PRUDENTIAL PRACTICE GUIDE

SPG 515 - Strategic and Business Planning

August 2019

Contents

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 515 Strategic Planning and Member Outcomes (SPS 515) sets out APRA's requirements for a registrable superannuation entity (RSE) licensee (RSE licensee) to set strategic objectives for its business operations and to maintain a written business plan that articulates an RSE licensee's approach to achieving these strategic objectives. Additionally, SPS 515 contains prudential requirements to ensure that fund expenditure is in the best interests of members and that there is a comprehensive decision making and monitoring process for expenditure that is determined by its size or nature to be significant.

SPS 515 also requires an RSE licensee to undertake a business performance review to annually assess its performance in achieving its strategic objectives. The guidance in this PPG relates to the business planning and expenditure management requirements in SPS 515. This PPG is also to be read in conjunction with *Prudential Practice Guide SPG 516 Business Performance Review* (SPG 516) which provides guidance on APRA's expectations with respect to the business performance review and the annual outcomes assessment required under section 52 of the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

Prudential Standard SPS 220 Risk Management (SPS 220) sets prudential requirements in respect of the business plan as a risk management tool.

Subject to the requirements of RSE licensee law[1], an RSE licensee has the flexibility to structure its business operations in the way most suited to achieving its strategic 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.

For the purposes of this guide and consistent with the application of SPS 515, 'RSE licensee' has the same meaning given in section 10 of the SIS Act.

[1] Refer to section 10 of the SIS Act for the definition of 'RSE licensee law'.

Introduction

1. Sound strategic and business planning supported by robust processes enables an RSE licensee to respond to strategic challenges and ensure its business operations are well positioned for the current and future provision of quality outcomes to members. Rigorous decision-making in relation to fund expenditure positions an RSE licensee to meet member best interest obligations and provide quality outcomes for members.

2. SPS 515 sets requirements intended to ensure that an RSE licensee's strategic objectives and business planning processes support the RSE licensee achieving the outcomes it seeks for members and ensure the sound and prudent management of its business operations. SPS 515 also sets out requirements in relation to expenditure management and decisions that will result in significant expenditure.

3. An RSE licensee's business plan will reflect decisions as to how it proposes to organise and manage its business operations and pursue its strategic objectives. The impact that these decisions have on the RSE licensee achieving its strategic objectives is assessed through the annual business performance review required under SPS 515. The findings of this review are required to be considered as part of the RSE licensee's annual review of its business plan and ultimately considered in the setting and review of strategic objectives. RSE licensees are expected to ensure that there is a clear connection between the annual business performance review, the strategic objectives and the business plan.

Strategic objectives

> The Board is responsible for approving strategic objectives for the licensee's business operations. The setting of strategic objectives guides an RSE licensee to determine, through its business planning process, the key activities it will undertake to provide quality outcomes for members.

4. SPS 515 requires an RSE licensee to develop strategic objectives that must be approved by the Board. Under SPS 515 the strategic objectives must support an RSE licensee to provide the outcomes it seeks for members and the sound and prudent management of the RSE licensee's business operations.

5. SPS 515 makes clear that there must be a strong link between the outcomes the RSE licensee seeks to provide to members and the strategic objectives set by the Board. It is therefore a requirement under SPS 515 that the outcomes that are sought for members and the most recent business performance review are considered by the Board when it sets or reviews its objectives and develops or revises its business plan.

6. APRA recognises that terminology used to describe strategic and business planning activities varies across the industry. For the purposes of the prudential framework, APRA views the strategic objectives of the RSE licensee as separate to and supportive of, concepts such as the RSE licensee's mission and values, which will generally be more aspirational in nature.

Articulating member outcomes

7. SPS 515 requires an RSE licensee to set strategic objectives that reflect the outcomes it seeks for beneficiaries. In this regard, articulating the outcomes that are sought serves as a key anchor to guide RSE licensee decision making and as a base against which the RSE licensee assesses performance and identifies areas for improvement, including through the business performance review under SPS 515.

