



**CHARTERED SECRETARIES
AUSTRALIA**

Leaders in governance

27 February 2013

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General Manager, Policy Development
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By email: superannuation.policy@apra.gov.au

Dear Mr Grummitt

Discussion paper: Prudential guidance for superannuation

Chartered Secretaries Australia (CSA) is the peak body for over 7,000 governance and risk professionals. It is the leading independent authority on best practice in board and organisational governance and risk management. Our accredited and internationally recognised education and training offerings are focused on giving governance and risk practitioners the skills they need to improve their organisations' performance.

Members of CSA are all involved in governance, corporate administration, legal practice and regulatory compliance and have a thorough working knowledge of applied governance, including matters such as board composition and renewal, director independence and risk management frameworks and are frequently charged with the responsibility of advising boards on these matters, both within companies and superannuation entities. The introduction of the prudential standards will therefore affect those CSA Members directly who are involved with providing advice and implementing the regulatory and governance frameworks in their organisations. Our Members' expertise is also useful in dealing with the applied aspects of the prudential standards.

CSA welcomes the Australian Prudential Regulation Authority's (APRA's) Discussion Paper: *Prudential guidance for superannuation* (the discussion paper) and the accompanying draft prudential practice guides which have been provided for comment. CSA draws on the experience of our Members in formulating our response.

General comments

CSA notes the amendment to the Superannuation Industry (Supervision) Act 1993 (the SIS Act) in September 2012 to provide APRA with a prudential standards-making power for prudentially regulated superannuation entities. CSA strongly supports the introduction of prudential standards for superannuation funds and recognises the importance of providing practical guidance for superannuation entities seeking to understand and abide by the new regulatory framework.

The proposed prudential practice guides (PPGs) form an important component of the superannuation reform process. CSA is cognisant that the superannuation industry has had a long and complex development. As part of the reform of the regulation of superannuation funds,

the prudential standards provide a central reference point for all organisations within the industry regardless of shape, size and complexity.

In this regard, CSA commends the flexibility which has been written into the guides to allow RSE licensees to be able to meet the standards according to their requirements. The capacity for superannuation entities to engage with the prudential standards and PPGs, and make a decision on whether or not to adopt specific practices, find and implement alternatives where appropriate, and also document the reasons for particular decisions, will result in improved governance frameworks, as each entity must work through the issues in relation to the particularities of the individual organisation.

Nonetheless, there will be implications for RSE licensees seeking to comply with the prudential standards, and while CSA recognises that the PPGs do not create enforceable requirements, RSE licensees will still incur costs in implementing various controls. CSA believes that the incursion of costs, while not unexpected, should be highlighted to RSE licensees in the PPGs.

CSA recommends, therefore, that the final paragraph in the 'About this guide' section of each of the PPGs should be revised to state the following, or words to the effect:

Not all of the 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. Some of the practices specified in this guide might also incur additional costs to a RSE licensee, and consideration should be given to the potential for these costs to affect the returns provided to a RSE licensee's members.

CSA strongly commends the PPGs as a good source of practical guidance for superannuation entities. CSA believes that the practical guidance should be highlighted to RSE licensees as an educative tool to assist superannuation entities with their governance and compliance obligations. CSA notes that taking this approach will be just as important as enforcing the prudential standards, and that where possible, different types of practices, and greater clarity on expectations should be built into the guidance for superannuation entities.

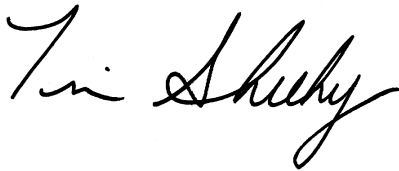
CSA highlighted in our submission to Treasury on the Exposure Draft – Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Bill 2012 that the requirement to publish a product dashboard and other information, including the remuneration of directors and executive officers, would help the transparency and accountability of superannuation entities. However, we also reinforced that the disclosure process should emphasise quality, not quantity. The disclosure of multiple facts does not of itself promote transparency.

Instead, there needs to be an emphasis on promoting the disclosure of meaningful information, whether to the public, through the product dashboard, or to APRA, as required by the prudential standards. This will require comprehensive engagement by RSE licensees with both the legislative and prudential frameworks, and an understanding of the responsibilities which subsequently arise. CSA reiterates that it is important, therefore, that the PPGs adequately reflect the intentions of the prudential standards but also provide assistance with complying with the broader context of the reform agenda. CSA recognises that the changes to the superannuation industry extend beyond simply the introduction of the prudential standards.

