

EXPLANATORY STATEMENT

Issued by authority of the Treasurer and Finance Minister

Future Fund Act 2006

Future Fund Investment Mandate Direction 2024

Section 18 of the *Future Fund Act 2006* (the Act) provides that the responsible Ministers may, by legislative instrument, give the Future Fund Board of Guardians (the Board) written directions about the performance of its investment functions, known collectively as the Future Fund Investment Mandate (Investment Mandate). The Board is subject to the requirements of the Act and the Investment Mandate. Subsection 33(3) of the *Acts Interpretation Act 1901* provides that where an Act confers a power to make, grant or issue any instrument of a legislative or administrative character (including rules, regulations or by-laws), the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend or vary any such instrument.

The Act establishes an Australian Government investment fund – the Future Fund (the Fund) – to strengthen the Commonwealth’s long-term financial position by provisioning for unfunded superannuation liabilities. The Board is responsible for deciding how to invest the Fund and must seek to maximise the return earned on the Fund over the long term, consistent with international best practice for institutional investment.

The purpose of the *Future Fund Investment Mandate Direction 2024* (Instrument) is to reflect current drafting practices and insert a new provision to ensure that the Board has regard to national priorities as part of the Fund’s overarching investment strategy.

The Board was consulted prior to settling the Instrument, in accordance with section 19 of the Act. The Board’s submission, if made, will be tabled in both Houses of Parliament and published on the Federal Register of Legislation.

The Instrument is a legislative instrument for the purposes of the *Legislation Act 2003*.

The Instrument is exempt from the sunseting regime set out in Part 4 of Chapter 3 of the *Legislation Act 2003* as a result of regulations made for the purposes of paragraph 54(2)(b) of that Act. Item 3 of the table under section 11 of the *Legislation (Exemptions and Other Matters) Regulations 2015* provides for class exemptions from sunseting if the instrument is a direction by the Minister to any person or body. The Instrument is a direction from the Treasurer and Finance Minister to the Board and therefore is exempt from sunseting.

As a direction from the responsible Ministers to the Board, the Instrument is also exempt from disallowance under section 42 of the *Legislation Act 2003* as a result of regulations made for the purposes of paragraph 44(2)(b) of that Act. Item 2 of the table under section 9 of the *Legislation (Exemptions and Other Matters) Regulations 2015* provides for class exemptions from disallowance if the instrument is a direction by the Minister to any person or body.

The Instrument commences the later of the 15th day after the Instrument is made or the day after registration.

Details of the Instrument are set out in Attachment A.

The Office of Impact Analysis (OIA) has been consulted (OIA24-08031) and agreed that an Impact Analysis was not required.

ATTACHMENT A

Details of the *Future Fund Investment Mandate Direction 2024*

Part 1 - Preliminary

Section 1 – Name

This section provides that the name of this instrument is the *Future Fund Investment Mandate Direction 2024* (Instrument).

Section 2 – Commencement

The Instrument commences the later of the 15th day after it is made and the day after registration. This is in accordance with subsection 18(8) of the *Future Fund Act 2006* (the Act), which requires a direction take effect no earlier than 15 days after the day on which it is given.

Section 3 – Authority

This Instrument is made under section 18 of the *Future Fund Act 2006*.

Section 4 – Schedules

Section 4 provides that each instrument that is specified in a Schedule to this Instrument will be amended or repealed as set out in the applicable items in the Schedules, and any other item in a Schedule to this Instrument has effect according to its terms.

Section 5 – Objects

The Board is to carry out the investment functions in accordance with the Act and the Investment Mandate. Section 5 sets out the objectives of this Instrument which are to:

- give guidance to the Board about the Fund’s investment strategy;
- set out the Government’s expectations about how the Fund will be managed and invested; and
- set out the Government’s expectations around the Board’s policies on risk and return and the allocation of financial assets of the Fund.

This is consistent with section 18 of the Act.

Section 6 – Definitions

Section 6 sets out definitions to support the operation of the Instrument. Expressions used in this Instrument have the same meaning as in the Act, as in force from time to time, as outlined in paragraph 13(1)(b) of the *Legislation Act 2003*. This ensures consistency between the Instrument and its enabling legislation. The definitions set out in section 6 are:

- *CPI* – CPI means the All Groups Consumer Price Index published by the Australian Statistician. The CPI can be found on the Australian Bureau of Statistics website (<https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation>).

- *economic resilience and security infrastructure* – Economic resilience and security infrastructure focuses on sectors of the economy where having some level of domestic capability is necessary for, or an efficient way to improve, the resilience and security of the economy.
- *energy transition* – covers increasing the overall use of renewable and low emission energy sources; increasing the capacity and efficiency of Australia’s energy infrastructure and decreasing Australia’s overall reliance on high emission energy sources, including by developing and improving technology to achieve that objective. Broadly, the definition is intended to cover Australia’s shift towards an energy mix that has a greater reliance on renewable energy sources. The note to the definition clarifies that the energy transition to net zero carbon emissions by 2050 may also involve the use of medium emission energy sources to decrease Australia’s overall carbon emissions during the transition period.
- *infrastructure* – Infrastructure covers transport, energy, communication and water infrastructure and economic resilience and security infrastructure as described above.
- *net zero transformation* – Australia’s net zero transformation means reducing Australia’s net greenhouse gas emissions to zero by 2050.
- *residential housing* – Residential housing has the same meaning as residential premises as defined by section 195-1 of the *A New Tax System (Goods and Services Tax) Act 1999*. Residential housing includes housing which forms part of a building, such as apartments and townhouses. The definition also includes social and affordable housing.
- *the Act* – refers to the *Future Fund Act 2006*.

