



Superannuation (prudential standard) determination No. 8 of 2012

Prudential Standard SPS 530 Investment Governance

Superannuation Industry (Supervision) Act 1993

I, Ross Jones, delegate of APRA, under subsection 34C(1) of the *Superannuation Industry (Supervision) Act 1993* (the Act), DETERMINE *Prudential Standard SPS 530 Investment Governance* in the form set out in the Schedule, which applies to all RSE licensees.

This instrument commences on 1 July 2013.

Dated: 15 November 2012

[signed]

Ross Jones
Deputy Chair

Interpretation

In this instrument:

APRA means the Australian Prudential Regulation Authority.

RSE licensee has the meaning given in section 10(1) of the Act.

Note 1 It is a condition imposed on all RSE licences that the RSE licensee and, if the RSE licensee is a group of individuals, each of the members of the group, must comply with the RSE licensee law [section 29E(1)(a)]. RSE licensee law includes the prudential standards [section 10(1)]. APRA may direct an RSE licensee to comply with a specified condition of its RSE licence by a specified time if APRA has reasonable grounds to believe that the RSE licensee has breached the condition [section 29EB]. A failure to comply with a direction may lead to cancellation of the RSE licence [section 29G] and may be an offence attracting a penalty of 60 penalty units [section 29JB].

Schedule

Prudential Standard SPS 530 Investment Governance comprises the 7 pages commencing on the following page.



Prudential Standard SPS 530

Investment Governance

Objectives and key requirements of this Prudential Standard

This Prudential Standard establishes requirements for an RSE licensee to implement a sound investment governance framework and to manage investments in a manner consistent with the interests of beneficiaries.

The Board of an RSE licensee is ultimately responsible for having an investment governance framework for the selection, management and monitoring of investments that is appropriate to the size, business mix and complexity of the RSE licensee's business operations. This investment governance framework must include the investment strategies for the whole of each RSE, and for each investment option, as required by the *Superannuation Industry (Supervision) Act 1993*.

The key requirements of this Prudential Standard are that an RSE licensee must:

- formulate specific and measurable investment objectives for each investment option, including return and risk objectives;
- develop and implement an effective due diligence process for the selection of investments;
- determine appropriate measures to monitor the performance of investments on an ongoing basis;
- review the investment objectives and investment strategies on a periodic basis; and
- formulate a liquidity management plan.

Authority

1. This Prudential Standard is made under section 34C of the *Superannuation Industry (Supervision) Act 1993* (SIS Act).

Application

2. This Prudential Standard applies to all registrable superannuation entity (RSE) licensees (RSE licensees) under the SIS Act.¹
3. All RSE licensees must comply with this Prudential Standard in its entirety, unless otherwise expressly indicated.
4. This Prudential Standard commences on 1 July 2013.

The role of the Board

5. An RSE licensee is ultimately responsible for the sound and prudent management of the investments of each RSE within the RSE licensee's business operations.²
6. The Board of an RSE licensee (the Board³) must, for the RSE licensee's business operations, at a minimum:
 - (a) approve investment objectives for each investment option offered in each RSE;
 - (b) approve an investment strategy, in respect of each RSE, that reflects the RSE licensee's duties to beneficiaries, including those in section 52(6) and Division 6 of Part 2C of the SIS Act, as relevant, and this Prudential Standard:
 - (i) for the whole of that RSE; and
 - (ii) in respect of each investment option offered in that RSE;
 - (c) monitor and assess regularly whether the investment objectives are being met; and
 - (d) take appropriate and timely action regarding information contained in reports to the Board on investment matters.

¹ For the purposes of this Prudential Standard, 'RSE licensee' has the meaning given in section 10(1) of the SIS Act.

² For the purposes of this Prudential Standard, an 'RSE licensee's business operations' includes all activities as an RSE licensee (including the activities of each RSE of which it is the licensee), and all other activities of the RSE licensee to the extent that they are relevant to, or may impact on, its activities as an RSE licensee.

³ For the purposes of this Prudential Standard, a reference to 'the Board' is a reference to the Board of directors or group of individual trustees of an RSE licensee and 'group of individual trustees' has the meaning given in section 10(1) of the SIS Act.