As such, CSA's attached submission focuses on both the language used to convey the RSE licensee's obligations, and highlighting the issues which RSE licensees need to consider in developing their practices and procedures for compliance with the prudential regulatory framework.

We would welcome the opportunity to discuss any of our views in greater detail.

Yours sincerely

A handwritten signature in black ink, reading "Tim Sheehy". The signature is written in a cursive, flowing style with a large initial "T" and a long, sweeping underline.

Tim Sheehy
CHIEF EXECUTIVE

Draft Prudential Practice Guide — SPG 510 — Governance

A sound and effective governance framework for a RSE licensee allows the entity to conduct its affairs with a high degree of integrity, transparency and accountability. A competent board is paramount to achieving this aim.

Board committees, similarly, play an important role in overseeing some of the critical functions of the board, such as audit, risk and nominations, and ensuring that the board is performing its oversight role. For example, a typical board remuneration committee will provide support and advice to the board on

- the level and composition of remuneration
- disclosure of remuneration policies, level and mix of remuneration, and
- the process for setting remuneration and assessing performance.

The structure of the superannuation industry, however, means that the remuneration committee of a RSE licensee plays a vitally important role in identifying conflicts of interest for directors who may also receive payments from outside the RSE licensee. In this regard, CSA strongly supports the requirement for prudentially regulated superannuation entities to have a remuneration committee which captures all forms of remuneration, regardless of where, or from whom, the remuneration is sourced.¹

In light of the added complexity of remuneration processes for directors and trustees within superannuation entities, **CSA recommends** that a further sentence describing the added dimension of the board remuneration committee's role be inserted in to paragraph 13 of SPG 510.

CSA notes further in relation to board committees that SPG 510 could be expanded to provide to RSE licensees with more information about the process for establishing and monitoring board committees. **CSA recommends**, therefore, the replacement of paragraph 16 of SPG 510 with the following:

- X. The board should be responsible for establishing and determining the committee membership, and it would be prudent practice for the committee to have a clearly defined charter setting out its role, responsibilities, composition, authority, tenure, structure, membership requirements, quorum, and reporting requirements. The committee should have sufficient members to adequately discharge their responsibilities with at least one member of the committee demonstrating relevant expertise and experience in dealing with the matters for which the committee has responsibility. The charter of the committee should be regularly reviewed and the skills and experience of those appointed to the committee should also be reviewed (see Board performance assessment).
- X. It would also be prudent practice for the board committee to report regularly to the board. A committee should consider all or a mix of the following:
 - keeping minutes of their meetings and including these (whether in draft form or signed) in the papers for the next full board meeting after each committee meeting
 - ensuring that the chairman of the committee provides a brief summary of the committee meeting at the next full board meeting after each committee meeting or on a less frequent basis (as required)
 - providing an annual report to the board, containing and reporting on all matters relevant to the committee's role and responsibilities as set out in the committee's charter (or terms of reference), including comment on

¹ Australian Prudential Regulation Authority 'Prudential Standard SPS 510 – Governance', paragraph 23, available from <http://www.apra.gov.au/Super/PrudentialFramework/Pages/superannuation-prudential-standards.aspx>

- the charter, the committee's operation and the membership composition, and/or
- making copies of the papers considered by the committee available to all directors, by request to the company secretary.

In line with the aforementioned recommendation, and the terms of the Prudential Standard SPS 510 on Governance (SPS 510), **CSA also recommends** replacing paragraph 22 with the following:

- X. SPS 510 requires the board to assess its performance and that of individual directors relative to its objectives on an annual basis.² It is recommended that the board also assess the performance of any board committees. In undertaking this assessment, a well-functioning board would typically consider and document the objectives that it sets for the Board collectively, its committees and for individual directors.

CSA is cognisant that SPS 510 only requires board performance assessments to be made of the board collectively and individual directors; however, CSA notes that SPS 510 also requires RSE licensees to form various board committees, such as an audit committee and a remuneration committee. CSA strongly encourages, therefore, APRA to consider including the above wording to ensure that RSE licensees monitor and utilise their board committees to assist the board's oversight of the superannuation entity.

