

APRA SPS515 Strategic Planning and Member Outcomes: Proposed Enhancements

Industry Super Australia (ISA) is a collective body for funds that carry the Industry SuperFund symbol. ISA manages research, advocacy, and collective projects on behalf of those funds and their five million members. Our aim is to maximise the retirement savings of all our members.

ISA welcomes the opportunity to comment on APRA's review of Prudential Standard SPS 515 Strategic Planning and Member Outcomes (SPS 515) and associated guidance. ISA has not responded to the specific questions posed in the discussion paper as we consider these to be more operational in nature and as such, our funds are best placed to respond to these issues. However, we have provided some more general comments below on specific elements of SPS 515 and the proposed enhancements.

In particular, we note that funds have limited access to detailed member data for the purposes of determining outcomes for cohorts of members. We have also considered the broader context of whether the best interest duty, and other recent legislative reforms, create a more comprehensive and complex regulatory framework, such that the role of SPS 515 within that framework requires review.

Following on from this analysis, ISA has made the following recommendations:

- ▶ ISA recommends that the government share with funds de-identified data held by government agencies on the relevant characteristics of members of the fund.
- ▶ ISA recommends that APRA consider enhancements to SPS 515 that ensure consistency with the requirements of the best financial interest duty.
- ▶ ISA recommends that APRA review its bottom-up approach to regulatory guidance in relation to the member outcomes covenant to ensure that parallel processes undertaken by funds to comply with SPS 515 (and supporting guidance) and the broader regulatory framework, are not duplicated.

Clearly defining outcomes for members

ISA supports APRA's proposed enhancements to the principles-based approach to setting cohorts outlined in the discussion paper. ISA accepts that cohort analysis can be a useful tool for RSE licensees to achieve a deeper understanding of their membership base to support effective strategic planning and delivery of outcomes to members. As noted in APRA's letter to all licensees: Member Outcomes and

Design and Distribution Obligations published 15 December 2020, “the quality of the BPR [Business Performance Reviews] and the Outcomes Assessments will hinge on an RSE licensee’s ability to access granular and accurate data, as well as how the licensee uses that data to improve its performance over time.”

However, if, as stated in the discussion paper, APRA expects RSE licensees to undertake analysis that relies on information beyond “simplistic cohorts that only reflect age, product and investment option”, such information must be easily and efficiently accessible to RSE licensees.

In fact, the feedback that we have received from funds is that they do not generally have access to a depth of information about members beyond their age, gender, address and super balance. Member surveys require significant cost to administer (which is passed on to members) and have yielded limited success due to a lack of engagement from members, and publicly available data is, understandably given privacy laws, limited.

Conversely, the Australian Tax Office and the Department of Social Services hold relevant data that would assist funds to identify the characteristics of cohorts of members. While privacy laws may prevent personal information about individual members being provided to funds, de-identified information would still be of assistance.

Recommendation 1: ISA recommends that the government share with funds de-identified data held by government agencies on the relevant characteristics of members of the fund.

This will assist funds to divide their members into appropriate cohorts for the purposes of clearly defining and delivering outcomes for members in accordance with SPS 515. It will also drive efficiencies for other complementary elements of the regulatory framework such as the retirement income covenant and the design and distribution obligations, both of which require funds to break down their membership data into segments, for example cohorts or target markets.

Expenditure management

The current framework for expenditure management set out in SPS 515 and supporting guidance largely (albeit, as noted below, not precisely) replicates the requirements of the best financial interests duty (BFID). SPS 515 requires that all expenditure and investment decisions by RSE licenses must be in the best interests of members and subject to appropriate record-keeping, monitoring, review and oversight. We note that a key policy intent of both SPS 515 and the BFID is to improve members’ financial outcomes.¹

The discussion paper notes that APRA will consider insights received from the current Your Future Your Super review (YFYS review) and the findings from its October 2021 expenditure thematic review to inform potential enhancements to the prudential framework to be consulted on in 2023.

¹ Explanatory Memorandum to the Treasury Laws Amendment (Your Future, Your Super) Bill 2021, 36

ISA will provide comments on these proposed enhancements at that time, however we wish to raise the following matters which we consider APRA should take into account when considering any potential enhancements.

