

Strategic Planning and Member Outcomes

UNISUPER SUBMISSION TO APRA DISCUSSION PAPER

11 November 2022

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UniSuper welcomes the opportunity to provide feedback to APRA's Discussion Paper – Strategic Planning and Member Outcomes: Proposed Enhancements.

We support the SPS 515 framework and the focus on monitoring and improving member outcomes. In particular we support APRA's intention to uplift the scenario and stress testing requirements of financial projections and the considerations around more in-depth provision of data for benchmarking purposes.

In order to reduce duplication or inefficiency of analysis and to better focus on the member outcomes being achieved, key issues we have described in our responses relate to:

- Business Performance Review – Due to the high level of overlap in terms of content and purpose with the Business Plan, Business Performance Review matters could be included as monitoring considerations within the Business Plan to prevent divergence or duplication.
- Cohorts – rather than requiring a more detailed formulation of cohorts, we suggest that funds be required to identify and monitor for specific detrimental member outcomes which may impact a group of members within a product/investment option. We expect this is better aligned with APRA's underlying intention.

UniSuper would welcome the opportunity to discuss the submission further and to provide additional information in respect of the comments made in this submission.

Should you have further queries, please contact [REDACTED] via email at: [REDACTED]

Consultation Questions

DEFINING OUTCOMES FOR MEMBERS

1. Which, if any, provisions in the SPS 515 framework have worked well in improving business planning? Which, if any, provisions have caused unintended consequences? Please provide details.

UniSuper is supportive of the SPS 515 framework as it is consistent with existing practice. We support the further requirements related to the Annual Outcomes Assessment contained within SPS 515 and would encourage APRA to consider additional updates to this area.

However, the requirements around scale, operating costs and basis for the setting of fees should be made more specific to the member outcomes that APRA seeks to improve. For example, scale should not be considered in isolation, but should link directly to the operating costs incurred by members, the ultimate financial impact. However, unless the fund is operating in a deficit position, the operating costs are already reflected in the fees charged to members, which is included in the legislated test items. This creates a clear potential overlap. We suggest the additional Outcomes Assessment requirements in SPS 515 could be updated to include the following items:

- Sustainability – noting existing APRA metrics could be used
- Scale – UniSuper is not aware of any fund that has concluded that it did not provide adequate scale to its members, either on the previous MySuper test or the current Outcomes Assessment. Consequently, to offer value, considerations around scale should be more specific to providing justification to what level of scale the fund seeks to provide to its members and how this was arrived at (i.e. at \$x FUM we believe our fees / costs would be below y% of the industry) and monitoring of how the fund was tracking to achieve this level of scale.

Areas of the SPS 515 framework which could be improved relate to:

- Business Performance Review

The SPS 515 Business Performance Review requirement currently has significant overlap with the Annual Outcomes Assessment. UniSuper is supportive of the components of the Business Performance Review. For simplicity, and to reduce unintended duplication of analysis, some of these matters could be moved directly into the Business Plan as 'considerations'.

Suggested amendments would be:

- Business Performance Review monitoring to be included as a requirement under the Business Plan, with a summary of the monitoring results to be included in each Business Plan, i.e. expansion of para 11
- Monitoring of strategic objectives to be as frequent as suitable for a fund's operations, preferably at a greater frequency than annually.

Expenditure and Reserves Management

The significant expenditure section in SPS 515 overlaps with the current BFID requirements. We note that APRA is considering the current YFYS review before making updates to expenditure management, however, our initial suggestion is that significant expenditure should be removed from SPS 515. We would also recommend a uniform regulatory approach that treats trustees the same regardless of whether they self-administer or outsource to an unrelated third party. Under a uniform regulatory approach, if there were to be any suggestion of a regulatory look-through to expenses incurred by a service provider to a trustee, the same categories of expenditure should be subject to the same regulatory scrutiny regardless of whether they are incurred by a related-party service provider or an unrelated service provider.

Cohorts

The current structure around cohorts and their formulation should be reviewed with a focus on placing greater emphasis on member outcomes. Further discussion is provided below under Question 3.

2. Has APRA correctly identified the areas for enhancement? What additional areas could benefit from enhanced requirements or guidance to support effective strategic planning and delivery of outcomes to members?

While a fund should clearly have outcomes which are quantifiable and objective (i.e., strong returns) we note that there may be some outcomes which are subjective in nature. An example of outcomes which may be more subjective relate to a fund's formulation of the retirement strategy, which given the wide variety of factors which impact a retiree's journey may be challenging to quantify. Consequently, it may not be appropriate to introduce a requirement where the Board can only approve an outcome if it must be framed in a constrained manner. It should be clear that at least some of the outcomes must be quantifiable and objective, however the Board should retain flexibility.

