



AUSTRALIAN INSTITUTE of  
SUPERANNUATION TRUSTEES

29 May 2019

Ms Heidi Richards  
General Manager, Policy Development  
Australian Prudential Regulation Authority  
GPO Box 9836  
SYDNEY NSW 2001

**Email:** [superannuation.policy@apra.gov.au](mailto:superannuation.policy@apra.gov.au)

Dear Ms Richards,

**In brief:**

AIST submits that APRA's proposed changes to Prudential Standard SPS 515 do not properly align it with the recent member outcomes assessment legislation.

The promotion of the financial interests of members required by law must be reflected in the prudential standards, especially by giving primary consideration to the long-term net returns that deliver optimal retirement incomes to members.

AIST proposes amendments and calls for the development industry benchmarks to support the assessment process.

**APRA Consultation Letter – *Proposed revisions to Prudential Standard SPS 515 Strategic Planning and Member Outcomes***

The Australian Institute of Superannuation Trustees (AIST) welcomes the opportunity to respond to this consultation letter.

We strongly support the intent of the *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Act 2019* which amended the Superannuation Industry (Supervision) Act 1993 (**SIS Act**) by adding additional covenants relating to regulated superannuation fund's annual outcomes assessment. The amendments to the SIS Act require trustees to promote the financial interests of members. However, we do not believe the proposed revisions to Prudential Standard SPS 515 are sufficient to aligning it with the updated legislation.

The purpose of the *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Act 2019* is 'to ensure that trustees are promoting the financial interests of their members, which is expected to lead to an increase in the overall quality of products'. The revisions proposed by APRA do not promote the financial interests of members. Unless this misalignment is addressed, this will both create uncertainty about how an RSE licensee is able to comply with both the legislation and APRA's proposed requirements. Most importantly however, APRA's proposals will diminish and distract from the requirement on funds to promote the financial interests of members.

We believe that prudential standard must be amended to align with the legislation and must be more clearly subordinate to the legislation and reflect its intent.

### Primacy must be given to long-term net returns

We strongly recommend that the proposed prudential standards are updated to better reflect the prioritisation of long-term net returns. We believe that it is long-term net returns that are of critical importance to the retirement outcomes of all members. This is what the member receives – it is the most important contributor to optimising retirement income.

It is imperative that the proposed prudential standards are updated to reflect the intent of the amendments to the SIS Act. The intent of the legislation is for the promotion of members financial interests to be the primary consideration of regulated superannuation funds with particular focus on how the net returns promote the financial interests of beneficiaries, as highlighted in section 52 (12) of the SIS Act below.

*Covenants relating to regulated superannuation funds—**promoting financial interests of beneficiaries***

*(12) If the entity is a regulated superannuation fund (other than a regulated superannuation fund with fewer than 5 members), the covenants referred to in subsection (1) include a covenant by each trustee of the entity to promote the **financial interests of the beneficiaries of the entity who hold a MySuper product or a choice product, in particular returns to those beneficiaries (after the deduction of fees, costs and taxes)***

In contrast, the proposed SPS 515 20 (a) outlines that it is up to each RSE licensee to document the methodology applied in undertaking the annual outcomes assessment including the relevant weight given to each of the factors it must have regard to in making its overall determination(s) under section 52 (9) of the SIS Act.

We believe that this requirement is at odds with the legislation which requires an RSE licensee to promote the financial interests of beneficiaries with particular focus on net returns to those beneficiaries and has included these multiple factors, not to be considered in isolation but to be linked back to the promotion of a member's financial interest. This is highlighted in section 2.22 & 2.23 of the detailed explanation of the *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Act 2019*;

*2.22 The new outcomes test requires trustees to assess their MySuper or choice product in respect to a range of product features including their insurance and investment strategies, and compare how their product is performing against other products and benchmarks, using certain performance metrics.*

*2.23 In this regard, the outcomes test provides trustees with a framework for assessing their product offering to determine whether it is achieving its intended outcomes and how it may be improved. The framework for the outcomes test endeavours to support the trustee's primary obligation to promote the financial interests of their members, in particular the net returns to those members.*

The terminology using 'relative weight' in the proposed SPS 515 unnecessarily diminishes the role of promoting the financial interests of beneficiaries. We reiterate that as highlighted above, the legislative test is absolute and that the promotion of financial interest must be supported by, and not relatively reduced by other factors.

The requirement to have a multi-factor approach risks increasing complexity and reduces the ease of comparison. If, however, the multi-factor approach is overlaid by a primary requirement to prioritise net returns, this becomes much simpler to both understand and assess. We reiterate that it is not our position that long-term net returns should be considered 'to the exclusion of other considerations' but that other considerations are secondary, yet still very important considerations that are more qualitative and subjective measures. In contrast, long-term net returns are much harder to dispute than the mix of quantitative and qualitative measures proposed.