Scope of the Thematic Review

The expenditure examined as part of the thematic review was subject to the best interest duty, rather than the BFID, and therefore, as stated in the Information Paper: Findings from APRA's superannuation thematic reviews October 2021 (information paper), the review did not examine whether and to what extent industry practices may have changed to accommodate the new obligation.

The thematic review also appeared to be unduly focused on marketing and sponsorship expenditure which the Explanatory Memorandum to the Treasury Laws Amendment (Your Future, Your Super) Bill 2021 (the Bill) regards as 'discretionary or non-essential'. SPS 515 and the BFID apply to all expenditure decisions, whether discretionary or essential, significant or otherwise.

As a result, the thematic review may be of limited assistance in informing potential enhancements to the prudential framework and, as recognised in the information paper, it needs to be considered in conjunction with the YFYS review. We make further comments regarding the YFYS review in the next section.

Best financial interest duty

SPS 515 currently requires an RSE licensee to ensure its expenditure decisions are for the purposes of the sound and prudent management of its business operations and consistent with the best interests of beneficiaries. This is inconsistent with the terms of the BFID as set out at s52(2)(c) of the SIS Act.

Similarly, SPS 515 distinguishes between 'significant' and other expenditure, with significance determined by the size of the expenditure or whether it is extraordinary in nature. Conversely, the Explanatory Memorandum to the Bill distinguishes between expenditure that is 'essential' to the prudent operation of a superannuation entity and 'discretionary or non-essential' expenditure, and contemplates different standards for determining whether the expenditure is in members' best financial interests.

ISA has concerns, described below, about the approach taken in the Explanatory Memorandum, however we wish to highlight here that, for clarity and to avoid undue regulatory burden, APRA should ensure alignment between SPS 515 and the requirements under the BFID, in considering enhancements to SPS 515 in relation to expenditure.

Recommendation 2: ISA recommends that APRA consider enhancements to SPS 515 that ensure consistency with the requirements of the best financial interest duty.

ISA provided a detailed submission to the YFYS review which incorporated our analysis and recommendations in respect of the best financial interest duty. In summary, ISA's submission on the best financial interests duty covered the following issues:

Higher costs of compliance

A stated policy objective of the BFID was to deliver financial benefits to members. However, the reverse onus and the lack of materiality threshold, in addition to the absence of meaningful guidance on record-keeping, has resulted in increased expenditure by funds on internal and external activities to support compliance with the obligation – the benefits of which are often not clear. These costs are ultimately borne by members.

Misdirected Focus

ISA has concerns that the focus of the law in relation to the BFID is misdirected in that:

1. The law does not scrutinise or hold trustees to the same standard to justify the setting of fees above cost recovery and payment of profits (ultimately extracted from member assets) to related parties which are then reflected in dividends to shareholders, despite the clear detriment to members' financial outcomes;
2. As described above, the Explanatory Memorandum to the Bill also distinguishes between 'essential' and 'discretionary' expenditure and requires a significantly greater level of scrutiny for discretionary expenditure, notwithstanding that essential expenditure captures some high-expense items that have a greater potential effect on member outcomes (for example, investment management and administration expenses, which are often made to related parties among retail funds); and
3. BFID measures do not focus on some key expenditures made by corporate trustees that are unlikely to be in the best financial interests of members, such as related party arrangements whereby fees and profit are directed out of member assets by related party service providers.²

APRA should have regard to ISA's submission when considering any potential enhancements to the prudential framework for 2023, including the following recommendations:

- ▶ The Government should apply a materiality threshold to the additional record keeping obligations related to the best financial interests duty.
- ▶ APRA should provide clear guidance on how expenses should be justified and what records should be kept.
- ▶ The level of scrutiny should be proportionate to the scale of the expenditure and the impact on member outcomes.
- ▶ Payments to related parties, including dividend or profit payments, should be disclosed to APRA, fund members and the public. Where such payments are material, trustees must keep records about how those payments are in the best financial interests of members.