Further discussion on the setting of member cohorts provided below under Question 3.

3. What additional guidance could be provided to help inform the development of cohorts?

While UniSuper is supportive of the continuous improvement of data collection and analysis, it is unclear how the current cohort approach will deliver benefits to our members. Historically, the need for 'cohorts' was clear given a large amount of comparison data was only provided at the Fund level. For example, the Productivity Commission Review of the superannuation system which sought to measure differences in fund level performance. Projects undertaken by APRA, including the MySuper and Choice heatmaps, have enhanced transparency and provided a universally accessible way to provide and access performance comparisons at the investment option level.

Data is now collected to allow each fund to compare, at a minimum, the majority of their products and / or investment options which should be carried out for the purpose of the Annual Outcomes Assessment as well as Business Performance monitoring (refer to Question 1 response).

For any grouping of members smaller than an investment option, UniSuper does not believe that cohort type analysis will provide value. Consequently, further guidance should not be provided and instead the requirement to monitor for cohorts in SPS 515 should simply be removed. The level of granularity provided by investment option comparison should arguably provide the most valuable, and readily comparative data.

UniSuper is supportive of APRA's expectation that member outcomes should be monitored for all members. We note that the member outcomes related to the strategic objectives, as set by the Fund, should already be monitored. Consequently, to alleviate concern of any sub-groupings of members who are being left behind, rather than trying to construct cohorts, each fund should be required to specifically list areas of concern which could cause specific members to suffer detrimental impact.

This would be consistent with the requirements of ASIC's Design and Distribution Obligation, where a product provider must monitor for detrimental impacts. A checklist should be developed help identify any groups of members whose member outcome for the period was lower than expected, for example:

- Excessive switching between investment options
- Excessive fees being charged
- Materially lower net return for the period, for example compared to a default member or after allowing for proxies.

This list of concerns would be expanded over time as the fund monitored its member outcomes, with APRA providing further guidance, particularly as it is rolled out across the industry. This should result in not only the member outcome continuing to be monitored (as per question 1) but also sub-groups of members with poorer member outcomes being explicitly identified.

We support the consideration of cohorts under SPS 250, as the assessment of an insurance benefit design is very different. The response above relates exclusively to the cohort requirements under SPS 515. Given the importance of

insurance in superannuation the fund's analysis required under SPS 250 should continue to also be considered as part of the overarching SPS 515.

4. *What challenges, if any, has industry faced in developing cohorts of members for the purposes of the retirement income strategy?*

The development of cohorts for the purposes of retirement income strategy (RIS) is challenging due to the uniqueness of member needs, and the multiple forms of assistance available to address these needs. Granularity in the RIS may lead to inappropriate or unnecessary grouping of members and a loss of focus on individual requirements.

The RIS outlines, in general, how funds will assist members to achieve and balance various objectives as set out in the Retirement Income Covenants (Covenants). As there are no prescribed or mandatory forms of assistance that must be provided by funds, funds are likely to differ – quite significantly in many cases – in the review and development of assistance provided to members, as well as in how the assistance is documented in the strategy and presented to members.

The assistance provided to members come in many forms, including provision of product solutions, services, education, guidance, and advice.

Our view is that member guidance, from a practical point of view, takes precedence over other forms of assistance – particularly member guidance around the need for and importance of considering these objectives (maximising expected retirement income, managing expected risks, and having flexible access to expected funds) before considering and deciding on solutions. This is because members are not used to considering and making retirement solution decisions as framed by these objectives, due to either: culture or history (no formal objectives of superannuation system), or institutionally (due to them being lifetime participants of a conventional defined contribution system in which the focus is usually placed on the value of the superannuation balance and the annual returns achieved).

Importantly, member guidance around these objectives, including why they are important and relevant for the consideration of retirement solutions, is equally applicable to all members who are approaching retirement – regardless of their characteristics and objectives. As such, cohorting is almost irrelevant in the context of member guidance, especially within the RIS itself.

While it may be tempting to define and create granular cohorts for the RIS, perhaps driven by the wish that a more tailored RIS may potentially be useful for different members, the opposite is true because:

- Having more granular cohorts is likely to result in an unnecessary complex RIS which would be difficult to be summarised and communicated to members – particularly in the form of a summary published on funds' website
- Retirement is a problem of one, meaning that a member's retirement objectives do not look like another member's although two members may have the same characteristics including those known to funds (superannuation balance, age, etc) and those unknown to funds (home ownership status, other information relevant assessing the amount of Age Pension a member may receive). Having overly granular strategies for different cohorts may have unanticipated effects on member decision making process and lead to unintended outcomes.

