branding	7,605,636	6,142,231	5,304,378	6,445,739	4,692,886	4,053,001	3,777,380	3,105,089	2,246,359	3,699,065
ISA & Joint Campaigns	3,511,278	3,540,295	3,421,732	3,237,262	3,208,356	3,198,143	3,296,083	3,268,184	3,267,337	3,245,560
Sponsorship	2,002,313	1,966,770	1,428,443	1,318,645	1,220,734	1,203,625	1,157,440	1,314,482	1,260,342	1,134,161
Business Development	659,390	536,048	275,344	193,399	72,017	-	-	-	-	-
Total Non-Admin Expenses	13,778,617	12,185,344	10,429,897	11,195,045	9,193,994	8,454,769	8,230,902	7,687,755	6,774,038	8,078,786
FUM (\$ billions)	41.4	35.5	33.1	28.6	23.8	19.6	18.4	15.5	12.9	13.6
% of Members Monies (FUM)	0.03%	0.03%	0.03%	0.04%	0.04%	0.04%	0.04%	0.05%	0.05%	0.06%

*Note: Best endeavours have been made to align expenses across years and categories, to account for changes to systems, accounting practices, reporting lines, etc, which have taken place. Due to legal requirements to only hold financial data for seven years, data beyond this time period (i.e. from FY2010 and earlier) is less detailed.

b) In respect of each kind of those other applications of members' funds, why was that application in the best interests of members?**Background on HESTA's performance and positioning in the market**

In the abovementioned applications of funds that HESTA considers do not fall within the categories of administration, investment or payment of benefits, HESTA has determined that those funds were expended on other areas being in the best interests of its members. It is considered that these expenditures go to achieving outcomes in the overarching themes of growing HESTA and helping members achieve better retirement outcomes.

HESTA has developed a view over a long period of time that there are significant benefits for members in the fund having appropriate scale and pursuing growth so that these benefits of scale are accretive over time for all members. Those benefits of scale include (but are not limited to):

- Keeping operating costs low
- Expanding the range of appropriate products and services available to members
- Supporting HESTA's long term patient investor approach, and ability to attract quality investment opportunities
- Being able to focus on continuously improving customer experiences and having higher customer satisfaction levels than the industry
- Delivering a superior net benefit to members (against the industry average).

This view is supported by the analysis provided by key benchmarking consultants. The 2017 SuperRatings Benchmark report provided to HESTA in February 2017 showed that over the past year:

- HESTA's market share of total assets had increased by 4.2% to 1.7% of the total market
- HESTA experienced a 1.2% rise in the number of accounts compared with the industry median decline of 1.3%
- HESTA further sustained a 1.1% fall in operating expenses accompanied by strong growth in net assets
- HESTA's management expense ratio fell from 0.30% to 0.27%, whilst HESTA's cost per member fell from \$113 in 2015 to \$109 in 2016.

The SuperRatings report further noted that "Over the past decade, HESTA has delivered \$6,221 in additional earnings relative to the average fund, while charging \$3,713 less in fees. Accordingly,

this would have added \$9,934 to a member's account for a member with a \$50,000 starting account balance and salary."

Branding

Branding is in the interests of members because strong branding drives member, employer and funds under management growth which in turn allow HESTA to deliver better services and outcomes to members.

A key component of HESTA's marketing activities is the development of the HESTA brand. HESTA operates in an extremely competitive environment, with highly-contested competition for members and contributing employers in the health and community services sectors. The ultimate beneficiary of the strong HESTA brand is members, as detailed above.

The major benefits of having a strong HESTA brand, which in turn will drive strong member, contributing employer, and funds under management growth are as follows:

- Having a strong brand builds customer recognition, which in turn drives potential member and employer acquisition.
- The HESTA brand is what differentiates it in a highly competitive marketplace, and contributes significantly to both member retention and acquisition.
- A key component of HESTA's advertising focus is shared values with members and employers in health and community services. These shared values build an emotional connection with customers and potential customers.
- Not only does HESTA compete for members and employers, it also competes for talent. Having a strong HESTA brand is a key component of HESTA's employee value proposition, enabling attraction and retention of key talent and capability which supports HESTA's ability to continue to serve members.
- A further dimension of this competitive environment is the competition for quality investment opportunities. Having a strong brand presence, and the ability to attract and retain talented employees in all areas of Fund activities including investment management and execution functions has proven to be very important in being able to secure the opportunity to invest in quality assets. This is clearly in the best interest of all members.

HESTA is committed to supporting and encouraging members to actively plan for their financial futures and achieve an improved retirement outcome. Ensuring members receive relevant, timely and effective superannuation and financial information that can help them engage with their super is a key objective of HESTA's branding activities.