RSE licensees that are part of a group⁴

7. Where an RSE licensee is part of a corporate group, and the RSE licensee utilises group policies or functions, the Board must approve the use of group policies and functions and must ensure that these policies and functions give appropriate regard to the RSE licensee's business operations.

Investment governance framework

8. An RSE licensee must at all times have an investment governance framework to manage investments to meet the RSE licensee's obligations to beneficiaries.⁵
9. An investment governance framework is the totality of systems, structures, policies, processes and people to address the RSE licensee's responsibilities with regard to investments of each RSE within the RSE licensee's business operations. This includes generating returns to meet investment objectives while managing and monitoring all identified sources of investment risk.⁶
10. The Board is ultimately responsible for the investment governance framework.
11. An RSE licensee's investment governance framework must, at a minimum, include:
 - (a) investment objectives for each investment option offered by the RSE licensee;
 - (b) a methodology for determining investment reporting measures⁷;
 - (c) the investment strategy for the whole of each RSE and for each investment option as required by section 52(6) of the SIS Act;
 - (d) all Board policies relating to investment activities;
 - (e) role statements that include the details of each role's responsibilities and reporting structures for all roles related to investment activities;
 - (f) structures, policies and processes for investment performance and risk measurement, assessment and reporting; and
 - (g) a review process to ensure that the investment governance framework remains effective.

⁴ For the purposes of this Prudential Standard, a reference to 'a group' is a reference to a group comprising the RSE licensee and all connected entities and all related bodies corporate of the RSE licensee, 'connected entity' has the meaning given in section 10(1) of the SIS Act and 'related body corporate' has the meaning given in section 50 of the *Corporations Act 2001*.

⁵ For the purposes of this Prudential Standard, a reference to 'beneficiaries' is a reference to 'beneficiaries of an RSE within the RSE licensee's business operations'.

⁶ An RSE licensee's investment governance framework must reflect the risks associated with investments as a material risk area identified in *Prudential Standard SPS 220 Risk Management*.

⁷ An RSE licensee's methodology for determining the investment reporting measures must also support compliance with relevant reporting standards made under the *Financial Sector Collection of Data Act 2001*.

12. An RSE licensee's investment governance framework must be appropriate to the size, business mix and complexity of the RSE licensee's business operations.
13. An RSE licensee must have procedures to ensure that all persons in roles related to investment activities of the RSE licensee are made aware of, and have processes and controls for monitoring compliance with, the RSE licensee's investment governance framework.

Review of the investment governance framework

14. An RSE licensee must ensure that the appropriateness, effectiveness and adequacy of its investment governance framework are subject to a comprehensive review by operationally independent, appropriately trained and competent persons at least every three years.
15. The scope of the review of an RSE licensee's investment governance framework must have regard to the size, business mix and complexity of the RSE licensee's business operations, the extent of any change to those operations and any changes to the external environment in which the RSE licensee operates.

Investment objectives

16. An RSE licensee must, when formulating the investment strategy for each investment option, set investment objectives that are:
 - (a) aligned with the size, business mix and complexity of the RSE from which the investment option is offered; and
 - (b) specific and measurable and, at a minimum, include:
 - (i) a return objective; and
 - (ii) a risk objective.

Formulating the investment strategy

17. When formulating each investment strategy for the whole of the RSE, and for each investment option, an RSE licensee must document how it has regard to each of the factors in section 52(6) of the SIS Act.
18. An RSE licensee must, when determining an appropriate level of diversification for each investment strategy⁸:
 - (a) identify the risk factors, and sources of return with which the risk factors are associated;
 - (b) where the strategy includes multiple assets and/or asset classes, identify how sources of returns are expected to interact, the variability in these

⁸ As required in section 52(6)(a)(ii) of the SIS Act.

interactions and the impact of these interactions on the overall diversification of the strategy in different market conditions;