The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry<sup>1</sup> highlighted that some trustees have difficulty in understanding and applying the best interests covenant, by alleging complexity of the covenant and the need to consider all of the circumstances. The required multi-factor approach proposed by APRA only serves to further this

---

<sup>1</sup> Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, Volume 1 (2019), 226-7. Available from:

<https://www.royalcommission.gov.au/sites/default/files/2019-02/fsrc-volume-1-final-report.pdf>

complexity and adds a potential conflict between promoting the financial interests of members and other considerations.

*As quoted by Commissioner Kenneth Hayne, a trustee 'must do the best they can for the benefit of their beneficiaries, and not merely avoid harming them'. This can be achieved if a trustee keeps the best interests of beneficiaries 'front of mind' at all times. The case studies revealed that, all too often, trustees did not. Usually, they did not because a conflict arose between the beneficiaries' interests and the interests of the trustee or another person or entity. He later emphasises that the surest way to prevent a breach of the covenant is to avoid the potential conflict entirely.*

Throughout the Royal Commission, the Commissioner noted that that some financial institutions focused too much on the interests of the institution in seeking to achieve the 'right balance' between the institution and the super fund member. In fact, the Commissioner noted that the pursuit of members best interest was not to be balanced against the interests of the financial institution and was not to be diminished or diluted by other considerations.

Our recommendation for the multi-factor approach of the prudential standards to be subject to a primary requirement to prioritise net returns to members, would avoid any such conflict, and would remove the risk of a trustee balancing a member's financial interest with other considerations.

### **Superannuation system *currently* cannot be meaningfully benchmarked**

The proposed business performance review requires funds to compare outcomes against objective benchmarks. However due to differences in fee, cost and return disclosure the superannuation system *currently* cannot be meaningfully benchmarked. For funds to be able to meaningfully do this, there is a need for a comprehensive data reporting framework that articulates the information needed to benchmark fund and system performance, and whether members' financial needs are being met.

We believe that in order to ensure consistency and comparability benchmarking should be done at an industry level. This approach would be much more efficient and cost effective whilst also being a more robust and transparent process. The proposed SPS 515 which allows individually chosen benchmarks will be overtaken in any event by the development of a de facto or actual industry benchmark.

This approach is supported by the Productivity Commission recommendation *that the annual outcomes assessment should be supplemented by clear benchmarking requirements for all MySuper and Choice investment options*. This would remove the subjectivity of each RSE licensee choosing their own method of performance comparison.

In addition, AIST has consistently advocated that Choice reporting should be aligned with MySuper fees, costs and performance reporting. Extending the provision of an annual outcomes assessment to both MySuper and Choice funds is a positive step towards this alignment. We do however have some concerns that the Choice products will only be compared to other Choice products. Particularly when you consider that there are significant differences in future retirement outcomes between members of MySuper funds compared to other products in the Choice sector<sup>2</sup>. This viewpoint is supported by the detailed explanation of the *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Act 2019* shown below;

*Schedule 1 recognises that although the features of MySuper products and choice products differ, the obligation to undertake an annual outcomes assessments in respect of beneficiaries holding either MySuper products or choice products should be done in as similar a way as is possible, recognising that trustee obligations to members should apply irrespective of product type.*

This highlights the importance of an industry benchmark inclusive of both MySuper and Choice funds. At the end of the day – super is about retirement outcomes. Whether MySuper or Choice is the vehicle to do this, all members want the optimal retirement income. While products may take different routes to get there (e.g. different asset allocation), their ability to get there and the steps they are taking to promote members financial interests should be able to be easily compared.

We were pleased to see that APRA is commencing a significant review of its superannuation data collection and that this includes reviewing reporting standards to ensure that the current definitions are both suitable and can be interpreted more consistently, the level of materiality reflects the purpose for which the data is being collected and that there is appropriate coverage of both MySuper and Choice products. We recommend that work in this area is given significant priority so that the proposed member outcomes test can be meaningfully implemented.

Whilst we are supportive of APRA collecting more data on Choice products, we question what this means for the efficient division of powers between APRA and ASIC. Insufficient attention is paid to the categorisation of MySuper, Choice, platforms and investments options (both pre-mixed and member constructed). We believe that assessment of products at all levels is important and should proceed on the basis of little or no regulatory carveouts. Greater clarity is needed on what rules apply, to what products and the policy intent of this these reliefs.

