



# Prudential Practice Guide

## **SPG 521 – Conflicts of Interest**

July 2013


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## About this guide

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 521 Conflicts of Interest (SPS 521)* sets out APRA's requirements in relation to an RSE licensee's management of conflicts of interest and duty. This PPG aims to assist an RSE licensee in complying with those requirements and, more generally, to outline prudent practices in relation to conflicts of interest.

This PPG is to be read with other PPGs and prudential standards relevant to the identification, avoidance and management of conflicts including SPS 521, *Prudential Standard SPS 520 Fit and Proper (SPS 520)*, *Prudential Practice Guide SPG 231 Outsourcing* (with respect to potential conflicts of interest arising from outsourced activities) and *Prudential Standard SPS 220 Risk Management* (with respect to consideration of conflicts of interest when assessing material risks).

For the purposes of this guide, and consistent with the application of SPS 521, 'RSE licensee' has the meaning given in the *Superannuation Industry (Supervision) Act 1993 (SIS Act)*.

A number of areas of law are also relevant to an RSE licensee's identification, avoidance and management of conflicts of interest, including general law requirements, sections 52(2)(d), 52A(2)(d) and 58A of the SIS Act and duties in the *Corporations Act 2001*.

Subject to these requirements, an RSE licensee has the flexibility to structure its business operations 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.

## Introduction

1. The SIS Act requires an RSE licensee to undertake its business operations in the best interests of beneficiaries, consistent with the retirement purposes of superannuation. In support of this, an RSE licensee and each individual director of an RSE licensee must comply with covenants set out in sections 52 and 52A of the SIS Act, respectively, to act honestly, to exercise a required degree of care, skill and diligence and to perform their duties and powers in the best interests of beneficiaries.
2. Under sections 52(2)(d) and 52A(2)(d) of the SIS Act (the conflicts of interest covenants), an RSE licensee is required to ensure that, where a conflict arises and has not been avoided, the duties to, and interests of, beneficiaries receive priority over any duties to, and interests of, other persons.
3. A conflict has the potential to prevent an RSE licensee from performing its duties by placing it in a position where it may deliberately or inadvertently prefer the interests of another person to those of a registrable superannuation entity's (RSE's) beneficiaries. Alternatively, a person or firm undertaking a material business activity for, or otherwise advising, an RSE licensee may have a conflict that could affect the nature or quality of the advice given or service provided.
5. This culture may be demonstrated through:
  - (a) openness, where requirements to disclose relevant duties and interests are understood, accepted and followed throughout an RSE licensee's business operations;
  - (b) recruitment and human resources policies that highlight, more generally, the importance of initial and ongoing disclosure of relevant duties and interests and resulting potential and actual conflicts;
  - (c) wide and regular promotion of the value of proactive disclosure of relevant duties and interests and resulting potential and actual conflicts through internal communications; and
  - (d) policies that encourage and support whistleblowing.
6. APRA considers that transparency of an RSE licensee's approaches is fundamental to the effective management of conflicts. The requirements in r. 2.38 of the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations) for the public disclosure of an RSE licensee's registers of relevant duties and interests, as well as its conflicts management policy, encourage an environment of openness and disclosure.

## Conflicts management culture

4. A strong conflicts management culture, as part of an RSE licensee's risk culture, is essential for the effective management of conflicts throughout an RSE licensee's business operations. An RSE licensee's conflicts management culture generally reflects its corporate values as well as the attitudes and behaviours of individuals within its business operations. Together, these determine an RSE licensee's commitment to conflicts management and the effectiveness of the RSE licensee's approach.

## Conflicts management framework

7. The Board of an RSE licensee (the Board) is ultimately responsible for the management of conflicts throughout the entirety of its business operations.
8. A conflicts management framework enables an RSE licensee to implement a holistic approach to the management of conflicts and ensure that all business units are aware of the potential impact of competing duties and interests on the RSE licensee's ability to comply with the conflicts of interests covenants. This can be achieved through ensuring that potential and actual conflicts are identified and disclosed, then assessed and avoided or, if not, managed.