8. An RSE licensee would be expected to take a multi-faceted approach to articulating member outcomes, incorporating both financial and non-financial outcomes, and considering both historical and forward-looking analysis.

9. APRA expects that the outcomes sought would, in many instances, be relevant to all or most members. For instance, common outcomes may include achieving a certain level of investment performance or reduction in fee levels over a certain time period. APRA also expects that targeting achievement of certain retirement benefit levels would be a key consideration for all RSE licensees in articulating member outcomes.

10. In addition to common outcomes covering all members, an RSE licensee should give due consideration to whether any specific member cohort outcomes are appropriate, reflecting the different products and options that are made available to various groups of members and the demographic or other characteristics of these member cohorts.

11. APRA expects that an RSE licensee would take a broad approach to articulating outcomes, including, but not limited to:

    a) risk-adjusted investment returns net of investment fees;
    b) administration and other fees;
    c) insurance product design, premiums, claims management, and terms and conditions;
    d) retirement products; and
    e) member services, engagement, and education.

12. For many members, investment performance will be central to the outcomes sought. However, in APRA's view, relying solely on net returns as a measure of outcomes, whether on a relative or absolute basis, would not be sufficient. In addition, seeking to provide the lowest relative fees and costs may not necessarily provide better outcomes for members over the long-term. An RSE licensee may conclude, for example, that members would benefit from short-term increases in costs where this will support appropriate investment in systems and services that are expected to deliver enhanced outcomes over time. Similarly, improved outcomes may result from investments that involve higher investment costs but are expected to provide higher (risk-adjusted) investment returns to offset these additional costs over time.

13. Ensuring insurance arrangements appropriately balance the cost of insurance with members' needs in respect of product design and claims management is also a relevant consideration in assessing overall long-term outcomes for members. APRA expects that in considering outcomes related to insurance, an RSE licensee would have regard to the covenants and requirements concerning insurance in the SIS Act and the requirements under *Prudential Standard SPS 250 Insurance in Superannuation*.

14. An RSE licensee's selection of outcomes would typically draw on extensive historical data, where possible. For example, an RSE licensee could consider long-term data on cost and fee levels in determining targets that are central to the outcomes it seeks to provide to members. In articulating the outcomes they seek for members, RSE licensees are expected to set targets or goals that drive continuous improvement, using the findings of the business performance review to inform these targets and goals.

Sound and prudent management

15. SPS 515 requires an RSE licensee to approve strategic objectives that support the sound and prudent management of the RSE licensee's business operations. Effective governance, risk management, and compliance systems and having the resources to support these functions are critical to the sound and prudent management of an RSE licensee. Such systems are inherently linked to the operational efficiency and sustainability of an RSE licensee's business operations as they are central to sound decision-making and resilience to unexpected events. APRA expects that an RSE licensee in developing and approving strategic objectives would assess whether enhancements are required to the necessary systems, processes and supporting infrastructure to support the core components of sound and prudent management.

Adequacy of resources

16. As part of the process of setting strategic objectives and managing its business operations in a sound and prudent manner, APRA expects an RSE licensee would form a view of its current and required level of financial resources. APRA expects that in determining the required level of financial resources, an RSE licensee would consider all relevant information and factors, including at a minimum:

    a) the financial interdependency of the RSE(s) with other entities, such as promoters, or where the RSE licensee is part of a broader group, related entities;
    b) its ongoing and forecast financial position and performance, including cash flow forecasts to meet the RSE licensee's liquidity, liability and operational requirements;
    c) membership projections, including the active member ratio, member demographics, operating costs and fees charged to members;
    d) changes in strategy, business plans, operating environment, current and potential sources of competition and other factors
    that might affect the operations or risk profile of the RSE licensee and its underlying RSE(s);
    e) access to shareholder capital and ongoing employer sponsor financial support where relevant; and
    f) the sustainability of and potential for innovation in the products and services available within the RSE(s).

