



Australian Government
Department of Finance



Department of Finance

Submission to the Finance and Public Administration Legislation Committee

Investment Funds Legislation Amendment Bill 2021

September 2021

Prepared in consultation with the Department of Health, the Future Fund Management Agency, the Australian Public Service Commission, the Attorney-General's Department, the National Recovery and Resilience Agency, the Department of the Prime Minister and Cabinet and the Treasury

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Introduction

Since the Future Fund was established in 2006, the Future Fund Board of Guardians (Future Fund Board), with the support of the Future Fund Management Agency (FFMA) has grown the Future Fund by over \$136 billion. The Future Fund Board has also become responsible for managing 5 other Australian Government investment funds, with total funds under management of more than \$245 billion as at 30 June 2021.

As the size of the Australian Government investment fund portfolio continues to grow and the investment environment becomes increasingly challenging, the Investment Funds Legislation Amendment Bill 2021 (the Bill) makes important amendments to support the continued growth and management of the Government's investment funds into the future.

The reasons for these amendments are discussed in this submission under the headings of the four schedules contained within the Bill.

Schedule 1 – *Future Fund Act 2006*

The new employment framework

Schedule 1 to the Bill amends the *Future Fund Act 2006* (Future Fund Act) to establish a new employment framework for the FFMA. This reflects that the FFMA is unique compared to other Commonwealth entities in that it operates within international financial markets in a substantially commercial environment.

Key investment management staff are recruited from around the world and staff structures and remuneration arrangements are different to Australian Public Service norms. For example, the FFMA employs staff on individual employment contracts, as opposed to broad-based enterprise agreements. This reflects the diversity of roles within the organisation and the level of competition for particular specialist skills and high-performing staff in the investment industry.

Under the new framework, staff will be employed by the Chair of the Future Fund Board (acting on behalf of the Commonwealth) under the Future Fund Act. This will provide a more flexible employment framework to suit the FFMA's unique operating environment. The terms and conditions of employment will be set by the Chair, who is the Accountable Authority of the FFMA. Staff of the FFMA will continue to be Commonwealth employees.

The new framework will be outside of the *Public Service Act 1999*, similar to other specialised Commonwealth agencies including ASIC¹, APRA² and the RBA³. The FFMA will continue to have internal policies for organisational matters, such as those relating to merit-based hiring, performance management and workplace health and safety.

Safeguarding good governance

While these changes will facilitate employment arrangements that are more suitable for the FFMA, the FFMA will continue to be a non-corporate Commonwealth entity under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act). This means that there

¹ See Part 6 of the *Australian Securities and Investments Commission Act 2001*

² See Part 4 of the *Australian Prudential Regulation Authority Act 1998*

³ See Part VII of the *Reserve Bank Act 1959*

will be no change to the requirement for the Chair of the Future Fund Board, as the Accountable Authority of the FFMA, to comply with the general duties of accountable authorities as set out in sections 15 to 19 of the PGPA Act. These general duties include the duty to govern the FFMA in a way that promotes the proper use and management of public resources for which the authority is responsible, to establish and maintain systems relating to risk and control and to keep the responsible Ministers (the Finance Minister and the Treasurer) informed of the activities of the entity and any subsidiaries of the entity. The obligations to provide information and reports to the responsible Ministers under the enabling legislation for the funds will also continue⁴.

FFMA staff will also remain as officials under the PGPA Act and will continue to be:

- required to comply with the general duties of officials as set out in sections 25 to 29 of the PGPA Act; and
- subject to the civil obligations and criminal sanctions set out in sections 58, 59, 61 and 62 of the Future Fund Act.

In addition, to ensure that the FFMA continues to meet the expectations of the Australian Parliament and the public:

- the Chair will be required to determine and publish a Code of Conduct and Values for the FFMA, that are, as far as practicable, consistent with the APS Code of Conduct and Values;
- the FFMA will remain subject to the Government's policy on the Average Staffing Level cap;
- consistent with the arrangements for all other Commonwealth entities, the FFMA will remain subject to the applicable Government workplace relations policies unless otherwise agreed;
- the remuneration of senior executives and other highly-paid FFMA staff will continue to be published in the Future Fund Annual Report in accordance with the PGPA Act; and
- the delegation of employment powers by the Chair can only be made to officers of the FFMA at a level equivalent to an SES employee.