9. SPS 521 requires that an RSE licensee have in place a conflicts management framework approved by the Board to ensure that the RSE licensee identifies all potential and actual conflicts in its business operations and takes all reasonably practical actions to ensure that they are avoided or prudentially managed. A sound conflicts management framework supports the ability of the Board to assess conflicts on an ongoing basis and address unexpected conflicts of duty or interest appropriately and in a timely manner. Prudent practice in relation to conflicts management would include continual assessment of the conflicts management framework in light of changes to matters such as:
  - (a) an RSE licensee's business operations;
  - (b) the structure of the RSE licensee;
  - (c) the RSE licensee's service providers and any changes to or within service providers; and
  - (d) responsible persons and changes in their composition or circumstances which would impact the RSE licensee's business operations.
10. In APRA's view, an effective conflicts management framework is one that mitigates and manages the risk that a conflict may result in an RSE licensee acting improperly to the detriment of its beneficiaries. It would also mitigate and manage the risk that an RSE licensee may be perceived to have acted improperly, which may affect the reputation of its business operations.
11. APRA also expects that reporting structures and processes for the escalation of issues, including any whistleblowing procedures, would be clearly defined and documented to enable implementation and consistent understanding of the conflicts management framework.
12. SPS 521 requires that an RSE licensee's conflicts management framework is comprehensively reviewed by operationally independent, appropriately trained and competent persons at least every three years, and that the RSE licensee also reviews the conflicts management framework on an annual basis. APRA expects the annual review would cover ongoing monitoring processes and controls focused on potential and actual conflicts as well as broader compliance with the conflicts management framework across the entirety of its business operations. If the annual review is undertaken by a person with a role in the implementation of the conflicts management framework, a prudent RSE licensee would consider appropriate steps to ensure the review is objective. The outcomes of the review may be used to assist the future development or enhancement of the conflicts management framework.

### Conflicts management policy

13. An RSE licensee's conflicts management policy is the primary means for clearly communicating its approach to the management of conflicts across its business operations.
14. In addition to meeting the minimum requirements for the conflicts management policy in SPS 521, APRA expects that an RSE licensee would consider whether the policy may also document:
  - (a) the relationship between the register of relevant interests and other gift or interests policies that apply to all employees within the RSE licensee's business operations; and
  - (b) processes for reporting additional relevant duties and interests that may not have been disclosed according to the policy.

15. An RSE licensee that is part of a broader group of associated entities may adopt conflicts management policies of the group provided that those policies meet the requirements of SPS 521 and, in particular, enable the RSE licensee to achieve the objectives of its conflicts management framework. If a group policy is adopted by an RSE licensee, APRA expects the RSE licensee would recognise that obligations or perceived obligations to other entities in the group may be the source of a conflict and ensure that this is taken into account in complying with the conflicts management framework and policy requirements in SPS 521.
16. SPS 521 requires an RSE licensee's conflicts management policy to include provisions relating to undertaking regular and thorough enquiries to identify all conflicts arising from certain relationships. APRA's view is that such enquiries would, in normal circumstances, take place when establishing a relationship, be reviewed no less frequently than annually and be sufficiently robust to ensure that the objective is met.

## Registers of relevant duties and relevant interests

17. An RSE licensee's registers of relevant duties and interests provide a means to identify potential and actual conflicts of the RSE licensee and of its responsible persons and associates.
18. An RSE licensee is required to disclose a register of relevant duties and interests.<sup>1</sup> It is important that these registers are kept up-to-date to achieve the goal of informing interested stakeholders about potential external influences on decision-making within an RSE licensee's business operations.
19. APRA expects that an RSE licensee would develop and structure its registers of relevant duties and interests in a way that best reflects the structure and complexity of its business operations. This may result in the production of a single register that covers both relevant duties and relevant interests where the RSE licensee considers this to be the most effective method of disclosure.