    In addition to assessing the current and required level of financial resources, APRA expects an RSE licensee would have an accurate understanding of existing human and technical resources. Whether this level of resourcing is adequate will be fundamental to an RSE licensee effectively executing and achieving its strategic objectives and the underlying business plan. Conducting analysis of resourcing for the purposes of setting strategic objectives would enable an RSE licensee to meet the adequacy of resources requirement under SPS 220.

Determining strategic objectives

17. SPS 515 requires strategic objectives to be specific, measurable and informed by the outcomes the RSE licensee seeks for members, the RSE licensee's risk appetite statement, the most recent business performance review and the RSE licensee's legislative obligations under the SIS Act relating to insurance, investments, risk and financial resources and the sole purpose test.

18. When setting strategic objectives, APRA expects an RSE licensee would consider its performance and achievements relative to previous business plans and its expectations for the future, including the strategic challenges that may arise from expected changes in the operating environment. For example, if membership has been declining for the last five years, the strategic objectives that are set would be expected to take this trend into account.

19. APRA expects that an RSE licensee that is part of a conglomerate group would develop and approve strategic objectives independently of the group to ensure that priority is given to the duties to and interests of members.[2]

20. APRA recognises that an RSE licensee may seek to align its strategic objectives with those of third parties that may be relevant to the provision of outcomes for members, such as promoters or other associated entities.[3] In such circumstances, however, APRA expects that the RSE licensee would exercise its own independent judgement and decision-making when setting strategic objectives.

21. It is important that an RSE licensee is aware of the strategic objectives of its material service providers, including those that are associated or related through a group structure, especially where the activities of these entities have the potential to affect the products and services that the RSE licensee provides to members, as well as any matters affecting business continuity arising from that provider. APRA therefore expects an RSE licensee would consider the extent to which the current and future activities of outsourced service providers need to inform the RSE licensee's strategic objectives.

22. SPS 515 requires an RSE licensee to develop and implement a process to monitor its performance relative to the business plan, including whether it is likely to achieve its strategic objectives. An RSE licensee would also be expected to develop a contingency plan where the monitoring process identifies that strategic objectives are unlikely to be achieved.

23. In developing a contingency plan, APRA expects that an RSE licensee would consider the circumstances in which a transfer of members to another RSE licensee would be consistent with its duty to act in the best interests of members.

[2] Refer to section 52(2)(d)(i) of the SIS Act.

[3] A reference to an 'associated entity' is a reference to an associate within the meaning of section 12 of the SIS Act; refer also to *Prudential Standard SPS 231 Outsourcing* (SPS 231) for requirements relating to outsourcing to associated entities.

24. APRA does not expect an RSE licensee would amend a strategic objective solely in response to the failure, or likely failure, to meet the objective, without undertaking analysis to determine the factors that may have caused the failure. APRA expects the business performance review would be central to an RSE licensee understanding the factors that have contributed to not meeting an objective. Where an RSE licensee decides to amend a strategic objective this must be approved by the Board consistent with SPS 515.

Linking strategic objectives and risk management

25. SPS 515 requires an RSE licensee to consider its risk appetite statement when determining its strategic objectives. APRA expects that an RSE licensee's risk appetite statement would identify the strategic and business risks of its business operations and clearly set out risk tolerances. The risk appetite statement would then inform the setting of objectives and the business planning process by focusing on the risks associated with new business initiatives and planned business activities.

26. APRA expects that an RSE licensee would, as part of its risk management framework, establish, maintain and document an effective Management Information System (MIS) as required under SPS 220. The MIS would be commensurate with the size, business mix and complexity of its business operations and would be utilised to monitor and report on material risks, including strategic risks relevant to the business plan. An effective MIS would provide appropriate information at each level of management and decision-making within the RSE licensee's business operations. APRA expects the MIS would be sufficiently flexible to support an RSE licensee's business operations when there are material changes in its strategic objectives, and as a consequence, the RSE licensee's risk profile. An effective MIS would be a key component in demonstrating the sound and prudent management of an RSE licensee.

Business planning

A business plan documents how an RSE licensee will achieve its Board-approved strategic objectives. A robust plan is formed from a comprehensive understanding of the environment in which the RSE licensee operates and considers the impact of differing assumptions and scenarios on the RSE licensee's business operations. Poor business planning may impede an RSE licensee's capacity to properly carry out its duties and its ability to provide quality outcomes for members.