---

<sup>2</sup> According to new research from Rice Warner, Australian workers who invest their super in funds outside the high performing MySuper sector could be as much as \$52.5 billion worse off in a decade's time. Available from: [http://www.aist.asn.au/media/1212739/analysis\\_of\\_mysuper\\_vs\\_choice\\_final.pdf](http://www.aist.asn.au/media/1212739/analysis_of_mysuper_vs_choice_final.pdf)

## Subjectivity in establishment of membership cohorts may not promote financial interests of all beneficiaries

Although we appreciate that establishing cohorts may assist an RSE licensee in understanding the performance of its operations, we believe that are risks and drawbacks of leaving it up to each RSE licensee to decide how to best segment their membership into meaningful cohorts.

Legislation requires an RSE licensee to promote the financial interests of beneficiaries with particular focus on net returns to those beneficiaries however by following the proposed SPS 515 (a) (ii) and having regard to the outcomes achieved for different cohorts of beneficiaries, relative to the outcomes sought and against objective benchmarks there is a risk that the net returns are not prioritised for all members.

The proposed standard implies that for some cohorts of beneficiaries, the primary focus is not long-term net returns and it is uncertain in this case how the financial interests of beneficiaries are being promoted as required by legislation. We believe that it is long-term net returns that are of critical importance to the retirement outcomes of all members.

The concern that an RSE licensee may put less effort into delivering the highest net return for all membership cohorts is supported by Productivity Commission findings;

*'In the choice segment, a proliferation of little used and complex products – some tens of thousands – increases fees without boosting net returns, and makes effective decision making elusive for most members. There is evidence that some members who use these products are unwittingly buying a degree of control over their super at the price of materially lower retirement incomes.'*

In addition to these issues, the requirement for each RSE licensee to determine how to best establish cohorts of beneficiaries risks duplicating the work required to be completed, which may increase both the time and cost burden to RSE licensees. An RSE licensee may be required to prepare a number of different annual outcome assessments, all of which need to be compared to relevant outcomes sought and relevant objective benchmarks.

This layer of subjectivity in establishment of cohorts will also make it more difficult to compare results with other RSE's and by allowing RSE licensees to decide how to establish cohorts there is an increased risk of manipulating results.

We do however support that product level assessment is required as we are concerned that poorly performing products will not receive adequate scrutiny by trustees. The December 2015 SPS 515 version clearly stated that as a minimum the RSE licensee had to consider each investment option offered however we note that this is no longer included in the proposed SPS 515.

There are an estimated 40,000 investment options across all APRA-regulated funds<sup>3</sup> – there is no evidence that every one of these is in the best interests of members. If trustees are required to assess each product and determine if they are delivering outcomes, then there are incentives for poorly performing products or those with high fees to no longer be offered to members.

#### **Unclear how defined benefits will be taken into account by APRA**

Further clarity is needed on whether the proposed annual outcomes assessment requirements of SPS 515 will apply to defined benefit products as previously required in the December 2018 SPG 516 – Outcomes Assessment Prudential Practice Guide.

This is in contrast to the *SIS Act* which requires an annual outcomes assessment of MySuper and Choice product offerings, whereby Choice products are defined as all products that are not MySuper products or defined benefit products.

AIST recommends that defined benefit funds should be excluded from the proposed annual outcomes assessment requirements as per legislation intent. Defined benefit funds differ substantially from accumulation style funds, and the outcome that members receive differs depending on their employment, years of service and the retirement formula applied.

#### **Reintroduce the need to consider basis for setting fees**

We advocate that the basis for setting fees should be reintroduced in the assessment in determining if the financial interest of beneficiaries of the RSE licensee who hold a MySuper product or choice product are being promoted. We recommend that this is added as an additional consideration in SPS 515 (21).

This is an important component of the member outcomes test value proposition. We advocate that the basis for setting fees should also clearly apply to both MySuper and Choice products and investment options, which on average, charge higher fees.

As highlighted in our response to CP 308: Review of RG 97<sup>4</sup>, we believe that fees and costs must be able to be meaningfully compared by members. However this remains difficult due to key

---

<sup>3</sup> Productivity Commission Inquiry Report, Superannuation: Assessing Efficiency and Competitiveness (2018), 203-4. Available from:

<https://www.pc.gov.au/inquiries/completed/superannuation/assessment/report/superannuation-assessment.pdf>

<sup>4</sup> AIST, Response to Consultation Paper 308: Review of RG 97 Disclosing fees and costs in PDSs and periodic statements (2019). Available from [http://www.aist.asn.au/media/1294746/submission\\_cp\\_308.pdf](http://www.aist.asn.au/media/1294746/submission_cp_308.pdf)

issues around fee disclosure consistency and transparency. Including the basis for setting fees in the annual outcomes assessment would be a step towards addressing these issues.