## Assessment of relevance of duties and interests

20. APRA considers that an RSE licensee is best placed to assess whether a particular duty or interest is relevant for the purposes of its registers of relevant duties and interests. APRA expects that the RSE licensee's processes and criteria for determining whether a particular duty or interest is relevant, including where the RSE licensee applies a dollar amount for the purposes of assessing the relevance of interests, would ordinarily be documented as part of the conflicts management policy. Attachment A provides a non-exhaustive list of examples of relevant duties and interests.
21. It would be prudent for an RSE licensee, when determining what it considers to be relevant for the purposes of the registers, to consider the nature of the duty or interest, including whether it is a one-off occurrence or whether it has an ongoing, recurring or cumulative nature.
22. APRA expects that an RSE licensee would ordinarily assess relevance of a duty by considering the extent to which the role giving rise to the duty could influence the duties owed by the RSE licensee, or a responsible person of the RSE licensee, to beneficiaries.
23. A director of an RSE licensee will often be nominated or appointed by, and may be under an expectation that they will represent the interests of, a nominating body or appointer. APRA considers that this relationship would ordinarily give rise to the director having an obligation to the nominating body or appointer. APRA expects that an RSE licensee would implement processes to ensure that, when appointed, such directors are aware of the strong possibility of a conflict between the interests of beneficiaries and the interests of the nominating or appointing body, as well as the need to disclose relevant duties and interests and avoid, if not manage, any resulting actual or perceived conflicts.

<sup>1</sup> Refer to r. 2.38 of the SIS Regulations.

24. An RSE licensee may consider whether a dollar amount (or equivalent value expressed as a dollar amount) is an appropriate measure of relevance for interests. APRA encourages a prudent approach to setting a dollar amount, including consideration of appropriate limits for different circumstances or for different types or categories of interests, including whether to implement limits based on one-off events as well as the cumulative amount arising from a series of low-value amounts.
25. Responsible persons are subject to fit and proper assessments under SPS 520. A person need not be an employee of an RSE licensee to be a responsible person. APRA expects that an RSE licensee would consider the extent to which its conflicts management framework and register of relevant duties and interests applies to consultants, contractors and employees of other entities, in particular RSE auditors and RSE actuaries<sup>2</sup>, within the context of the RSE licensee's business operations.
26. An RSE licensee may determine that a duty or interest held by any person performing functions for the RSE licensee is relevant to the capacity of that person to undertake their role in a manner that is consistent with the interests of beneficiaries. This may include staff of the RSE licensee who are not defined as responsible persons under SPS 520. Where this is the case, APRA expects that an RSE licensee's conflicts management framework would ordinarily cover these duties and interests.
27. APRA encourages RSE licensees to take a pragmatic approach when determining whether interests held by an associate of the RSE licensee fall within the operation of the conflicts of interest covenants. This may involve a process whereby an RSE licensee determines that a gift received by the associate will be considered to be a relevant interest only where it would be treated as exceptional under the associate's own conflicts management policy or approach.

## Avoidance and management of conflicts

28. Recording relevant duties and interests enables an RSE licensee to demonstrate that it is taking steps to enable it to identify all potential or actual conflicts of interest. The next key stage in the conflicts management process is avoidance and, if avoidance is not possible, management of potential and actual conflicts. In APRA's view, the act of declaring that a relevant duty or interest has resulted in a conflict is not in and of itself sufficient to manage that conflict. It is APRA's expectation that an RSE licensee would ensure that it is able to clearly demonstrate that the actions that it has taken in response to a potential or actual conflict are prudent and defensible.
29. APRA considers the conflicts of interest covenants to be relevant where an RSE licensee or responsible person is considering a particular course of action and is affected by a conflict. The conflicts of interest covenants do not authorise an RSE licensee or responsible person to proceed where general law requires the conflict to be avoided altogether.
30. APRA recognises that, in some circumstances, an RSE licensee may identify conflicts that it has determined are so acute or pervasive that they cannot be managed, or are of a kind where the general law requires avoidance. In these circumstances, an RSE licensee may determine that it has no option but to take steps to avoid the conflict.
31. In avoiding or managing conflicts associated with a relevant duty or interest, an RSE licensee may decide it is necessary or prudent for the person to relinquish the duty to another person, dispose of the interest or cease their role with the RSE licensee.