To provide appropriate safeguards for FFMA staff, they will continue to be employed on the same terms and conditions as those that applied immediately before the transition, and will retain all of their existing leave entitlements and access to existing superannuation arrangements. After the transition, the Chair cannot reduce the benefits of an employee as provided under the minimum standards in the National Employment Standards.

In summary, the new employment framework will better align the FFMA with its operating environment and comparable entities, improve its processes to recruit and retain specialised staff and facilitate its objective to maximise investment outcomes. At the same time, appropriate organisational controls, risk management practices and safeguards will remain in place to ensure continued strong governance.

Schedule 2 – *Freedom of Information Act 1982*

A partial exemption for investment activities

The Bill will amend Schedule 2 of the *Freedom of Information Act 1982* (FOI Act) to provide the Future Fund Board and the FFMA with a partial exemption in respect of their investment

⁴ See, for example, sections 54 and 55 of the *Future Fund Act 2006*

activities. A partial exemption is consistent with the treatment of other entities that deal regularly with commercial information, including NBN Co, Australia Post and Export Finance Australia.

A partial FOI Act exemption will remove risk and uncertainty in assessing FOI applications for investment-related documents, particularly those that contain information that is commercially sensitive or obtained in confidence. The exemption is intended to cover documents including those in relation to:

- past, current or proposed investment strategies for the Australian Government's investment funds;
- the evaluation of potential or current investments and investment managers;
- managing investments or making investment transactions;
- the expected financial performance of specific investments or strategies;
- advice from investment consultants on investment strategies and risks; and
- internal investment-related process and policy documents.

The FOI Act will continue to apply to the Future Fund Board and the FFMA in respect of documents concerning non-investment activities.

The case for a partial exemption

The public release of Future Fund Board and FFMA documents in relation to investment activities could place at risk their ability to pursue and achieve their trading strategies and consequently the returns that could be earned by the investments managed by the Future Fund Board. These entities regularly produce, negotiate and receive documents that include confidential, competitive and commercially sensitive information, which if released to the public could compromise the ability of the entities to implement their investment strategies. For example, the public knowledge of the Future Fund Board's proposed investment strategies, or its intention to buy or sell an investment, could affect the market price and distort financial markets. Given the size of the funds under management (valued at over \$245 billion as at 30 June 2021)⁵, this could have a material fiscal impact on the Government's finances.

The existing exemptions under the FOI Act do not provide sufficient certainty that documents containing highly sensitive commercial and proprietary material that are provided to the Future Fund Board and the FFMA by potential investment managers will not be disclosed.

The Future Fund Board is required by the Future Fund Act to invest through external investment managers. The risk of disclosing highly sensitive commercial and proprietary material has led to investment managers withholding information or reducing their engagement with the Future Fund Board and the FFMA. This presents an investment and governance risk, which can result in reduced information and insights on risks and exposures underlying investments, reduced access to investment opportunities and negative investment outcomes. It could also prejudice investment managers in their dealing with other market participants, which in turn could make the Future Fund Board and the FFMA less attractive clients.

The purpose of the partial FOI exemption is to provide certainty to the Future Fund Board and the FFMA, and their relevant investment managers, that commercially sensitive or in-confidence investment information is automatically excluded from release under the FOI

⁵ See website: <https://www.futurefund.gov.au/investment/investment-performance/portfolio-updates>

Act. This will help to place them on a more even footing with commercial competitors in the highly competitive global institutional investment market.

Transparency through the reporting framework

The Future Fund Board and FFMA have reporting obligations under the PGPA Act and the Future Fund Act, which will continue to apply.

Section 46 of the PGPA Act (supported by sections 80 and 81 of the Future Fund Act) requires the Future Fund Board and the FFMA to jointly prepare and give an annual report to the nominated Minister (the Finance Minister) for tabling in the Parliament⁶. The Future Fund annual reports contain detailed information on investment strategy, investment performance, governance and financial reporting. This and other investment information is published on the Future Fund website. The FFMA is also required to publish its corporate plans under the PGPA framework⁷ and appear at Senate Estimates hearings.

The Future Fund Act has a reporting framework to ensure the responsible Ministers remain appropriately informed of the operations of the Future Fund Board⁸. To this end the responsible Ministers have issued a Statement of Expectations, which requires the Future Fund Board to provide quarterly information on the performance outcomes of the investment funds including information on asset allocation. In response, the Future Fund Board has published a Statement of Intent⁹, stating how it will comply with the responsible Ministers' request. In addition to providing the responsible Ministers with the quarterly reports, the Future Fund Board publishes the reports on its website.