27. SPS 515 requires an RSE licensee to have a rolling business plan of at least three years duration, updated annually. The business plan must set out details on how the strategic objectives will be achieved. APRA expects that the business planning process would be the responsibility of the Board and senior management and any decision-making delegations relating to the business plan would be clearly articulated.

28. The business plan must cover the entirety of an RSE licensee's business operations, and reflect the size, nature and complexity of those operations. It is open to an RSE licensee to develop a business plan that best suits the structure of its business operations. A

business plan need not be a single document but can instead be a suite of appropriate planning documents, for example a strategic plan and a business plan, as determined by the RSE licensee.

Developing the business plan

29. SPS 515 requires an RSE licensee to include in its business plan the initiatives it will undertake to achieve the strategic objectives, its financial projections over at least the next three years, the key assumptions that underpin these projections, and the key performance indicators the RSE licensee will utilise to monitor performance of the plan.

30. Initiatives or projects detailed in the business plan will vary in size, complexity, duration and associated budget or expenditure. APRA expects that the detail provided in the business plan will reflect the complexity and size or budget of each initiative. More complex initiatives would have a separately documented decision making process (e.g. a project plan) distinct from the broader business plan, where the initiative, results sought and its budget are assessed, including the use of a business case where appropriate.

31. APRA expects that for all initiatives there will be predetermined metrics to enable tracking of the initiative and an assessment of whether the initiative has achieved the expected results documented in the business plan.

32. As part of its business planning processes, an RSE licensee would typically prepare budgets for the coming period(s). APRA expects these budgets and associated forecasts of income and expenditure will form the basis of the financial projections contained in the business plan.

33. SPS 515 requires the RSE licensee to detail the key assumptions that inform its financial projections. APRA expects that such assumptions would typically include membership and/or account growth, members in retirement phase, membership demographics, asset growth, operating cost base and fee level forecasts.

34. Fees charged to members are a primary source of revenue for an RSE licensee's business operations and are therefore central to the projections and assumptions that underpin an RSE licensee's level of financial resources. APRA therefore expects that an RSE licensee would adopt an informed and rigorous process that not only ensures compliance with the general fee rules where relevant (including approaches to setting fees on a cost recovery basis) but also considers the impact of fees on the financial interests of members and the ongoing viability of its operations.[4]

Implementing the business plan

35. Once the business plan is approved by the Board, an RSE licensee would ensure that responsibilities are assigned to senior managers to ensure that detailed plans for relevant initiatives, including budgets, are developed and incorporated into the operational plans of the RSE licensee. It would be prudent practice for an RSE licensee to

[4] Refer to Part 11A of the SIS Act and Division 5 of the SIS Act (in respect of MySuper products).

clearly articulate and regularly review the resources allocated to the ongoing implementation of the business plan.

36. APRA expects that a component of the performance based remuneration set for senior management would be linked to successful implementation of key business plan initiatives, achieving both business plan targets and the strategic objectives. However, incentives linked to the business plan should be one component of an overall performance scorecard which is appropriately aligned to the RSE licensee's risk management frameworks and long-term financial soundness.

Monitoring performance

37. SPS 515 requires an RSE licensee to specify key performance indicators that will be utilised to monitor performance against its business plan and trigger action where necessary. Effective monitoring of progress against the business plan enables an RSE licensee to identify when its initiatives are not achieving their expected outcomes, or when the assumptions on which strategic objectives are based are no longer appropriate. Additionally, the monitoring of the performance against business plan is a key input into the business performance review under SPS 515 and the RSE licensee's conclusions on its performance in achieving its strategic objectives.

38. Monitoring also assists an RSE licensee to quickly identify and respond to emerging issues. APRA expects an RSE licensee to have a monitoring process which clearly specifies the triggers that will require reporting to the Board and to consider any necessary action to respond to, or to address, the underlying issues, including activation of the contingency plan. Importantly, trigger levels or tolerances would not be expected to be set at unrealistic levels, such that it is unlikely they would ever be breached.