### **Concerns regarding possible requirement to appoint an independent expert**

We have concerns regarding how the provisions of clause 16 in the proposed SPS 515 would operate:

*APRA may require an RSE licensee, by notice in writing, to appoint an appropriate independent expert to provide to APRA a report on a particular aspect of an RSE licensee's business performance review, within a timeframe agreed to by APRA. An RSE licensee must bear the costs of such an appointment.*

We note that there remains no guidance in the proposals as to how this would work. If this remains in SPS 515, AIST strongly recommends that a series of criteria be included in the guidance. For example:

- APRA may appoint an independent person only in cases where it reasonably believes the RSE licensee does not have sufficient capabilities to undertake the work.
- APRA has provided prior notice to the RSE licensee as to its concerns. This would provide an opportunity for the RSE licensee to address the concerns.

Given the expanded responsibilities of APRA and in light of the increased size and complexity of the superannuation sector, we are supportive of proposals to provide additional resources to APRA on a risk weighted basis.

### **Implementation should be delayed**


APRA has proposed to maintain the commencement date of SPS 515 as 1 January 2020. We challenge the presumption that the overall substance of requirements for RSE licensees in revised SPS 515 are unchanged and we recommend that given the numerous concerns identified above that implementation is delayed by 6 months.

Another important consideration and reason for the delay is that regulations in relation to the SIS Act amendments have not yet been released and finalised, therefore we believe the proposed timing for implementation of SPS 515 is pre-emptive.



For further information regarding our submission, please contact Zach Tung, Policy and Regulatory Analyst on [REDACTED] or at [REDACTED]

Yours sincerely,

  
[REDACTED]

Eva Scheerlinck  
**Chief Executive Officer**

*The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.*

*As the principal advocate and peak representative body for the \$1.3 trillion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.*

*AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.*

## Appendix: AIST recommended revisions to Prudential Standard SPS 515 Strategic Planning and Member Outcomes

Our recommended changes to SPS 515 are summarised below;

### Business performance review

Page | 10

14. An RSE licensee's business performance review must include:

(a) analysis of its performance in achieving its strategic objectives, having regard to:

(i) the results of its monitoring of its business plan required under paragraph 12;

~~(ii) the outcomes achieved for different cohorts of beneficiaries (such that all beneficiaries are covered), relative to the outcomes sought, and against objective benchmarks; and~~

(iii) the outcomes assessment under section 52(9) – (13) of the SIS Act.

(b) the key factors identified by the RSE licensee as having affected the results of the analysis under 14(a); and

(c) the RSE licensee's conclusions as to whether it achieved, and will continue to achieve:

~~(i) promoting the financial interests of beneficiaries, in particular matters affecting returns to beneficiaries;~~

~~(ii) the outcomes it seeks for beneficiaries; and~~

(iii) the sound and prudent management of its business operations.

15. If the RSE licensee determines that changes to its business operations would likely improve the outcomes for beneficiaries or the sound and prudent management of its business, the RSE licensee must reflect those changes in its business plan.

16. APRA may require an RSE licensee, by notice in writing, to appoint an appropriate independent expert to provide to APRA a report on a particular aspect of an RSE licensee's business performance review, within a timeframe agreed to by APRA. An RSE licensee must bear the costs of such an appointment.

~~APRA may appoint an independent person only in cases where it reasonably believes the RSE licensee does not have sufficient capabilities to undertake the work.~~

## Annual outcomes assessment

20. An RSE licensee must, at a minimum, document the methodology applied in undertaking the annual outcomes assessment under section 52(9) of the SIS Act, including:

(a) how each product continues to meet the primary obligation to promote the financial interest of beneficiaries of the fund , in particular matters affecting returns to beneficiaries;

(b) the relative weight given to each of the other factors it has had regard to in making its overall determination(s) under sections 52(9) - (13) of the SIS Act and how they promoted the financial interest of beneficiaries; and

(d) how the RSE licensee has determined the comparable choice products under the SIS Regulations for the purposes of undertaking the annual outcomes assessment.

21. Pursuant to section 52(11)(e) of the SIS Act, in determining whether the financial interests of the beneficiaries of the RSE who hold a MySuper product or choice product are being promoted, an RSE licensee must also assess the following matters:

(a) whether because of the scale of, and within, the RSE licensee's business operations, those beneficiaries are disadvantaged;

(b) whether the operating costs of the RSE licensee's business operations are inappropriately affecting the financial interests of those beneficiaries;

(c) the basis for the setting of fees; and

(d) each investment option offered by the RSE licensee to be considered.