- (c) determine the target exposure to the risk factors in paragraph 18(a); and
 - (d) determine the asset classes and/or individual assets that it will invest in to achieve the desired risk exposure and whether making, holding and realising investments in those asset classes and/or individual assets can be implemented in a manner consistent with the interests of, and the RSE licensee's duties to, beneficiaries.
19. An RSE licensee must, for each investment strategy:
- (a) determine appropriate stress scenarios that cover a range of factors that can create extraordinary losses or make the control of risk in the investment strategy difficult; and
 - (b) undertake stress testing based on the scenarios in paragraph 19(a) to confirm that the strategy is appropriate, prior to implementation.
20. An RSE licensee must, at a minimum, determine for each investment strategy for an investment option that includes multiple assets and/or asset classes:
- (a) asset allocation targets and ranges that are appropriate to the investment objectives of the investment option;
 - (b) the basis on which asset allocation targets and ranges would be changed; and
 - (c) a policy to monitor and maintain the asset allocation within the determined ranges within a reasonable timeframe.
21. For the investment strategy of a MySuper product, an RSE licensee must also document, in addition to the requirements in paragraphs 17 to 20 inclusive, at a minimum, how the investment strategy:
- (a) is diversified over multiple risk factors and sources of return as required in the SIS Act;
 - (b) complies with sections 29VN(d)(i) and 29VN(d)(ii) of the SIS Act; and
 - (c) demonstrates compliance with rules for the relevant permissible fees in a MySuper product.

Giving effect to the investment strategy

22. An RSE licensee must have processes and criteria for selecting each investment to give effect to the investment strategy (investment selection process) to ensure that effective due diligence that is commensurate with the nature and

characteristics of the investment is undertaken prior to the selection of an investment for an investment option.⁹

23. An RSE licensee's investment selection process must result in the RSE licensee being satisfied that:
 - (a) it has sufficient understanding and knowledge of the investment selected, including an assessment of any factors that could have a material impact on achieving the investment objectives of the investment option;
 - (b) it has sufficient understanding of how the investment is expected to perform under the range of stress scenarios determined under paragraph 19(a); and
 - (c) the investment is appropriate for the investment option.

Monitoring investments

24. An RSE licensee must determine appropriate measures, approved by the Board, to monitor the performance of each investment in each investment option and each MySuper product on an ongoing basis.
25. An RSE licensee must ensure that persons applying and assessing the measures required in paragraph 24 are operationally independent from persons who are responsible for making the investment.
26. An RSE licensee must ensure that the performance of each investment is regularly reported to the Board and senior management.

Reviewing the investment strategy

27. For each investment strategy, an RSE licensee must have a review policy that is approved by the Board and that, at a minimum, requires each investment strategy to be reviewed against its investment objectives on at least an annual basis. The policy must also include:
 - (a) the triggers that will cause an interim review of the investment strategy in addition to the annual review;
 - (b) the processes for reporting the results of each review to the Board; and
 - (c) the criteria that will determine whether the investment strategy must be changed.
28. On receipt of the results of a review of an investment strategy undertaken in accordance with the review policy, the Board must ensure that a decision to amend the investment strategy is supported by sufficient justification and analysis for the amendment.

⁹ Where an RSE licensee engages an external service provider under an investment management agreement or mandate, the RSE licensee must comply with the requirements in *Prudential Standard SPS 231 Outsourcing*.

Stress testing

29. An RSE licensee must have a comprehensive stress-testing program that includes, at a minimum, the performance of each investment option against the stress scenarios required in paragraph 19(a).
30. An RSE licensee must document a description of the methodology used to select and carry out stress tests that aligns with the RSE licensee's risk management framework.
31. An RSE licensee must ensure that the results of the stress tests are reviewed periodically by senior management and reflected in the RSE licensee's investment governance framework.

Liquidity and cash flow management

32. An RSE licensee must have a liquidity management plan, approved by the Board, for each RSE within its business operations that, at a minimum:
 - (a) covers each investment option in the RSE;
 - (b) outlines the procedures determined by the RSE licensee for measuring and managing liquidity on an ongoing basis;
 - (c) includes consideration of how the liquidity of investment options in an RSE can be managed in a range of stress scenarios;
 - (d) identifies the circumstances the RSE licensee considers to be a significantly adverse liquidity outcome that requires action (liquidity event); and
 - (e) outlines what action the RSE licensee will take when a liquidity event occurs.

Adjustments and exclusions

33. APRA may, by notice in writing to an RSE licensee, adjust or exclude a specific prudential requirement in this Prudential Standard in relation to that RSE licensee.¹⁰

¹⁰ Refer to section 34C(5) of the SIS Act.