39. The use of appropriate metrics would be a core feature of tracking performance against the business plan. When deciding these metrics, a prudent RSE licensee would consider:

    a) whether the metrics can be meaningfully measured and monitored;
    b) the balance between qualitative and quantitative data underpinning the metrics; and
    c) the balance between leading and lagging metrics.

40. A non-exhaustive list of relevant metrics is provided in Attachment A to serve as a guide for RSE licensees.

Updating the business plan

41. SPS 515 requires an RSE licensee to update its business plan annually based on the results of the most recent business performance review

42. An RSE licensee's business performance review may identify certain actions that would improve outcomes for members and/or the sound and prudent management of its business operations. APRA expects the RSE licensee to undertake a comprehensive decision making process to determine the most appropriate action; this process would be supported by a cost-benefit analysis. An RSE licensee would document any planned actions and implementation timeframes in the business plan and appropriate supporting

documents. For example, when an RSE licensee's assessment identifies areas of concern in respect of its insurance offering, APRA expects that any action chosen to address the concerns, such as through a re-tendering process, would be reflected in both the business plan and the insurance strategy.[5]

Expenditure management

The management of expenses is an essential component of business planning. Rigorous expenditure management practices ensure that the expenses incurred by an RSE licensee are in the best interests of members and support the sound and prudent management of its business operations.

43. The expenditure management requirements in SPS 515 are intended to ensure that all expenditure by the RSE licensee is in the best interests of members and for the purpose of the sound and prudent management of its business operations. Additionally, SPS 515 places heightened requirements on spending that is determined to be significant. APRA's intent with this requirement is to ensure there is a rigorous decision making process underpinning all expenditure, but in particular items of significant expenditure, and that the outcomes achieved from the spending are monitored and reviewed and consistent with providing quality outcomes for members.

Expenditure policies and procedures

44. APRA expects that an RSE licensee's expenditure policies would set out criteria to assist RSE licensee staff to interpret where expenditure may be inconsistent with the requirement that all expenditure is in the best interests of members and for the purpose of the sound and prudent management of the business operations. For example, a policy that covers travel expenses would be expected to detail criteria to ensure travel spending is appropriately being undertaken in the interests of members and in support of an RSE licensee's business operations.

45. APRA expects that controls and approval processes for fund expenditure would be set out in relevant policies and procedures to ensure an appropriate level of oversight. While the controls and delegations would differ based on the size and nature of the expenditure, the approval of items of spending would be based on the documented policy. For example, hospitality spending above a certain amount would need to be approved by a senior manager of the RSE licensee based on the set criteria.

Determining significant expenditure

46. SPS 515 has heightened requirements for the decision making associated with items of significant expenditure. Significance under SPS 515 is determined by the size of the expenditure or whether it is extraordinary in nature.

[5] Refer to *Prudential Standard SPS 250 Insurance in Superannuation*.

Size of expenditure

47. An RSE licensee would be expected to consider past experience with expenditure associated with projects or initiatives to determine a threshold or benchmark that indicates whether the expenditure is large in size. APRA expects the threshold would not solely be set by reference to the size of the RSE licensee's business operations, for example assets under management. Where the size of future expenditure is unknown, APRA expects the RSE licensee to take a conservative approach when estimating future payments in order to assess significance.

48. Projects or initiatives often involve a series of expenses that coincide with particular timeframes, project milestones or discrete project components. For example, different service providers contracted by the RSE licensee may undertake distinct components of a project over an extended period. While the payments may in isolation be relatively small, an RSE licensee would be expected to consider whether a series of smaller payments or ongoing expenditure is significant in total.

49. For the avoidance of doubt, an RSE licensee's spending on material service provision, such as administration and investment services, would generally be considered as significant by virtue of their importance to quality member outcomes. The approach to meeting the requirements for SPS 515 for these services, in conjunction with meeting other prudential requirements, is outlined below.