The Future Fund Board and the FFMA also publish a range of relevant information online to assist accountability and transparency. This includes but is not limited to:

- as required by each fund's enabling legislation (see, for example, section 24 of the Future Fund Act), a Statement of Investment Policies¹⁰, outlining strategic investment information for each investment fund managed by the Future Fund Board, including the overall investment strategy, investment managers, asset selection and risk management;
- other investment policies such as its Environmental, Social and Governance Policy¹¹;
- a list of all investment managers;
- a list of the top 100 holdings in listed equities¹²;
- a yearly 'Financial Year in Review'¹³ publication, which outlines investment performance, asset allocation, risk positioning and the investment outlook; and
- a disclosure log of all information released under FOI requests¹⁴.

Together with the continuation of the existing reporting framework, the partial exemption under the FOI Act for documents relating to investment activities will provide an appropriate balance between maximising investment returns and ensuring appropriate transparency.

⁷ See section 35 of the *Public Governance, Performance and Accountability Act 2013*

⁸ See sections 54 and 55 of the *Future Fund Act 2006*

⁹ The Statements of Expectations and Intent are found at: <https://www.futurefund.gov.au/about-us/legislation-and-governance>

¹⁰ See website: <https://www.futurefund.gov.au/investment/how-we-invest/investment-policies>

¹¹ See website: <https://www.futurefund.gov.au/investment/how-we-invest/esg>

¹² See website: <https://www.futurefund.gov.au/investment/how-we-invest>

¹³ See website: <https://www.futurefund.gov.au/about-us/publications>

¹⁴ See website: <https://www.futurefund.gov.au/about-us/access-to-information/freedom-of-information/foi-disclosure-log>

Schedule 3 – *Medical Research Future Fund Act 2015*

The amendments to the *Medical Research Future Fund Act 2015* (MRFF Act) fall into two categories:

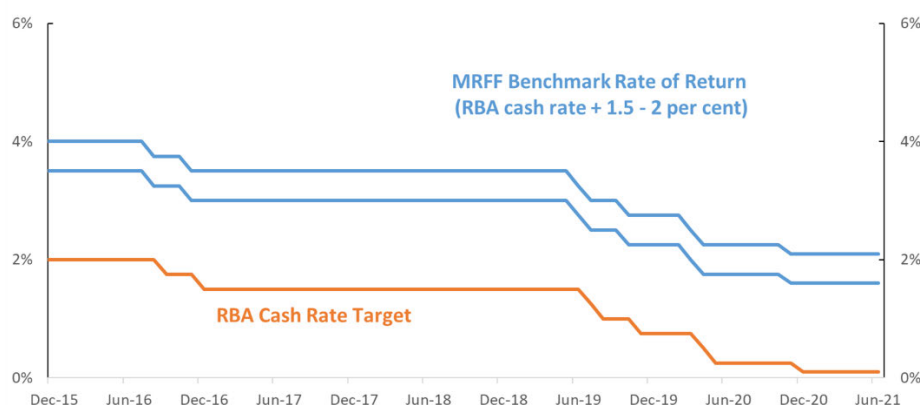
- changes to the disbursements framework; and
- improvements to the operation of MRFF grants programs.

Changes to the disbursements framework

The Australian Government credited \$3.2 billion to the MRFF on 21 July 2020. This brought the total credits to \$20 billion, consistent with the Government's commitment in the 2014-15 Budget when the establishment of the MRFF was announced.

The amount of money available to be disbursed from the MRFF each year for grants programs is currently set by an annual determination from the Future Fund Board. The Future Fund Board calculates the maximum disbursement amount based largely on the benchmark rate of return in the investment mandate, which is linked to the RBA cash rate. In determining the annual disbursement amount, the MRFF Act requires the Future Fund Board to also consider the principles of preserving the nominal credits to the fund (\$20 billion) and moderating volatility in annual disbursements¹⁵. As shown by Chart 1, the RBA cash rate is at a historically low level, having trended lower since the MRFF was established in 2015.

Chart 1: MRFF benchmark rate of return since inception



The recent historic lows in the RBA cash rate has resulted in the most recent maximum annual disbursement determination of \$455 million for 2021-22 being significantly lower than previously estimated. Table 1 shows the maximum disbursement amounts by financial year since the MRFF's establishment. As announced by the Minister for Health on 17 December 2020, the Government is providing a one-off supplementation of \$172.5 million¹⁶ in 2021-22 to maintain the Government's commitments under the MRFF 10-year Investment Plan¹⁷.

