AIST

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Dear Sir/Madam

Strategic planning and member outcomes: Proposed enhancements

Brief

AIST supports the proposed updates to the Member Outcomes framework, and request clarity and guidance around the types of cohort enhancements APRA seeks in order to be meaningful and fit for purpose. We also note that the timing and availability of data that feeds into business performance assessments remains challenging.

About AIST

Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public sector superannuation funds. As the principal advocate and peak representative body for the $1.7 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research. AIST advocates for financial wellbeing in retirement for all Australians regardless of gender, culture, education, or socio-economic background. Through leadership and excellence, AIST supports profit-to-member funds to achieve member-first outcomes and fairness across the retirement system.

Submission

AIST thanks APRA for the opportunity to provide input to this consultation.

Funds are generally very positive about the implementation of SPS 515. Mandating strategic objectives that support the achievement of member outcomes has improved business planning and structured processes. Enhancements to the existing regime are broadly welcomed.

The annual assessment requirement to demonstrate whether the "financial interests of beneficiaries of the fund are being promoted" could potentially be made stronger and more explicit through linkage to the Best Financial Interests duty.

Clearly defining outcomes for members

The discussion paper states that APRA seeks more granular and measurable cohort analysis to reduce the risk of pockets of poor performance or outcomes being masked. Cohorting is also a feature of the Design and Distribution Obligations (DDO) and Retirement Income Covenant (RIC), both of which have been introduced since the Member Outcomes regime was introduced. There may be some alignments and efficiencies to be found where the requirements overlap but it is noted that for cohorting to me meaningful, it needs to be tailored to the purpose at hand.

AIST member funds primarily offer default MySuper products that are designed to accommodate large and diverse populations of members and require a single uniform approach under the MySuper regime. Their approaches to cohorting differ according to whether the MySuper product is a lifecycle strategy or single strategy product.

Many funds currently take a "whole of fund" approach to cohorting, noting the characteristics that broadly reflect the whole of their membership. These membership characteristics differ between funds and inform funds' strategic objectives, but cohorts are not commonly sub-segmented within the fund, or if they are, not beyond the MySuper/Choice/pension product level.

There are challenges in developing meaningful sub-cohorts within single-strategy MySuper products as any changes to the product aimed at improving outcomes for one particular group of MySuper members may also impact the rest of the MySuper product membership. The available data for benchmarking of performance, fees and costs is also limited to whole-of-product comparisons. The emphasis should be placed on monitoring specific detrimental outcomes within a product or investment option rather than developing specific cohorts.

The granularity of the data available to funds about their members is generally restricted to high-level demographic information such as age, gender, geographic location, balance, insurance status and whether the account is active or inactive. While insurance status is a contributor to different outcomes, the entitlement to default insurance is a direct function of age, balance and activity so this metric is of limited utility for the purpose of defining cohorts.

Some information about working patterns, income and occupational industry may be broadly deduced from representative industry, contributing employer data and occupational insurance rating but this is not guaranteed to be accurate and does not expose specific roles within known businesses. It is also noted that disruptions to the traditional funnel of industry-linked membership, such as stapling, and mergers of funds with significantly different industry representations will change fund demographics moving forward.

Due to their default nature, the uptake of "choice" options in these funds is demonstrably low and typically undertaken by more highly engaged members seeking outcomes that align with their specific needs and objectives. Funds don't have access to data on other factors that influence retirement adequacy such as other super accounts, home ownership, relationship status and spousal financial position, debt position, other income sources or assets and savings outside of their balance. This makes it difficult to assess whether the outcomes delivered by these products are in line with those being sought from members, or to make interventions about retirement adequacy without straying into advice territory.

Similar challenges arise in the development of cohorts for post-retirement product development. There is little external information available at the individual member level that would permit meaningful cohorting for the development of the Retirement Strategy. Targeting of retirement products and measurement of outcomes in the retirement space remains problematic.

- **Guidance is required with concrete and realistic examples of the sort of cohort identification and implementation that is being sought by APRA from the proposed amendments.**

Soundly run business

Management of financial resources on a business-as-usual basis

AIST funds report that they already undertake stress testing and scenario analysis as a matter of good business practice, even though this is not an existing APRA requirement. The proposal to adopt this approach will not have a significant impact on existing processes nor create an undue regulatory burden.

It is noted, however, that it is difficult to align long-term (30+ years) outcomes targets with short term financial decision making and mid-term strategic planning. Business plans are required to reflect strategic plans over 3-5 year periods and be reviewed and updated annually to make improvements to business operations. It is challenging to guarantee that daily/annual expenditure management decisions necessarily lead to long term outcomes. This short- and mid-term planning does not seem to be strongly recognised in the framework.

Financial resources to manage and respond to operational risk

AIST eagerly awaits APRA's response to its review on *Strengthening financial resilience in superannuation* and welcomes APRA's consideration of amendments to the prudential framework to create greater flexibility in responding to operational risk events that cause negative outcomes for members.

As stated in our submission to the above-named consultation, the prescribed amount, purpose and allowable uses of the Operational Risk Financial Requirement (ORFR) should be reviewed. Under current settings, the quantum of capital can act as a drag on investment returns and the reserve is quarantined from the ability to make proactive risk management uplifts that would also contribute to strengthening member outcomes.