For the purposes of the RIS, UniSuper has taken a deliberate approach of keeping the classes of beneficiaries simple for reasons stated above.

Importantly, having a simple RIS (i.e., without many cohorts / sub-classes) does not imply that UniSuper is not taking a more granular approach in designing and reviewing different forms of assistance in practice where relevant – especially in its review of the retirement income product offering and the design of the Guided Choice framework.

As an example, the assisted choice framework, as described in the UniSuper RIS, will be designed to signpost members towards several potential retirement income product solutions – with each solution representing a good starting point to achieve and balance the objectives differently. While the eventual implementation of the Guided Choice

framework (as well as the solutions presented to members) may or may not be significantly different for different members / cohorts, the underlying analysis will be carried out to cover all key UniSuper members of different characteristics.

MANAGING FINANCIAL RESOURCES

5. *To what degree would taking the above approach to financial management, including adoption of performance measures, monitoring and stress testing, differ from current practices? How might such obligations be implemented without undue regulatory burden?*

Based on the APRA discussion paper, there would be limited impact to existing UniSuper practices and any new obligations would be expected to be consistent with the ongoing development of internal financial modelling capability.

6. *What, if any, unintended consequences may arise from these proposed requirements? Please provide details.*

Not applicable.

7. *Given the scope of the current requirements in SPS 114, much of the financial resources to manage and respond to operational risk have, necessarily, been met through existing reserves. How do RSE licensees presently use their financial resources to minimise the impact of operational risk events on members?*

UniSuper does not have any key operational risk concerns currently. However, we continually invest in our services and operations to respond to potential scenarios. Expenditure, including material projects, are considered as a matter of existing business planning or the project prioritisation process.

FINANCIAL PROJECTIONS

BOARD OVERSIGHT OF PROJECTIONS

8. *How does the Board currently satisfy itself that a robust financial projections methodology underpins the business plan? How does the Board intend to develop its use of financial projections (and assumptions underpinning them) presented in the business plan?*

UniSuper provides robust financial projections underpinned by a considered methodology, including key assumptions and scenario testing, as part of the Business Plan. The projections, which are an integrated approach in terms of our usual financial budgeting, are internally coordinated and verified to ensure soundness. UniSuper ensures its board is composed of individuals with the ability to interpret and interrogate financial projections through the use of a skills matrix and thorough selection process.

As a large and growing fund, including positive growth on the three-sustainability metrics included in the APRA heatmap, we do not have any particular areas of concern when carrying out our financial projections in the near or medium term. Consequently, our current use of financial projections is primarily to consider: i) what are the downside risks and scenarios which could threaten our strategic objectives, and ii) considerations of different levels of growth.

To ensure that financial projections are robust and appropriate for the Business Plan, we suggest two areas of enhancement:

1. Future assumptions are, by definition, based on unknown events. The Business Plan could be required to include areas where actual performance over the year was materially lower than the previous assumptions in the Business Plan. That would allow the Board to consider whether the fund's strategic outcomes were likely to be achieved in the future by focussing on actual events and numbers. This could be included in the Business Performance Review monitoring requirements, which we recommend to be included in the Business Plan to limit duplication and provide a better representation of past events and future assumptions (refer to Question 1 response)
2. Funds should be required to receive sign-off from appropriate professionals. This could include requiring the projection methodology and key assumptions were appropriate, particularly when considered as a whole. Requiring sign-off by professionals, whether in-house or external, would ensure that the technical material was being reviewed by the most appropriate party. Appropriate professionals would likely include the fund's Actuary or Auditor.

FEE SETTING PRINCIPLES

9. *What additional fee setting principles should be reflected in the SPS 515 framework?*

Additional fee setting principles are not relevant to UniSuper's operations, however, we note that the overall fee is considered by existing principles proposed by APRA.

ASSESSING PERFORMANCE

10. *What challenges have RSE licensees experienced in aligning the timing of the member outcomes assessments and annual BPRs and business planning cycles? How might these challenges be avoided in future?*

UniSuper recommends that the Business Performance Review requirement be removed as a standalone artefact, and instead the considerations of the BPR should be considered as part of the Business Plan. Greater information is provided in our response under Question 1.

