



17 March 2023

General Manager, Policy
Australian Prudential Regulation Authority

Email: [REDACTED]

Dear Sir/Madam

Consultation: Proposed Updated Prudential Practice Guide SPG 530 Investment Governance

The Actuaries Institute ('the Institute') welcomes the opportunity to comment on the proposed update to Prudential Practice Guide SPG 530 Investment Governance released on 17 November 2022 that will introduce new and additional guidance on the new requirements in Prudential Standard SPS 530 and APRA's expectations of how RSE licensees will consider environmental, social and governance (ESG) risk factors as part of their overall investment risk management.

The Institute is the peak professional body for actuaries in Australia. With expertise in managing risks that are complex and long-term, our members have significant involvement in supporting RSE licensees to continue to meet their obligations to prudently select, manage and monitor investments.

The draft SPG 530 provides further clarity in APRA's investment governance guidance, however there are specific areas where we recommend additional guidance, as set out in the remaining sections of this submission.

Importantly, we support APRA's decision to produce an integrated version of the draft SPG 530 as it improves readability and makes clear the linkages with SPS 530. We recommend APRA continue to consider this integrated approach for future updates to Prudential Practice Guides.

1 Enhancements to SPG 530

In the context of APRA's consultation on the proposed enhancements to Prudential Standard SPS 530 Investment Governance, the [Institute's submission](#) proposed the following recommendations to SPG 530, which we still recommend to be included.

- Provide examples of adverse stress scenarios, particularly following the COVID-19 early release of super program, which was unlikely to have been identified as a hypothetical event by RSE licensees.
- Consider examples of cohort based scenarios, for example in a period of heightened investment switching activity consider the outcomes of transacting members versus non-transacting members.

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- Stress testing should be framed in terms of member outcomes. For example, members close to retirement are expected to be more adversely impacted by poor investment performance.
- Under the valuation governance framework, set out the responsibilities that should remain with the Board, for example devising valuation processes.
- Particularly for unlisted assets, RSE licensees should consider reasonable alternative valuation assumptions and how they may lead to different valuation outcomes.
- With respect to paragraph 40(e) of draft SPS 530, RSE licensees should consider whether prevailing market conditions have led to a spike in investment switching activity, and whether an interim valuation is necessary to protect member equity.
- Guidance on investment monitoring should be extended to consideration of the quality of the overall investment strategy in delivering member outcomes. This includes assessing investment return outcomes on an after-tax and after-fees basis.

On the last point we recommend further specific guidance be provided under draft SPG 530 paragraph 70 on specific criteria required to ensure effective monitoring of investment performance.

2 Liquidity at RSE Level

The liquidity management plan, described in SPS 530, focuses on liquidity management at an investment option level. For example, liquidity stress scenarios are to assess liquidity of the investment options. Draft SPG 530 notes an expectation that a RSE licensee would consider the characteristics of the RSE and the liquidity demands on the RSE.

We recommend SPG 530 goes further, by setting an expectation that a RSE licensee will establish their liquidity risk tolerance on aggregated assets at the RSE level.

3 Time Horizon of Stress Scenarios

When a stress event occurs, it can take time to recover back to a neutral position. It should not be assumed that the full impact to investment options and the RSE are felt immediately. The current in force SPG 530 (paragraph 148) dated November 2013 refers to adverse stress scenarios over a defined time horizon, which is no longer included within this draft SPG 530. We recommend the final SPG 530 sets an expectation on RSE licensees to produce stress testing outcomes that consider impacts over time, particularly to member outcomes in different cohorts. It would be valuable to include the stress testing outcomes as part of the business performance review of each RSE.

4 Stakeholder Engagement when Reviewing the Investment Strategy

A RSE licensee will have a number of other stakeholders with an interest in the process of reviewing the investment strategy. A specific example is the case of a RSE licensee of a defined



benefit plan, where changes to the investment strategy relating to defined benefit assets can affect:

- The advice provided by the RSE Actuary; and
- The funding required by the Employer Sponsor.

We recommend further guidance in final SPG 530 that extends the criteria in the review of the investment strategy to recognise stakeholder considerations.

5 Integrating ESG Risk Considerations is Challenging

The Institute recognises the importance for RSE licensees to have ESG risk considerations integrated into investment governance and supports the additional guidance on ESG factors. However, integrating ESG risk considerations will be challenging for RSE licensees.

- For listed assets where ESG risk considerations can be integrated using available data providers (for example, Sustainalytics, ISS, and MSCI) this is data intensive as it has to be performed at a stock level not an asset class level. There are also inconsistencies (some due to subjectivity) and gaps between data providers. This a complex and fast-changing area, in terms of availability of data, and of acceptable and best practice by investment managers. For example, for energy transition, there are anomalies, such as increased carbon emissions in the near term, to enable lower carbon emissions in the long term. This makes aggregation of data across portfolios hard, as risks can be stock specific and/or open to misinterpretation.
- For unlisted assets, in many cases, there may be a lack of useful or meaningful quantitative data on ESG risk factors. This means RSE licensees may need to rely solely on qualitative assessments in some cases.

We expect RSE licensees will need time to mature their ESG risk processes and given the long term and complex nature of ESG risk we recommend RSE licensees obtain the support of appropriate expertise.

6 Remuneration and Reward

We recommend the final SPG 530 provide more emphasis on the importance of the remuneration and reward structure as it relates to investment governance. Examples of remuneration and reward considerations under an investment governance framework include:

- Ensure that remuneration and reward of key internal investment personnel are closely linked to member outcomes.
- Assess an external manager's remuneration structure as part of the manager rating/selection process.

Currently, the draft SPG 530 only refers to the appropriate remuneration to attract and retain appropriately skilled investment staff. We recommend a cross-reference to Prudential



Standard CPS 511 will provide appropriate emphasis on remuneration and reward considerations.

Further information

We would be pleased to discuss this submission or to provide further information. If you would like to do so, please contact [REDACTED] of the Actuaries Institute, on [REDACTED]

Yours sincerely

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President