Prudential Practice Guide

SPG 510 – Governance

July 2013
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Prudential Practice Guides (PPGs) provide guidance on APRA’s view of sound practice in particular areas. PPGs frequently discuss legal requirements from legislation, regulations or APRA’s prudential standards, but do not themselves create enforceable requirements.

*Prudential Standard SPS 510 Governance* (SPS 510) sets out APRA’s requirements in relation to the governance of an RSE licensee. This PPG aims to assist an RSE licensee in complying with those requirements and, more generally, to outline prudent practices in relation to certain governance matters.

For the purposes of this guide, and consistent with the application of SPS 510, ‘RSE licensee’ has the same meaning given in the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

Subject to the requirements of SPS 510, an RSE licensee has the flexibility to structure its governance framework in the way most suited to achieving its business objectives. Not all practices outlined in this PPG will be relevant for every RSE licensee and some aspects may vary depending upon the size, business mix and complexity of the RSE licensee’s business operations.
Principles

1. A number of principles underpin a sound and effective governance framework for an RSE licensee. These include:

   (a) responsibility — the board of directors (the Board) is ultimately responsible and accountable for the decisions and actions taken by an RSE licensee;

   (b) independence — demonstrated by a Board that discharges its review and oversight role effectively and independent of the interests of dominant shareholders, management, and competing or conflicting business interests;

   (c) renewal — a policy of renewal provides for fresh insight and general reinvigoration of the Board while also ensuring ongoing understanding of the business of the RSE licensee;

   (d) expertise — demonstrated by a Board with the necessary expertise to fulfil its role and functions, and access to independent expertise not readily available amongst the current directors;

   (e) diligence — demonstrated by a Board that discharges its duties and responsibilities carefully and conscientiously;

   (f) prudence — demonstrated by a Board with a clear focus on the prudent management of the RSE licensee’s business operations;

   (g) transparency — demonstrated by a Board that is open and honest in its dealings on behalf of the RSE licensee; and

   (h) oversight — demonstrated by a Board that is able to satisfy itself that the management and operation of the RSE licensee’s business operations conforms with its strategy, direction and policies.

The Board and senior management

2. As stated in SPS 510, the Board has ultimate responsibility for the sound and prudent management of an RSE licensee’s business operations. A well-functioning Board will review and approve business strategies and significant policies of the RSE licensee. It will also satisfy itself that an effective system of risk management and internal control is established and maintained, and that senior management monitors the effectiveness of the risk management framework.

3. Senior management has responsibility for day-to-day management of the RSE licensee’s business operations. This includes the implementation and monitoring of structures, processes, information and oversight arrangements used in managing the RSE licensee.

Residency

4. As a guide, a person might be considered ‘ordinarily resident’, as referred to in SPS 510, if they are likely to be in Australia for a majority of days in any 12-month period.

Composition of the Board

5. Section 10(1) of the SIS Act contains a definition of ‘independent director’, a term that is used in Part 9 of the SIS Act, which deals with equal representation of employers and members in relation to standard employer-sponsored funds. APRA’s view is that a prudent equal representation Board would consider the benefits of the appointment of at least one independent director.

6. A non-equal representation Board might similarly consider the benefits of the appointment of at least one director who is free from any business or other association that could materially interfere with the exercise of their independent judgement.

7. For the purposes of this PPG, a director who is free from these other associations is referred to as ‘a non-affiliated director’.
8. Further, APRA’s view is that a prudent RSE licensee would consider whether the appointment of an independent or non-affiliated director, as relevant, as chairperson of the Board would benefit the Board’s fulfilment of its duties.

9. When assessing whether a director is a non-affiliated director, the Board may have regard to whether the director:

   (a) is a substantial shareholder of the RSE licensee or an officer of, or otherwise associated directly with, a substantial shareholder of the RSE licensee;

   (b) is employed, or has previously been employed, in an executive capacity by the RSE licensee, another group member or a standard employer sponsor and there has not been a period of at least three years between ceasing such employment and serving on the Board;

   (c) has within the last three years been a director of a standard employer sponsor, a principal of a material professional adviser or a material consultant to the RSE licensee or another group member, or an employee materially associated with the service provided;

   (d) is a material supplier of the RSE licensee’s business operations or another group member, or an officer of or otherwise associated directly or indirectly with a material supplier;

   (e) has a material contractual relationship with the RSE licensee or another group member other than as a director;

   (f) is eligible to be a member representative or employer representative on the Board; or

   (g) has served as a member representative or employer representative at any time in the last three years.

10. It would be prudent practice for an RSE licensee to consider the current and past associations of candidates when seeking to appoint new directors. Where a current or past association could impact a director’s ability to effectively carry out their role, APRA expects that the Board would consider whether that appointment is appropriate and in the best interest of members.

11. APRA’s view is that membership of an RSE within the RSE licensee’s business operations does not preclude a director from being considered to be non-affiliated.

12. APRA considers it prudent practice for a Board to also closely consider whether it would be appropriate to include independent and/or non-affiliated directors, as relevant, within the membership of its Board Remuneration Committee and Board Audit Committee.

RSE licensees that are part of a corporate group

13. Where an RSE licensee is part of a corporate group, APRA expects that the Board would consider the potential impact on the RSE licensee of the operations, including but not limited to the policies and procedures, of other entities in the group. If the RSE licensee is the head of the group, APRA expects the Board would consider the impact of the operations of member entities of the group on all RSE licensees within the group.