Extraordinary expenditure

50. APRA expects that extraordinary instances of expenditure will result from projects or initiatives that are unusual or infrequent. In many cases extraordinary spending will be linked to the pursuit of strategic objectives and the business plan; however, it is also intended to capture spending that is connected to events or circumstances that are unexpected and therefore may not be covered in the business plan or associated budgetary process.

51. Items of expenditure that may not necessarily be large in size may still be extraordinary in nature. For example, a specific marketing initiative or product design and implementation project could be extraordinary due to its connection to the RSE licensee's strategic objectives. APRA expects that expenditure associated with key initiatives under the business plan would be considered to be extraordinary.

52. APRA expects that a payment or series of payments made to a related party or associate, such as a parent entity, that is attributable to a specific one-off project or investment that is linked to the pursuit of the RSE licensee's strategic objectives, would be considered extraordinary in nature.

53. An RSE licensee may operate under a business model that enables a return (e.g. dividend) to be paid to a parent company. In such circumstances, APRA expects the RSE licensee would be able to demonstrate that the level of return is consistent with the provision of quality member outcomes.

Decision making

54. The Board of an RSE licensee would be expected to have comprehensive oversight of expenditure decisions that are significant. APRA expects that significant expenditure decisions would be approved by the Board and supported by a business case where necessary. APRA also expects that the RSE licensee would document the circumstances that would trigger a review of the expenditure, including whether it should take place. Where senior management has delegated authority to approve certain expenditure, APRA expects there to be appropriate reporting to the Board regarding the decisions taken under delegated authority.

55. An RSE licensee's largest ongoing items of expenditure are in most circumstances associated with investment management, administration, custodial services and the general operations of the RSE licensee. A number of these items may be provided by a service provider and in most cases will be subject to the material business activity requirements under *Prudential Standard SPS 231 Outsourcing* (SPS 231).

56. Where relevant, an RSE licensee may utilise the processes and documentation prepared under SPS 231 to assist it to satisfy the significant expenditure requirements. In particular, an RSE licensee that is able to demonstrate that it has comprehensively met the requirements under SPS 231 for entering into or renewing an outsourcing agreement, including a rigorous approach to assessing outsourcing operations, would be able to utilise this documentation to assist in meeting the significant expenditure requirements.

Monitoring outcomes

57. As part of demonstrating the rigour of decision making associated with significant expenditure, the RSE licensee must have metrics to monitor whether the expenditure is achieving its stated outcomes. APRA's view is that the metrics to monitor the outcomes as required under SPS 515 do not necessarily have to be distinct for each payment or project milestone; an overarching set of metrics may apply to the entire project or initiative. Further, APRA expects that, where the initiative associated with the significant expenditure is detailed in the business plan, any metrics used to monitor the performance of the initiative in accordance with the business plan are likely to be the same as those utilised to monitor the outcomes of the expenditure.

Use of reserves[6]

The reserves of an RSE are typically regarded as monies forming part of the net assets of the RSE that have been set aside for a clearly stated purpose. The use of reserves ultimately affects outcomes for members and therefore they must be managed in a consistent and equitable manner.

58. Reserves are typically held by an RSE licensee to address contingent events and equity issues between different classes of members or over time. It is important for an RSE licensee to be clear on the purpose of reserving funds before the reserve is established.

59. APRA expects that an RSE licensee would develop policies and processes to determine the need for reserves, as well as their size and management in the context of their purpose. The policies and processes would articulate the rationale for the establishment of the reserves and ongoing objectives and measures to manage the reserves.