¹⁵ See paragraphs 34(4)(a) and 4(b) of the *Medical Research Future Fund Act 2015*

¹⁶ See website: <https://www.health.gov.au/ministers/the-hon-greg-hunt-mp/media/1725-million-funding-top-up-to-support-australian-medical-research>

¹⁷ See website: <https://www.health.gov.au/sites/default/files/documents/2020/01/medical-research-future-fund-mrff-10-year-investment-plan.pdf>

Table 1: Amount available for MRFF grants, as determined by the Future Fund Board

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Amount available for MRFF grants	69	118	155	243	396	579	455
(\$ million)							

The Bill will simplify the disbursements framework and provide increased certainty by specifying a fixed maximum disbursement amount of \$650 million per year from 2022-23. This is expected to avoid the need for unplanned supplementation and provide confidence that the Government will meet its spending commitments in the MRFF 10-year Investment Plan. It will allow approximately 3 per cent of the MRFF's balance to be disbursed in a given year from 2022-23, which reflects an appropriate balance between making meaningful disbursements for medical research and innovation in the short term, and supporting the perpetual funding objective over the long term.

Under the current framework, the Future Fund Board's determination of the maximum disbursement amount relates to a single year, which limits certainty about future commitments. A fixed maximum disbursement will provide greater certainty of funding and assist in the orderly planning and administration of medical research grants programs, as the level of disbursements will be independent from short-term financial market fluctuations.

The responsible Ministers will be required to review the maximum disbursement amount at least every five years and will have the ability to update the amount for future years via a disallowable legislative instrument. This will allow the responsible Ministers to increase the maximum disbursement amount if the MRFF is able to support higher disbursements in the future, while ensuring appropriate parliamentary scrutiny and oversight via the disallowance process, in line with standard parliamentary procedures.

Under the new disbursements framework, the requirement to consider the principle of preserving the nominal credits to the MRFF over the long term will no longer exist. This will allow the Government to issue a new investment mandate for the MRFF with a higher benchmark rate of return. This will increase expected earnings and support the perpetual funding objective.

A new investment mandate with a higher benchmark rate of return would allow the Future Fund Board to match the MRFF portfolio's level of risk with other Australian Government investment funds including the Future Drought Fund and the Emergency Response Fund. This is expected to create operational efficiencies for the Future Fund Board.

Improvements to the operation of MRFF grants programs

The Bill will make states and territories (including state and territory government entities) eligible to receive funding directly from the MRFF Health Special Account. This will make states and territories eligible to apply for competitive MRFF grants rounds and promote competition for MRFF grants.

Allowing states and territories to apply for competitive MRFF grants rounds is consistent with the funding avenue for other entities such as medical research institutes, universities and corporations. This promotes competition for MRFF grants, resulting in grants being awarded directly to the entity best placed to deliver the intended policy outcome.

While the MRFF Act provides a legal avenue for payments to states and territories through the COAG Reform Fund, this avenue has never been used because a payment to a state or territory as a result of an open, competitive grants process is classified as a Commonwealth Own-Purpose Expense (COPE). The current Intergovernmental Agreement on Federal Financial Relations, which governs payments through the COAG Reform Fund, does not provide for COPE payments to a state or territory.

The Bill will change the timeframes for updating the Australian Medical Research and Innovation Strategy from 5 years to 6 years, and the Australian Medical Research and Innovation Priorities from 2 years to 3 years, to better reflect the long-term nature of medical research and medical innovation. The Bill will also align the timing of future updates of the Strategy and Priorities, which will reduce the consultation burden on the medical research and medical innovation sector.

The Bill will clarify that MRFF grants can be paid in instalments to reflect best practice in grants administration. This change will clarify that milestone payments can be paid to grant recipients upon the achievement of agreed milestones, which incentivises recipients to ensure timely progress towards those milestones. The use of instalment payments also allows funds to be retained in the MRFF until they are needed, allowing those funds to remain invested and generate additional returns for the MRFF.

The Bill will clarify that the Health Minister can request debits from the MRFF Special Account without having to identify each individual grant to which a debit relates. Identifying individual grants that relate to each debit is inefficient, given the number of grant recipients and scale of funding that is disbursed from the MRFF each year.