<sup>2</sup> Refer to s. 10(1) of the SIS Act for definitions of 'RSE auditors' and 'RSE actuaries'.

32. APRA expects that a director of an RSE licensee with a relevant interest or duty that conflicts with the duty to or interests of beneficiaries, and relates to a matter that is being considered at a directors' meeting, would not ordinarily be present while the matter is being considered at the meeting or otherwise vote on the matter. APRA expects that an RSE licensee's conflicts management policy would ordinarily prohibit the retention of gifts and hospitality above a certain value.
33. In some circumstances, an RSE actuary that acts for the RSE licensee may also act for an employer sponsor, giving rise to the RSE actuary having a duty to both the RSE licensee and the employer sponsor. This scenario may lead to situations where the actuary has a potential or actual conflict. In such scenarios, APRA expects that an RSE licensee would pay particular attention to the appropriateness of that actuary continuing to act for both parties and, in the event of the actuary continuing to act for both parties, what actions it would take to manage any potential or actual conflicts. An RSE licensee may consider requesting the actuary to communicate the actuary's approach to conflicts management

### **Conflicts of interest covenants and tied service provider override**

34. The conflicts of interest covenants interact with the tied service provider override in section 58A of the SIS Act. This override requires an RSE licensee to disregard any provision in the governing rules that purports to require the RSE licensee to use a particular service provider or providers. This enables the RSE licensee to consider other potential service providers, investment vehicles or financial products, including entities that are not associated with the RSE licensee. Section 58A does not prevent an RSE licensee from using or continuing to use an associated service provider, but the RSE licensee must continue to comply with the conflicts of interest covenants, as well other relevant covenants and duties.



## Attachment A

1. Examples of scenarios that might arise at the RSE licensee level include, but are not limited to:
  - (a) where the RSE licensee has an association with a service provider (such as an investment manager or administrator), investment vehicle or financial product and the governing rules permit the RSE licensee to engage those service providers, invest in those vehicles or purchase those financial products; and
  - (b) where the RSE licensee is the trustee of multiple RSEs and it is considering a successor fund transfer from at least one of these RSEs to another.
2. Examples of scenarios that might arise in relation to responsible persons include, but are not limited to:
  - (a) where a responsible person is a director or other officer of another entity, and that other entity:
    - (i) provides a service or financial product to, or operates as an investment vehicle for, the RSE licensee;
    - (ii) is being considered by the RSE licensee as a possible provider of such a service, financial product or investment vehicle;
    - (iii) is being considered by the RSE licensee as the transferring fund or successor fund in a successor fund transfer; or
    - (iv) operates in the same market as the RSE licensee, potentially in competition;
  - (b) where a responsible person has an ownership interest in an entity referred to in paragraph 2(a) of this Attachment;
  - (c) where an entity currently provides a service or financial product to, or operates as an investment vehicle for, the RSE licensee, and that entity offers gifts or hospitality; and
  - (d) where a responsible person is also a member of the RSE and may be personally affected by a decision of the RSE licensee.
3. Examples of scenarios that might arise in relation to external service providers include, but are not limited to:
  - (a) where the RSE is a defined benefit fund and the RSE actuary provides advice on funding matters to both the RSE licensee and a relevant employer sponsor; and
  - (b) where a service provider provides staff who take part in the internal operations of the RSE licensee and are involved in a decision that affects the future commercial relationship between the RSE licensee and the service provider.



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