60. Measures that APRA regards as sound reserve management include, but are not limited to:

    a) clear definition of the purpose, or purposes, of each reserve and the sources from which the reserve will be drawn or accumulated;
    b) setting the conditions for the use of reserve monies and limits on the amounts that may be transferred out of the reserve, including consideration of how payments from the reserve into members' accounts are made in a fair and equitable manner;
    c) determination by the RSE licensee of an appropriate target amount or range for each reserve, including how and over what period the reserves are to be initially established and subsequently replenished after a transfer from the reserve;
    d) determination by the RSE licensee of how it would respond in circumstances where a reserve has been exhausted or is insufficient to meet the cost of a contingent event, including whether and over what period, other assets of the RSE could be relied upon;
    e) where a reserve is specific to a particular sub-fund of an RSE, or a particular type of interest within an RSE or sub-fund, effective mechanisms to ensure that the reserve is quarantined to that sub-fund or type of interest;
    f) periodic review to ascertain that each reserve remains appropriate to the RSE's circumstances and that controls and procedures implemented by the RSE licensee ensure that reserves are used only for the intended purpose or purposes;
    g) a process by which the RSE licensee would determine that a reserve is in excess to requirements of the relevant policy for the management of the reserve, or no longer required, and the process to be followed to distribute the excess, for example, a cap on the size of the reserve and periodic monitoring as to the ongoing appropriateness of the cap level;

[6] This guidance applies generally to all reserves, but does not replace the requirements set in relation to reserves maintained for the purposes of satisfying the operational risk financial requirements in *Prudential Standard SPS 114 Operational Risk Financial Requirement* or associated guidance in *Prudential Practice Guide SPG 114 Operational Risk Financial Requirement*.

h) a process for recording the balance of each reserve, the movements in and out of the reserve and the purpose of the movements; and
i) reporting of reserves to APRA as required by reporting standards made under the *Financial Sector (Collection of Data) Act 2001*.

61. APRA expects that an RSE licensee's strategy for managing reserves would address how to equitably attribute the accumulation of reserves across different cohorts of members, including consideration of intergenerational issues. Appropriate and prudent management of reserves benefits all members of an RSE, even if the circumstances that would warrant use of the reserve do not eventuate during the membership of a particular cohort of members.

62. Reserves should not be used as a mechanism for transferring value between different cohorts of members. Where a reserve is established, it should be maintained for the collective benefit of all members through the provision of a funding mechanism to address risks or equity issues. For example, an investment reserve should not be used to smooth fluctuating returns that should properly be applied to an individual member or cohort of members.

63. Whilst reserves are monies that have not been allocated to members, not all unallocated monies constitute reserves. Unallocated monies that are not reserves include accounting constructs such as suspense accounts used to record contributions and rollovers pending their allocation to the accounts of specific fund members. Provisions for accrued administration expenses, taxation liabilities or other present costs would not be regarded by APRA as reserves for the purpose of this guidance. APRA's view is that items of this nature would not be classified as reserves for reporting purposes.

64. Where an RSE licensee has an insurance premium adjustment mechanism in place, such that an insurer returns a portion of the premium when the claims experience is better than what was expected at the time the premium was set, the prudent practice would be for such a mechanism to be managed through a specific insurance reserve. The reserve would only be used to meet insurance premium costs in future and should not be used for any other purpose.An RSE licensee's insurance reserve policy would ordinarily ensure appropriate, equitable and timely use of the insurance reserve for this purpose.

Attachment A - Examples of metrics

Examples of metrics that an RSE licensee may consider using to monitor progress against its business plan, include, but are not limited to:

Financial performance indicators
• target investment performance, including net returns relative to appropriate benchmarks over the medium and long term
• target net asset growth
• target cost or expense base, including average operating costs per member and average operating costs per active member
• target fee levels
• target liquidity measurements, including net outflow ratio
• target insurance product premiums and claim payment ratios for different cohorts and types of insurance, where appropriate
Membership indicators
• measures of member switching and the reasons for switching
• target levels of active and inactive members
• target levels of default employers or default members
• membership demographics, including, consideration of age, gender, account balance, employment status, retirement product preferences
• targets for member engagement through various channels, including utilisation by members of different communication channels
Business initiative indicators
• results of initiatives such as new/enhanced services or changes in benefits/product design and associated member take-up or other targets
Outsourcing arrangement indicators
• target performance by service providers
• target budget for outsourcing arrangements
• analysis on the availability of alternative service providers in the event of a price increase or service disruption
• analysis on the ability or potential ability of the RSE licensee to in-house functions currently undertaken by third parties

APRA