CSA also notes the guidance offered in relation to external board assessments, identified in paragraph 25 of SPG 510, in which APRA specifically asks RSE licensees to undertake an external board assessment at least once every three years. While CSA supports the intention of the requirement to encourage RSE licensee boards to undertake external assessments regularly, There is no similar requirement in either paragraph 35 of Prudential Standard CPS 510 on Governance³, or the related Prudential Practice Guide APG 510 on Governance⁴, which applies to all other authorised deposit taking institutions (ADIs). Similarly, CSA also notes that the Australian Securities Exchange (ASX) Corporate Governance Council's *Corporate Governance Principles and Recommendations* (the Principles and Recommendations) does not mandate a three-year external board assessment process for listed companies.

In line with our earlier comments as to the provision of flexibility in the guidance, although SPG 510 presents a higher standard beyond that applied to other entities in the financial services sector or public listed companies in relation to externally-facilitated board assessment, CSA is of the view that this is appropriate, as it is provided as guidance in relation to sound practice and is not an enforceable requirement.⁵ CSA is of the view that the guidance is likely to result in improved governance practices and greater clarity about board renewal for superannuation entities. However, we note that there is no explanation in SPG 510 as to why APRA would expect to see board assessment facilitated externally every three years. **CSA recommends** therefore that APRA clarify the rationale for why external board assessments should be undertaken every three years, including the benefits that can accrue to this.

CSA also recommends that further clarity be provided to paragraph 26 of SPG 510, to ensure that it is clear that the requirements being set out apply only to the policy governing the assessment of

² A cross reference to paragraph 19 of Prudential Standard SPS 510 – Governance should be inserted to ensure that the RSE licensee is aware that the annual assessment is a prudential requirement

³ Australian Prudential Regulation Authority 'Prudential Standard CPS 510 – Governance', paragraph 35, available from <http://www.apra.gov.au/adi/PrudentialFramework/Pages/prudential-standards-and-guidance-notes-for-adis.aspx>

⁴ Australian Prudential Regulation Authority 'Prudential Practice Guide APS 510 – Governance', paragraphs 20-22, available from <http://www.apra.gov.au/adi/PrudentialFramework/Pages/authorised-deposit-taking-institutions-ppgs.aspx>

⁵ Australian Prudential Regulation Authority 'Discussion Paper: Prudential Guidance for Superannuation' Chapter 2, p. 8, available from [http://www.apra.gov.au/Super/PrudentialFramework/Documents/Discussion-Paper-Prudential-guidance-for-superannuation-\(Dec-12\).pdf](http://www.apra.gov.au/Super/PrudentialFramework/Documents/Discussion-Paper-Prudential-guidance-for-superannuation-(Dec-12).pdf)

board performance, and not to the policy which applies to executive assessment. **CSA recommends** that the opening sentence of paragraph 26 be replaced by the following:

- X. APRA expects that a Board would ordinarily have in place a document policy on board performance assessments which includes...

CSA is cognisant that the nomination and appointment of member and employer representatives poses many problems for RSE licensee boards. CSA recognises that many boards of superannuation entities are comprised of an equal number of directors appointed by either an employee body (a union) or employer body or, in the case of public-sector funds, a state or federal government.

As such, **CSA recommends** that a cross reference to Prudential Practice Guide – SPG 521 – Conflicts of Interest should be inserted at the end of paragraph 29 of SPG 510.

Draft Prudential Practice Guide — SPG 520 — Fit and Proper

CSA supports the broad concept underlying the fitness and propriety standards which require a RSE licensee to be responsible for ensuring that the responsible persons of the entity are fit and proper for the role.

CSA notes that paragraph 14 of SPG 520 captures this requirement by requiring members of the board collectively and individually to satisfy the fit and proper requirements. CSA is concerned, however, that the wording of paragraph 4 may inadvertently discourage superannuation entities from seeking and recruiting less experienced or qualified board members as part of their succession planning process, as strict compliance with SPG 520 would require that a responsible person's skills, knowledge and expertise are among the characteristics required to determine their fitness and propriety.