Part 2 – Directions

Section 7 – Investments in financial assets only

Section 7 reiterates that the investments of the Fund consist of financial assets, as per Part 3 of the Act.

Section 8 – Maximise return

Section 8 requires the Board, in performing its investment functions, to maximise returns earned on the Fund over the long term, consistent with international best practice for institutional investment. The requirement to maximise returns does not apply to the extent that the Board would be required to act in a way that is inconsistent with the Act and Investment Mandate, including those provisions relating to risk and return. However, the requirement to maximise returns does apply to the extent that it is inconsistent with section 9 of the Investment Mandate (having regard to national priorities).

Section 9 – Board must have regard to national priorities

Section 9 requires the Board to have regard to Australia’s national priorities in undertaking its investment functions as part of its overarching investment strategy. Subsection 9(2) clarifies that this requirement does not apply to the extent that it would require the Board to

act inconsistently with the Act or the Instrument, including those provisions relating to risk and return.

The requirement to maximise returns in section 8 takes precedence over the requirement to have regard to national priorities in section 9.

The national priorities are:

- supporting an energy transition as part of the net zero transformation of the Australian economy;
- increasing the supply of residential housing in Australia; and
- delivering improved infrastructure located in Australia.

These considerations might lead to the Board progressing an investment in a national priority area ahead of another area that presented a similar investment opportunity if it was consistent with the Board's investment strategy, including on matters relating to risk and return for the portfolio. By way of example, in having regard to the national priorities, the Board may consider progressing investments in:

- renewable energy and transmission infrastructure (as part of supporting an energy transition as part of the net zero transformation of the Australian economy);
- property which contributes towards increasing the supply of affordable housing across Australia (as part of increasing the supply of residential housing in Australia); and
- basic facilities and systems serving Australia, such as roads or airports, or energy infrastructure (as part of delivering improved infrastructure located in Australia).

The direction to have regard to national priorities does not require the Board to make investments that are inconsistent with the requirements of the Act and other provisions of the Instrument. Those requirements include the Board's obligation to maximise returns over the long term in a manner consistent with international best practice for institutional investment (consistent with section 18 of the Act), while targeting the long-term benchmark return and taking an acceptable but not excessive level of risk for the portfolio.

In having regard to international best practice for institutional investment when implementing its approach to corporate governance principles, and provided it is consistent with applicable laws and the Instrument, the Board is expected to have regard to the national priorities in performing its investment functions. This includes through the ongoing management of investments, and when determining its approach to its stewardship and voting activity.

Section 10 – Benchmark return

For the purposes of this Instrument, the Government has directed the Board to adopt, as the long-term benchmark for the performance of the Fund, an average return over the long-term of at least the CPI + 4 per cent to + 5 per cent per annum.

Implementing a benchmark rate of return with a range provides the Board with scope to target lower returns when it believes the prospective reward for investment risk is

relatively low, and conversely, higher returns when it believes the prospective reward for investment risk is relatively high.

The Government is conscious of the risks inherent in investing a large portfolio of financial assets and acknowledges that in practice this will involve some short-term volatility in the Fund's returns, including the possibility of losses in some years. In targeting the long-term benchmark, the Board is directed to determine an acceptable but not excessive level of risk for the Fund. This level of risk should be measured in terms such as the probability of losses in a particular year.

Section 55 of the Act requires the Board to keep the responsible Ministers informed of the operations of the Board and give the nominated Minister such information in relation to those operations as is appropriate. This could include information the Board considers to be relevant on any significant changing circumstances of the Fund or broader financial markets.

Section 11 – Limits on holdings in certain companies

The Act sets out a number of legislative restrictions in relation to the investment of the Fund. Sections 21 and 84C of the Act prohibit the Board from triggering the takeover provisions under the *Corporations Act 2001* and restrict the Board from holding a stake of more than 20 per cent in any foreign publicly listed company.

To provide the Government with comfort that these legal restrictions will be met, the Instrument directs that the Board must establish a practical working limit to prevent a breach.

Section 12 – Board must consider impacts of investment strategy

The Government has a broad obligation to the Australian community to make decisions that are economically and fiscally responsible. In establishing the Fund, it is the expectation of the Government that the investments of the Fund should not disrupt the normal operation of domestic financial markets. The Board, in setting the investment strategy and in instructing the investment of the Fund, must act in a manner that minimises the potential of causing any abnormal change in the volatility or efficient operation of Australian financial markets.

The Board is also required to act in a manner that is unlikely to have a negative impact on the Government's reputation in Australian and international financial markets.

The Government participates in a number of international organisations which pursue high standards of conduct in financial markets. The Government recognises that the Board will invest in international capital markets as part of a sound investment strategy involving diversification. In doing so, the Government expects that the Board will act in a manner that is unlikely to cause reputational damage to Australia.

Section 13 – Corporate governance

In undertaking its investment functions, the Board must act consistently with, and establish policies on matters relevant to, international best practice for institutional investment. In

particular, the Government expects the Board's policies to include its approach to corporate governance principles, including the voting policy for investments of the Fund.

Schedule 1 – Repeals

Schedule 1 of the Instrument repeals the previous Investment Mandate, the *Future Fund Investment Mandate Direction 2017*. The Instrument remakes the Investment Mandate to reflect current drafting practices and to provide updated directions on national priorities.