11. *How have RSE licensees incorporated the result of APRA's heatmaps and the legislated performance test into their BPRs?*

UniSuper has included consideration of the APRA Heatmaps in the Annual Outcomes Assessment, and the results of the Annual Outcomes Assessment is considered in the Business Performance Review. However, as UniSuper already had existing industry research subscriptions to evaluate our investment options, this has had limited impact.

12. *What additional benchmarks do RSE licensees consider when assessing performance? In determining an overall assessment of outcomes, how are the various benchmarks weighted?*

UniSuper uses existing industry research subscriptions to consider our product and investment option performance.

In terms of an overall assessment of outcomes, particularly the requirement under the Annual Outcomes Assessment, UniSuper has not needed to carry out a detailed weighting in the past as our analysis demonstrates that both our fees and returns as well as other benefits are strong. UniSuper is not aware of how other funds have been weighting their assessments, however it may be beneficial if APRA introduced guidance on a specific weighting methodology. We note that similar methodology is already carried out in benchmarking services provided by industry research bodies and is also used commonly in competitive tenders for institutional clients.

13. *What additional areas of data would be useful in developing comparable assessments of performance?*

Information (i.e., fees, investment return and net return) on all investment options across the industry would be valuable, noting that not all investment options would be comparable, and each fund should review the data as appropriate for their analysis. When comparing the investment options, further details to consider the appropriateness of the inclusion for comparisons would be required, such as:

- Clarity on growth allocation, noting current industry research in this area
- Appropriate breakdowns of asset allocations, including passive, active management styles and listed / unlisted
- Volatility data, in conjunction with the above.

The above would be helpful in providing more complete and comprehensive analysis of investment options across the entire industry.

APRA should also consider whether the current provision of investment performance is consistent across all products, including whether more specific definitions are required such as those contained under FSC Standard no. 6.

14. *What data (including benchmarks) do RSE licensees plan to use to develop retirement cohorts and assess performance of post retirement income strategies?*

There is no immediate plan to develop retirement cohorts (i.e., expanding beyond the current sub-classes) for the purpose of the RIS.

We acknowledge that assessment is an important element as it facilitates accountability and provides a framework for further improvement. However, we also recognise and acknowledge that it is difficult to objectively measure the effectiveness of the RIS as there are no easily quantifiable metrics that could measure how well the Fund assists members in achieving and balancing the objectives. The nature of a broad range of assistance makes retirement income strategies quite difficult to assess.

For example, how would one assess the effectiveness of guidance provided to members in identifying a suitable retirement income solution that addresses the objectives? Who will be doing the assessment? Trustees? Members? Regulators? Or a combination of all? Members might be in the best position to provide the inputs required for the assessment because they are the consumers of the guidance but there are multiple issues that are not easily resolved:

- It is not possible to know which solutions have worked out well for a particular member until they get to the end of their lives as the success of the solutions – particularly for individuals – can technically only be measured *ex-post*, i.e., when the individual dies, as only by then, one will know if there was enough money or there was enough income, or that all the needs and objectives were met
- There is a difference between the effectiveness of a strategy / retirement income solution *in expectation* (*what outcomes the strategy / solution is expected to produce*) and the effectiveness of it *in execution* (*what outcomes the strategy/solution produces in practice given the actual experience*). As an analogy, this is not dissimilar to the issue widely raised by the industry regarding the Your Future Your Super (YFYS) performance test and its failure to measure the most important thing, which is whether a fund is pursuing an investment strategy (i.e., asset allocation) that's appropriate for its members by focusing solely on implementation (performance against a SAA benchmark portfolio).

Given the issues raised and explained above, we would suggest an ex-ante quantitative approach for the purpose of assessing the effective of different strategies and solutions.

In broad terms, the quantitative approach would evaluate simulated outcomes against stated objectives of retirement solutions designed for cohorts (each of which might be captured by a representative individual) in order to generate an assessment of those solutions. Given the prevalence of account-based pension drawn at the minimum drawdown rates, it is appropriate to use it as the benchmark (or floor, depending on how different objectives are weighted/balanced) for the assessment of new strategies and solutions. This approach has the potential to provide a framework for funds to measure the potential impact of different initiatives that would make a meaningful impact on member outcomes.

Given the superannuation industry is only at the beginning of building a “retirement” industry, it will take time before it becomes clear which retirement strategies work well. As such, the development of RIS assessment should be approached as an evolutionary process.

About UniSuper

UniSuper is one of Australia's largest super funds with more than 500,000 members and close to \$110 billion in funds under management. With a heritage of supporting the higher education and research sector, UniSuper opened its doors to all Australians in July 2021.