In addition, a strong brand also enables engagement with members and employers. The superannuation industry has long sought to overcome persistent low engagement by members with their retirement savings. HESTA research indicates that these barriers to engagement are even more acute when it comes to women engaging with their personal finances.

To do this HESTA continually looks for innovative ways to reach and engage members across an increasingly diverse range of mediums that they are interacting with whether that be via digital and social media channels or traditional media platforms.

HESTA's branding activities support the growth of HESTA and assist members achieve better retirement outcomes – both of which are considered in the best interests of HESTA members.

Industry Super Australia and joint industry campaigns

Joint industry campaigns are in the interests of members because they assist superannuation consumers in making educated and informed decisions about their retirement savings.

Industry Super Australia ("ISA") undertakes joint industry activities including marketing campaigns, policy, research, government relations and public advocacy work on behalf of industry superannuation funds that elect to be participants of ISA. The purpose and objectives of the activities undertaken by ISA are to maximise the retirement benefits delivered to the members of the funds, approximately made up of 5 million Australians. The education and promotion of industry funds to the wider community as a distinct category within the broader superannuation industry is important to assisting superannuation consumers in making informed decisions about their retirement savings.

HESTA engages ISA to provide specific campaign services as part of HESTA's business strategy for a fee. ISA also provide a platform for industry superannuation funds to collectively advocate on pertinent superannuation policy matters impacting on its members. HESTA is of the view that engaging in this collective activity is an efficient and effective way for it to access quality research and advocacy.

ISA have also undertaken the joint "Industry Super Funds" campaign ("ISF"), which promotes the values of industry super funds and their profit-to-members business models.

Sponsorship

Sponsorships are in the interests of members because they deliver opportunities for HESTA to continue to grow and retain the employer and membership base in order to obtain benefits of scale for its current members. Engagement with strategic partners is designed to ensure HESTA has efficient and effective opportunities to engage with existing and prospective members and this is facilitated by sponsorship arrangements with relevant and appropriate organisations.

HESTA enters into sponsorship arrangements with key stakeholders from employer and employee representative organisations within the health and community services sector. HESTA's sponsorship activities have been developed to ensure it remains the primary fund of choice within the health and community services sector, retains and continues to have the support of current members, and to attract new members and contributing employers. These activities support growth through both acquisition and retention.

HESTA has a Sponsorship Policy to ensure that it assesses and approves, manages and reviews the sponsorships undertaken. Where sponsorship arrangements are entered into with HESTA's guarantor organisations, HESTA's conflicts management processes and policies ensure these are undertaken on appropriate commercial terms and any necessary controls applied to manage any actual or perceived conflicts that may arise.

The aims of the HESTA sponsorship arrangements include:

- Maximising brand exposure amongst delegates attending forums and the broader audience to whom the event is promoted
- Tailoring the promotion of HESTA where appropriate to capture future growth opportunities and retention activities within an increasingly competitive market
- Improving engagement with key stakeholders which include, but are not limited to current and potential peak bodies, unions and current and potential employers.

HESTA sponsorship arrangements enable engagement via:

- attendance and participation at state and national conferences
- member forums
- award programs which acknowledge individuals and organisations in health and community services
- promotion via health and community services industry publications.

Engagement assists with improving the knowledge and awareness of the products, services and benefits offered to employers and members, so that informed decisions and choices can be made about superannuation. This engagement assists members and employers in making the most out of their superannuation arrangements and retirement benefits, which fundamentally go to achieving the best possible outcomes for members.

Business development

Business development is in the interests of members as it creates, develops and nurtures the relations with new potential employers and members, which in turn leads to the growth of HESTA.

Growth is crucial for the success of HESTA and the successful retirement outcomes of both current and future members. Growth delivers scale benefits as noted above and is vital to ensuring HESTA remains sustainable in delivering on its objectives to its members.

HESTA uses business development activities to grow its number of members. Business development activities include responding to requests from employers and stakeholders for information about HESTA and promoting the HESTA value proposition to potential members, employers and the health and community services sector.

Assessment of overall costs and benefits

HESTA is focused on keeping costs and expenses at an appropriate level, and assess these on an ongoing basis against an appropriate cohort of funds. The services of SuperRatings are engaged to help assess the benefit to members delivered by HESTA's scale, using a range of simple, consistent and transparent measures to provide an independent view of a fund's scale.