The reporting obligations in Part 5 of the MRFF Act will continue to require the Health Minister to report to the Parliament on the financial assistance provided by the MRFF at the conclusion of each set of Priorities. The requirement to publish information on the internet on grants provided from the MRFF, consistent with requirements under the Commonwealth Grant Rules and Guidelines, remains unchanged.

The Government publishes, and will continue to publish, detailed information on all MRFF grants programs and grant recipients on the Department of Health website, including total funding allocated to each project.

Expenditure from the MRFF will continue to require a formal decision of Government, informed by the Australian Medical Research and Innovation Priorities. In accordance with the MRFF Act, the Health Minister must take into account the Priorities that are in force in making decisions about whether to request the Finance Minister to debit the MRFF Special Account in order to provide financial assistance from the MRFF.

The Bill will also streamline the MRFF's administrative processes by allowing copies of directions to debit the MRFF Special Account (for the purposes of paying grants) to be exchanged between senior departmental officials, in instances where the Finance Minister has delegated the power to make a transfer in accordance with the MRFF Act. This will reduce the administrative burden while still ensuring that Ministers remain suitably informed by their departments, including under section 19 of the PGPA Act.

Schedule 4 – *Emergency Response Fund Act 2019*

Transfer of Function

The amendments to the *Emergency Response Fund Act 2019* (ERF Act) are administrative in nature and reflect Machinery of Government changes. The amendments will implement the transfer of responsibility for expenditure from the Emergency Response Fund (ERF) to the newly established National Recovery and Resilience Agency (NRRA) and will streamline administrative arrangements in relation to transfers from the ERF.

To facilitate the transfer of responsibility for the expenditure from the ERF, the Home Affairs Emergency Response Fund Special Account will be renamed as the Emergency Response Fund Payments Special Account (Payments Special Account), with the Accountable Authority of the NRRA responsible for the Special Account. Information relating to ERF grants and arrangements will be published on the NRRA website rather than the Department of Home Affairs website. The Emergency Management Minister will still be responsible for entering into grants and arrangements and administering funding from the ERF.

Streamlining administrative activities

The remaining administrative amendments to the ERF Act will streamline the grants administration arrangements, making them more consistent with those for the MRFF.

The Bill will strengthen the governance framework by allowing administrative directions in relation to the Emergency Response Fund Special Account (managed by the Secretary of the Department of Finance as the Accountable Authority) and the Payments Special Account (managed by the Coordinator General of NRRA, as the Accountable Authority) to be exchanged between senior departmental officials. This will only occur where the Finance Minister or the Emergency Management Minister have delegated their respective powers under the ERF Act. This will reduce the administrative burden and streamline the process while ensuring that Ministers still remain suitably informed by their departments and the NRRA, including under the provisions of section 19 of the PGPA Act.

The Bill will also allow the Emergency Management Minister to request the Finance Minister to debit the Emergency Response Fund Special Account and credit the COAG Reform Fund for the purpose of making grants to states and territories. This differs from the current arrangements, where the Emergency Management Minister directs the Department of Finance to make the transfer. It is not common practice for a Minister to direct a department outside of their portfolio.

For consistency with the amendments noted earlier in this section, the Bill will allow administrative directions (to debit the Emergency Response Fund Special Account and credit the COAG Reform Fund) to be exchanged between senior departmental officials in instances where the Finance Minister has delegated this power. This will reduce the administrative burden while ensuring that Ministers remain suitably informed by their departments including under section 19 of the PGPA Act.

Conclusion

The Bill makes important amendments to the employment framework for the FFMA to reflect its unique and commercial operating environment within the financial markets while still

ensuring the FFMA remains subject to appropriate controls in line with the Parliament's and the community's expectations.

A partial FOI Act exemption will remove risk and uncertainty in assessing FOI applications for investment-related documents, particularly those that contain information that is commercially sensitive or obtained in confidence.

The new disbursements framework for the MRFF will provide certainty of funding to meet commitments under the Government's 10-year Investment Plan and support significant disbursements over the long term to fund vital medical research and medical innovation projects.

The transfer of responsibility for expenditure from the ERF from the Department of Home Affairs to the newly established NRRRA supports recommendation 3.5 of the Royal Commission into National Natural Disaster Arrangements.

Finally, the administrative improvements to the MRFF and the ERF will streamline the operation of these two investment funds to support the valuable funding streams they provide into the future.