Again, CSA is aware that there is no equivalent of paragraph 4 inserted into either the Prudential Practice Guide – APG 520 – Fit and Proper, or the Prudential Standard – CPS 520 – Fit and Proper for ADIs. CSA is also cognisant that the Prudential Standard – SPS 520 – Fit and Proper also refers only to 'persons' acting in responsible person positions, and not the collective board.⁶

In order to ensure that RSE licensees properly consider their board renewal and succession planning procedures, **CSA recommends** that paragraph 4 be redrafted to provide RSE licensees with assurance that the employment of less qualified or less experienced board members as part of a succession planning arrangement will not adversely impact upon the declarations required under paragraphs 58 – 60 of SPG 520.

CSA also recommends the redrafting of paragraph 16 to emphasise the importance of documenting any training and induction considered necessary for responsible persons within the superannuation entity. While the current wording suggests that a RSE licensee 'might' consider documenting training and induction processes, CSA believes that RSE licensees 'should' be encouraged to document their processes.

Further clarity should also be provided in respect of the persons whom APRA has identified as being disqualified from holding responsible person positions within superannuation entities. CSA notes that the Australian Securities and Investments Commission (ASIC) currently maintains a register of disqualified persons on their website which informs companies about people who have been disqualified from being involved in the management of a corporation, or banned from practising in particular industries. **CSA recommends** a similar register of disqualified persons be kept by APRA and made publicly available on the APRA website.

⁶ Australian Prudential Regulation Authority 'Prudential Standard SPS 520 – Fit and Proper', paragraph 6, available from <http://www.apra.gov.au/Super/PrudentialFramework/Pages/superannuation-prudential-standards.aspx>

Draft Prudential Practice Guide — SPG 521 — Conflicts of Interest

As noted above, remuneration practices for RSE licensees can reveal issues of conflict for board members. The amendments to the SIS Act and legal framework, including the requirements to publish a product dashboard and executive remuneration information will also ensure that there is greater scrutiny of remuneration practices within superannuation entities. However, CSA believes that SPG 521 could be redrafted to provide RSE licensees with further information about how they can ensure compliance; that is, how they can keep information up to date, as required by the regulations. **CSA recommends**, therefore, that paragraph 6 of SPG 521 be amended to include a further sentence which states the following, or words to the effect that:

in order to keep information published in accordance with the SIS regulations up to date, the RSE licensee should consider undertaking an annual review of all the information to check for accuracy, currency and conciseness

CSA notes further that APRA expects a RSE licensee to implement processes to ensure that directors appointed by a sponsoring body are cognisant of their duties to the RSE licensee and the beneficiaries of the superannuation entity. A nominee director/trustee is often appointed to the board of a superannuation entity by, and to represent the interests of, an appointer. They are often appointed to control or influence, as well as monitor, the activities of the superannuation fund to which they are appointed. CSA notes that there have been many prominent examples where a director/trustee has been placed on the board of a superannuation entity by the government or a union, with the intention of influencing the operation of the entity.

CSA believes that nominee directors should be explicitly reminded of their legal obligations as well as the expectations of both their appointer and the superannuation entity to which they are appointed with respect to their conduct as a director, including, for example the fact that they represent all investors and not just their appointers.

CSA has written governance guidance on the issues to consider when developing a policy on directors appointed by sponsoring bodies⁷, as well as on the issues to consider in developing a policy on conflicts of interest⁸, and copies of these guides are attached to our submission.

Draft Prudential Practice Guide — SPG 220 — Risk Management

CSA supports the guidance issued in respect of SPG 220 and seeks to make comment on only one aspect of the guide.

CSA notes that paragraph 67 of SPG 220 requires a RSE licensee to notify APRA of material changes to the size, business mix and complexity of the superannuation entity's business operations, however, the guide provides no further information about the expected timelines for advising APRA of the aforementioned material changes.

CSA strongly recommends that further clarification be provided to paragraph 67 to provide RSE licensees with guidance on acceptable timeframes for the notification of material changes to the business.

⁷ Chartered Secretaries Australia, 'Good Governance Guide: 'Issues to consider when developing a policy on directors appointed by sponsoring bodies', available from <http://www.csaust.com/knowledge-resources/good-governance-guides.aspx>

⁸ Chartered Secretaries Australia, 'Good Governance Guide: 'Issues to consider when developing a policy and process for managing conflicts of interest for a superannuation entity', available from <http://www.csaust.com/knowledge-resources/good-governance-guides.aspx>

As changes to a superannuation entity's outsourcing processes would also be captured within the provisions of paragraph 67, **CSA also recommends** that a footnote which references the specific requirements of Prudential Practice Guide – SPG 231 – Outsourcing (SPG 231) should also be included at the end of paragraph 67. The footnote should highlight that further guidance on reporting to APRA concerning changes to outsourcing processes is captured in SPG 231.