AIST looks forward to participating in the upcoming *Prudential Standard SPS 114 Operational Risk Financial Requirement* consultation process.

Board oversight of projections

AIST agrees with APRA that assumptions used to conduct projections should be robust, evidence-based, and subject to board approval.

However, the framing of this in the discussion paper puts the onus and responsibility for business activities on the Board rather than delegated management or other specialists when the role of the board should be oversight of the sound and prudent management of the business. This framing has come through in several consultations, most recently *CPS 230 Operational Risk Management*.

Senior management of funds routinely present multiple projection scenarios underpinned by clear assumptions to the board in the annual budget planning process, with opportunity to question those assumptions. They further undertake tactical scenario analysis to inform routine business decisions during the financial year, with those decisions made visible to the board via its specialist committees. The board is not actively involved in setting or assessing the assumptions used for routine business decisions or annual projections, nor should its remit be expanded to set such assumptions.

APRA's concern that "assumptions underpinning RSE licensee analysis are often unsubstantiated or inconsistent with historical trends, and are not routinely subject to robust stress-testing." would appear to be more about the robustness of the board approval process and the endorsement of inadequately supported assumptions than where the responsibility for prudently assessing what those assumptions should be. It should not be addressed by tasking the board with developing the methodologies by which the projections are to be set.

Any role beyond oversight should remain with delegated and suitably qualified specialists such as actuaries, risk and investment professionals, board committees and senior management as relevant.

- **APRA should not use updates to its prudential framework to task boards with additional roles and responsibilities beyond oversight as a mechanism to improve board governance.**

Assessment of performance

The performance assessment cycle

APRA has an expectation that funds will have regard to the annual performance test and heatmaps when preparing their annual outcomes assessments. As these resources are reliant on data reported to APRA under the data collection requirements, it follows that funds are also heavily reliant on APRA's statistical publications to interpret the underlying information and align the data and calculation processes to those required for the assessment regime. Inconsistency in the way that fee metrics are considered in each regime is one area of confusion and inefficiency.

The timing of APRA's releases is another challenge. The performance test is released in August while the annual APRA statistical publications and heatmaps are released in mid-December, leading into a time of year when there is a concentration of public holidays and annual leave.

Funds seeking to complete their annual assessments before the end of the calendar year have a limited window in which to make use of the data. Board strategy planning cycles that commence ahead of December must rely on independent rating agency data that risks being incomplete.

Boards rarely meet between early December and early February for completed assessments to be digested and appropriate sign-offs obtained.

Suggestions to address such bottlenecks include bringing forward APRA's publication dates, recognising that all APRA-regulated funds are reliant on the data for appropriate benchmarking at a difficult time of the year, and, rather than APRA publishing individual timed releases, developing a database (similar to those provided by Chantwest and SuperRatings under subscription models) that houses a single data source to facilitate consistent benchmarking and comparison between funds.

It is also noted that the requirements for provision of information to members have evolved since the Member Outcomes Assessment (MOA) was first required to be published on member websites. Funds are now required to publish Target Market Determinations, Retirement Income Strategy statements and Annual Member Meeting Notices (AMMN) in addition to Product Dashboards, Product Disclosure Statements and Annual Reports. There is an expectation that all of these will be presented in a manner and format that is accessible and digestible to members, yet these have all been introduced in isolation and without regard to each other.

A MOA published in February or March is already eight months out of date at the point of publication as it is based on data for the prior financial year. It is required to be provided with the AMMN which is likely to be provided to members in August or September at the earliest, so is over a full year out of date at the point of distribution. The utility of its provision at this point is questionable. AIST funds are keen to find ways of communicating with members that are more meaningful than just meeting a disclosure compliance requirement, which may mean some form of rationalisation of overlapping requirements and/or centralisation of member-focused information.

Merging of the Business Performance Review as a standalone requirement in SPS 515 into the annual Business Plan as monitoring considerations should also be considered.

- **Align calculation processes between the performance test, heatmap methodology and member outcomes assessment methodology to enable easier benchmarking and limit confusion**
- **Bring forward APRA's publication dates for annual statistical publications**
- **Develop a database accessible by APRA-regulated entities to facilitate consistent benchmarking and comparison between funds.**
- **Review the timing and value of the Member Outcomes Assessment to consumers, in line with other disclosure requirements**
- **Merge the Business Performance Review into the annual Business Plan.**

Benchmarks & Data

APRA's guidance supporting the SPS 515 prudential standard recognises that there are challenges in developing benchmarks for outcomes related to insurance, due to the unique nature of many products. As insurance is an integral feature of the superannuation system that can have a significant impact on member outcomes, AIST has long supported the inclusion of insurance metrics in mandatory SuperStream reporting data, APRA data collection and product comparisons including the Your Super tool.

Access to such information would permit funds to more easily analyse insurance outcomes within their fund to influence product design and to benchmark their offerings against their peers without seeking costly third-party analysis of individual funds' insurance disclosures.

- **Include insurance metrics in mandatory data collection and make this information available to funds and members**

For further information regarding our submission, please contact [redacted], Senior Manager, Advocacy & Research via email at [redacted]

Yours sincerely,

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