² APRA recently identified poor outsourcing practices in a review released on 5 October 2022. It found examples of poor benchmarking practices focused on justifying the status quo rather than improving members outcomes, further highlighting the importance of scrutiny and transparency around these arrangements.

Interaction with broader regulatory framework

As recognized in the discussion paper, the operating environment for RSE licensees has changed markedly since the SPS 515 framework was introduced. The Your Future Your Super reforms introduced a number of elements aimed at creating a more efficient and fair superannuation system that improves the retirement outcomes of Australian workers. Most relevantly, the performance test introduces an annual assessment of performance to hold RSE licensees to account for members' financial outcomes through greater transparency and increased consequences. APRA's heatmaps are also driving greater transparency and scrutiny of product performance. In addition, the new retirement income covenant and the design and distribution obligations embed improved member outcomes at the centre of superannuation products and services.

The legislated outcomes assessment in s52(9) of the SIS Act and the SPS 515 framework that supports it are also intended to drive "the superannuation industry towards addressing underperformance and improving member outcomes".³ However, this approach focuses on how RSE licensees conduct their business operations in order to drive better outcomes for members, rather than assessing the outcomes themselves. This "bottom-up" approach requires RSE licensees to self-assess whether they have promoted the financial interests of their members and prescribes documents that RSE licensees must produce to demonstrate member outcomes are reflected in strategic objectives and business operations.

While this approach can be useful guidance for RSE licensees in understanding how to ensure member outcomes are central to business operations, it can also lead to a procedural, check-box approach which does not necessarily lead to superior outcomes for members, and which can result in a focus on compliance with process, rather than on performance and member outcomes.

For example, BT Super MySuper has recently failed the annual performance test for the second consecutive year. However, in the annual member outcomes statements published on its website, BT claimed they promoted their members' best interests.⁴ Similarly, in its thematic review, APRA highlighted the inclination amongst some RSE licensees to employ a narrow interpretation in respect of the requirements of SPS 515 and supporting guidance and to undertake only limited analysis or testing to support claims made in relation to outcomes and performance.⁵

The more recent legislative measures described above, in particular the performance test and the APRA heatmaps, introduce a more objective, consistently-applied assessment of whether RSE licensees are improving member outcomes. This approach can help to drive RSE licensees' internal processes and decision-making to meet the objective benchmarks in a less prescriptive, more flexible manner.

We do not suggest that the performance test regime should replace the SPS 515 framework. Under the covenant, trustees must take into account the results of the annual performance test when completing their annual outcomes assessment, and passing the performance test does not of itself lead to improved member outcomes.

³ APRA media release, APRA finalises new measures to strengthen outcomes for superannuation members, 12 December 2018

⁴ [18526A-0322 BT Super and BT Super for Life \(MySuper and Choice\) summary](#)

⁵ APRA Information Paper Findings from APRA's superannuation thematic reviews October 2021, 13-14

However, while the APRA discussion paper recognizes the changes in the regulatory landscape regarding member outcomes, it fails to consider the broader question of whether the content of SPS 515 should evolve as a result of those changes. The paper seems to focus on refining and extending the existing SPS 515 framework without considering whether the role and scope of the framework should be revisited in light of the recent legislative developments. This leads to the issue of duplicate or overlapping regulatory requirements and increased regulatory burden on RSE licensees without additional benefit (and with potentially greater cost) to members.

Recommendation 3: ISA recommends that APRA review its bottom-up approach to regulatory guidance in relation to the member outcomes covenant to ensure that parallel processes undertaken by funds to comply with SPS 515 (and supporting guidance) and the broader regulatory framework, are not duplicated.

For example, APRA may wish to undertake a mapping exercise of SPS 515 against the other legislative elements to identify areas of duplication and regulatory gaps, and to consider the level of prescription necessary in respect of how RSE licensees operate their business and deliver quality outcomes to members. We note that APRA has undertaken this type of work previously in relation to the interaction between the member outcomes obligations and design and distribution obligations. We suggest APRA takes a more holistic approach in the context of its upcoming review of the prudential architecture (including this current review of SPS 515) in order to better streamline compliance obligations and provide clarity to RSE licensees.