Draft Prudential Practice Guide — SPG 232 — Business Continuity Management

CSA does not wish to make any comments on Prudential Practice Guide – SPG 231 – Business Continuity Management, and leaves it to other organisations to comment.

Draft Prudential Practice Guide — SPG 530 — Investment Strategy - Formulation

CSA recognises the importance of a RSE licensee identifying and approving the investment objectives of their investment options. A robust investment governance framework enables a RSE licensee to prudently manage investment risks that arise from the complexities of investment decision making.

The key aspect of the prudential standard on investment governance is ensuring that there is clarity surrounding the range and options of investments which are available to members.

CSA believes that paragraph 4 of SPG 530 should be amended to ensure that the advice to RSE licensees is clear concerning the circumstances when it will seek external advice in relation to the formulation of an investment strategy. Paragraph 4 currently requires the RSE licensee to 'articulate' the circumstances for seeking external advice, but does not state to whom the articulation should occur. CSA believes that documenting of the process for seeking external advice should be an internal trigger for superannuation entities and not a matter for reporting by the RSE licensee. As such, **CSA recommends** that the word 'articulate' be replaced with the word 'document' in paragraph 4. The sentence should read, therefore, as follows:

... An RSE licensee would be expected to *document* the circumstances when it will seek external advice in relation to the formulation of an investment strategy, and the process by which it would do so (emphasis added).

Clarification is also sought concerning the interaction of paragraphs 9, 30, 31 & 36 where a RSE licensee offers a single security or single sector option to beneficiaries. While paragraph 9 considers a single security option appropriate after due consideration, paragraph 30 notes:

where an RSE licensee has offers a single security option, that option is clearly not diversified. The SIS Act requires, however, that investment options offered by an RSE licensee must ensure a beneficiary is provided with a sufficient range of investment to be able to construct an adequately diversified portfolio with an appropriate mix of assets.

Paragraphs 31 and 36 provide some context for a RSE licensee wishing to choose to offer a single sector or single security option, however, the clear subtext is that APRA will not likely endorse a single security option, as the beneficiary's investment mix and the lessened access to liquidity will mean that a single security option will not be a viable product for a RSE licensee to offer.

While CSA agrees that only in very limited circumstances would a single sector or single security investment be appropriate, the guidance which has been drafted does not convey a clear message to RSE licensees.

CSA recommends that APRA consider re-phrasing the guidance concerning single security options to ensure that RSE licensee should only consider this approach in limited circumstances where the RSE licensee has given due regard to the beneficiary's investment mix, how liquidity will be managed, and whether or not the single security option meets investment objectives.

Draft Prudential Practice Guide — SPG 531 — Investment Strategy – Implementation

CSA does not wish to make any comments on Prudential Practice Guide — SPG 531 — Investment Strategy – Implementation, and leaves it to other organisations to comment.

Draft Prudential Practice Guide — SPG 114 — Operational Risk Financial Requirement

CSA notes that the Operational Risk Financial Requirement (ORFR) forms an integral component of the risk management framework of the RSE licensee, providing direction and guidance on the maintenance of adequate financial resources to address operational risks. CSA supports the guidance provided in SPG 114.

However, CSA also believes that some further clarification can be provided in respect of paragraph 40 which requires a RSE licensee to maintain records of a 'near miss incident'.

CSA is unsure whether the RSE licensees will fully understand the terminology of a 'near miss incident' without further guidance on the types of records which should be kept, and the relevant standard which APRA will consider appropriate for documenting such events.

CSA recommends that further guidance on what constitutes a 'near miss incident' should be provided in the guide.

Draft Prudential Practice Guide — SPG 231 — Outsourcing

CSA does not wish to make any comments on Prudential Practice Guide — SPG 231 - Outsourcing, and leaves it to other organisations to comment.

Draft Prudential Practice Guide — SPG 250 — Insurance in Superannuation

CSA does not wish to make any comments on Prudential Practice Guide — SPG 250 — Insurance in Superannuation, and leaves it to other organisations to comment.