One of the major assessments considers the Net Benefit, which measures returns less all fees and taxes, and the fees levied on a member, under a consistent set of assumptions. HESTA's net benefit to member is displaying a 'Leading' trend, with outperformance recorded over 1 and 5 years, while the fund's fee on a \$50,000 account balance also continues to exhibit a 'Leading' trend. In addition, on a cost basis, HESTA is positioned within the Lowest Operating Cost Quadrant, with its level of operating expenses, relative to the size of its membership base and assets, positioned below industry medians.

c) What are the cost centres that make up costs attributed to administration in each of those years?

The cost centres attributed to administration in each of the past ten years are detailed below*, with those years relevant to that cost centre identified by a "✓".

Administration cost centre	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
Total Outsourced Administration	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Employer Arrears Collection	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Regulator & Licence Fees	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Professional Fees (Audit, Actuarial, legal fees, tax, etc)	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Depreciation & Amortisation Expense	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Employee Training & Development	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Postage, Courier & Direct Mail	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Insurance	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Finance Expenses/Bank Charges	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
IT Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Communication Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Servicing and meals	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Motor Vehicle Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Office Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Other Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
(Gains)/Losses on Disposal of Property, plant and equipment	✓	✓	✓	✓						
Premises Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Employment Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Subscription & Membership	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Telephone & Internet	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Business Travel	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Board Expenses	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓

* Please note that best efforts have been made to align expenses across years and categories, to account for changes to systems, accounting practices, reporting lines, etc, which have taken place. Due to legal requirements to only hold financial data for seven years, data beyond this time period (i.e. from FY2010 and earlier) is less detailed.

We have provided, below, a description of the activities within each administration cost centre:

Administration cost centre	Key activities include:
Total Outsourced Administration	Amounts paid to our external administrator to assist in administering the Fund, which covers, operating the Fund's contact centre, contribution and benefit processing, insurance administration, regulatory changes, system upgrades, account maintenance and any corrections, and other general fund administration.
Employer Arrears Collection	Arrears collection costs, including legal fees relating to arrears.
Regulator & Licence Fees	Annual levies/fees paid to APRA and ASIC to regulate the RSE and Fund.
Professional Fees (Audit, Actuarial, legal fees, tax, etc)	Payments to our service providers, for example, external audit (year-end audit fee of financial statements and APRA Return), internal audit (internal audit function and Quality review audit fees), tax agents fees and advice, actuarial fees (current exempt pension income tax deduction), legal fees (advice covering review of legal contracts, trust deed etc.)

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Administration cost centre	Key activities include:
Depreciation & Amortisation	The charge for depreciation/amortisation of our property, plant and equipment, which includes office equipment, computer hardware and laptops etc.
Employee Training and Development	Employee training costs including mandatory AFS License training, technical training and upgrade, driver education and first aid training.
Postage, Courier & Direct Mail	General postage (stamps, Australia Post), courier charges and freight charges, direct mail expenses
Insurance	General and travel insurance premiums
Finance Expenses/Bank Charges	Bank account charges and corporate card fees
IT Expenses	Ongoing software license costs, IT service provider fees, costs associated with Business Continuity Plan, non-capital IT purchases
Communication Expenses	These costs include design of Publications/Fund literature and printing (PDS, brochures, member and employer magazines) and website development/hosting.
Servicing and Meals	Servicing our employer/members through employer visits, presentations/seminars including meals/catering
Motor Vehicle Expenses	Motor vehicle leasing, maintenance, insurance premiums and registration, fuel and other consumables
Office Expenses	Document Storage, Repairs, Office Supplies / Stationery, Other Equip & Service Charges, In-House Catering
Other Expenses	Sundry operating expenses
(Gains)/Losses on Disposal of Property, plant and equipment	Accounting for profit/loss on disposal of property, plant and equipment
Premises Expenses	Rental - office space (nationwide), car parking spaces, security costs, office lighting and heating, cleaning costs
Employment Expenses	Salary/wages - permanent and temporary employees, payroll tax, annual leave, long service leave, superannuation, work cover premium costs, recruitment costs, FBT
Subscription & Membership	Subscriptions to newspapers, periodicals, books. Subscriptions and Membership costs to organisations eg ESG membership, AIST, Women in Super, CA, CPA, FPA
Telephone & Internet	Telephone and internet expenses
Business Travel	Travel related expenses including accommodation, meals, taxis, airport parking, airfares, rail tickets, car hire
Board Expenses	Director Fees including super, payroll tax, Director training and development, travel costs (including - airfares, accommodation, meals), Director professional indemnity insurance premiums

We trust the above information is helpful for the Commission and would be happy to provide any further clarifications required. Please direct any communications to HESTA to both me and Jordan Lam, Company Secretary & General Counsel by phone on ([REDACTED]) Our direct contact details have been provided to the Royal Commission via email.

Yours sincerely,



Debby Blakey
 CEO
 HESTA

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