14. A person may act as a director on more than one APRA-regulated entity within a corporate group. Where an RSE licensee is part of a corporate group, a person who is a director of the RSE licensee and is also an independent director elsewhere in the group, within the meaning given in Prudential Standard CPS 510 Governance, would not ordinarily be considered a non-affiliated director of the RSE licensee.

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1 Refer to s. 12 of the SIS Act for the definition of ‘associate’.
2 Refer to s. 10(1) of the SIS Act for the meaning of ‘member representative’ and ‘employer representative’.
Board committees

15. A well-functioning Board will typically consider whether there may be merit in establishing board committees for the purpose of overseeing critical functions. While SPS 510 requires only the establishment of a Board Remuneration Committee and a Board Audit Committee, the Board may find the establishment of other committees beneficial for certain functions and for strengthening the overall governance arrangements of the RSE licensee.

16. While some functions and responsibilities of directors may be delegated to board committees, as appropriate, the Board retains ultimate responsibility for ensuring that those duties are performed.

17. In establishing committees, a well-functioning Board will have regard to the risk profile of the RSE licensee and the complexity of its business, as well as the experience and expertise of the directors.

18. Where board committees are established, it would be prudent practice for these committees to have clearly defined charters that set out their role and objectives, responsibilities, authorities and tenure, and that the charters of these committees be regularly reviewed. It would also be prudent practice that board committees report regularly to the Board.

Board Audit Committee

19. APRA expects that, in addition to the requirements in SPS 510, the Board Audit Committee would, from time to time, meet separately with the internal auditor and RSE auditor without other parties being present.

Board Risk Committee

20. APRA does not require an RSE licensee to establish a dedicated Board Risk Committee. However, APRA expects that the Board would have considered the necessity of such a committee and the suitability of arrangements for dealing with risk issues at the Board level. Typically, larger and more complex RSE licensees would have a separate Board Risk Committee.

21. A Board Risk Committee would be responsible for reviewing the risk management framework of the RSE licensee, for determining policies that ensure the risk management framework is adhered to and for monitoring adherence to those policies.

22. It would be prudent practice for the Board Risk Committee to allow those responsible for risk management functions to meet with it, without other parties being present.

Internal audit

23. While SPS 510 requires the internal audit function to have a reporting line and unfettered access to the Board Audit Committee, this does not preclude the internal auditor from having a reporting line to management, provided that this does not undermine the independence of the internal audit function, either in appearance or in fact.

Board performance assessment

24. SPS 510 requires the Board to assess its performance and that of individual directors relative to its objectives. In undertaking this assessment, a well-functioning Board would typically consider and document the objectives that it sets for the Board collectively and for individual directors.
25. Objectives for the Board could include:

(a) establishing the overall strategy for the RSE licensee and ensuring reporting against this strategy;
(b) assessing operating and financial conditions against forecasts;
(c) assessing senior management performance against agreed criteria, which would include, for relevant senior management, the effectiveness of risk controls; and
(d) making key decisions in a timely manner.

26. Objectives for individual directors may include:

(a) demonstrating the required expertise for their role;
(b) attendance and participation at Board meetings; and
(c) contributing to Board deliberations and the overall direction of the RSE licensee.

27. APRA expects the Board to consider whether its annual Board assessment would be best undertaken by a party who is free from connection to the RSE licensee or its associates. At a minimum, APRA expects the Board assessment would be undertaken by an external party at least every three years.

28. APRA expects that a Board would have in place a documented policy on Board performance assessments which includes:

(a) the timeframe within which assessments will be conducted;
(b) how sufficient independence in performance assessments will be achieved;
(c) how the Board will manage the outcomes of performance assessments and recommended courses of action in the event of performance that is below expectations; and
(d) a reasonable timeframe for action after performance assessments have been conducted.

Board renewal

29. It would be prudent practice for a Board’s renewal policy to document the maximum tenure period for all directors, including the circumstances where the RSE licensee may step outside the terms of its tenure policy. APRA expects that an RSE licensee would develop and implement a considered approach for assessing each director on the cessation of their term, and at the end of the RSE licensee’s maximum tenure period, to determine whether it is appropriate for the individual to be reappointed. APRA expects that the circumstances where a person is reappointed at the end of a reasonable total period of tenure would be exceptional.

30. The process for nominating directors would be expected to ensure that terms of tenure are staggered to support continuity and the appropriate transfer of knowledge and skills to new directors.

Board renewal and equal representation requirements

31. APRA considers that it is important that formal procedures are in place to support the nomination and appointment of member and employer representatives in an equal representation environment. This includes ensuring that all eligible potential representatives can submit nominations and that the duties, requirements and expected skills and experience of a director are clearly communicated to potential representatives. In circumstances where nominating bodies select directors for appointment, it is prudent practice for the RSE licensee to communicate to the nominating body the manner in which its nomination process can support the board renewal policy.
32. Member and employer representatives are subject to the requirements of SPS 510 as well as those contained in Prudential Standard SPS 520 Fit and Proper (SPS 520). APRA expects an RSE licensee would carefully consider the requirements of both SPS 510 and SPS 520 when appointing new directors noting that the equal representation requirements do not, in APRA's view, absolve an RSE licensee from the obligation to determine whether an individual is appropriate to act as a trustee or director of a corporate trustee.