



18 December 2015

To all RSE licensees

## Governance arrangements for RSE licensees: Outcomes of consultation

### Background

On 31 August 2015, APRA released a consultation package, 'Governance arrangements for RSE licensees'.<sup>1</sup> The package included the following:

- *Prudential Standard SPS 510 Governance (SPS 510)*;
- *Prudential Standard SPS 512 Governance Transition (SPS 512)*;
- *Prudential Practice Guide SPG 510 Governance (SPG 510)*; and
- *Prudential Practice Guide SPG 512 Governance Transition (SPG 512)*.

The consultation package proposed a number of amendments to SPS 510 and SPG 510 intended to support sound governance practices by the boards of all RSE licensees, including provisions to support APRA's administration of the Government's proposed amendments contained in the Superannuation Legislation Amendment (Governance) Bill 2015 (the Bill).

The Bill, which proposes to mandate a minimum proportion of independent directors on the board of all RSE licensees, is currently before the Senate. The Government has indicated that the Bill will be considered further in 2016.<sup>2</sup> As such, APRA does not intend to formally finalise its consultation on governance arrangements at this time.

However, APRA considers it appropriate to provide a response to industry that summarises the outcome of consultation on the other aspects of the proposed amendments to SPS 510 and SPG 510. These amendments cover governance frameworks, the nomination, appointment and removal of directors, board renewal and tenure limits, and board size.

APRA intends to formally reflect in the prudential framework the set of proposals outlined in the attachment to this letter at the earliest opportunity. APRA will also respond more formally to the issues raised in submissions, including APRA's proposed administration of the Bill and the associated transitional arrangements, at the appropriate time.

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<sup>1</sup> <http://www.apra.gov.au/Super/Pages/Governance-arrangements-August-2015.aspx>

<sup>2</sup> <http://kmo.ministers.treasury.gov.au/transcript/075-2015/>

## **Consultation feedback**

APRA received eight written submissions on the consultation package from a range of stakeholders including RSE licensees, consultants, industry bodies and professional bodies. All non-confidential submissions are available on the APRA website.

Feedback was generally supportive about the revised sections of draft SPS 510 and SPG 510 that address aspects of sound governance practices in areas not directly related to the Bill.

### ***Governance framework***

Draft SPS 510 proposed that an RSE licensee be required to have a governance framework which sets out policies and procedures that the RSE licensee is required to have in place to support effective governance practices. Submissions supported the introduction of the concept of a governance framework into SPS 510 and made some suggestions to support the more effective operation of the framework in practice.

APRA therefore intends to include the requirements for a governance framework in SPS 510. Where an RSE licensee forms the view that its governance framework would be enhanced by going beyond the minimum requirements specified in SPS 510, APRA encourages the RSE licensee to do so.

### ***Processes for appointing, nominating and removing directors***

Draft SPS 510 proposed that an RSE licensee be required to establish and implement policies and processes for the nomination, appointment and removal of directors that address, inter alia, management of vacancies, assessing the suitability of candidates, reappointment processes, processes for resolving disputes about director appointments, when and how a director will be removed from the board and policies on voting rights and procedures regarding director appointments.

Submissions expressed support for requirements to have documented policies and procedures relating to appointment, nomination and removal of directors. As such, APRA intends to proceed with the proposed provisions in SPS 510. SPG 510 will also provide additional supporting guidance, broadly as outlined in the draft released for consultation.

### ***Director tenure***

In addition to the existing requirement for a renewal policy, draft SPS 510 sets out a new requirement for an RSE licensee to have in place a policy on director tenure which addresses maximum tenure periods. This proposal is consistent with existing provisions in SPG 510 which outline expectations regarding tenure.

Submissions were generally supportive of the new requirement for a tenure policy, with some requesting that APRA confirm expectations regarding the maximum number of terms a director can be appointed to the Board. Some submissions indicated that the maximum tenure for a director should be in the vicinity of 9-12 years (i.e. no more than three terms of three or four years).

APRA considers that appropriate board renewal supports effective governance of RSE licensees and their business operations, and this view was supported by submissions. APRA therefore intends to update SPG 510 in due course to reflect both that boards are expected to consider director's tenure at the end of each term served, and that APRA

expects that there would be limited circumstances in which maximum tenure limits exceeding 12 years would be appropriate.

### **Board size**

Draft SPS 510 proposed to require that an RSE licensee's governance framework include the board's policy on board size, with guidance on APRA's expectations relating to board size included in draft SPG 510. In particular, draft SPG 510 stated that 'it is difficult to envisage circumstances in which an RSE licensee would need a Board of more than 12 directors'.

Submissions suggested that the size of an RSE licensee board should always be a matter for the board to decide as it is best placed to do so, but some submissions did indicate that, in normal circumstances, an optimal board size would be no more than 12 directors.

APRA agrees that an RSE licensee board is best placed to determine the target size for its board, taking into account the mix of skills and experience needed to manage the size, business mix and complexity of the RSE licensee's business operations, and intends to confirm this view in SPG 510. Nonetheless, it remains APRA's view that, excepting temporary or transitional considerations, there are likely to be limited circumstances where a board of more than 12 directors is required to maintain appropriate skills and experience.

### **Next steps**

The attachment to this letter includes relevant sections that reflect the final position that APRA intends to include in SPS 510 and SPG 510 when they are finalised. In the meantime, for further information please contact your APRA responsible supervisor.

Yours sincerely



Helen Rowell  
Deputy Chairman  
Australian Prudential Regulation Authority

## Attachment: Revisions to SPS 510 and SPG 510

APRA intends to include in SPS 510 and SPG 510, as relevant, the following provisions at the earliest appropriate opportunity. These provisions reflect APRA's views as reflected in the draft versions of the SPS 510 and SPG 510 released for consultation in August 2015, with modifications to respond to issues raised in submissions.

### *Prudential Standard SPS 510 Governance*

#### Section A: Governance framework

- A1. An RSE licensee must at all times have a governance framework that sets out how the Board oversees and exercises its authority in relation to the business operations of the RSE licensee and which encompasses the totality of systems, structures, policies, processes and people within an RSE licensee's business operations.<sup>3</sup>
- A2. The Board is ultimately responsible for the governance framework.
- A3. An RSE licensee's governance framework must, at a minimum, include:
- (a) a formal charter that sets out the roles, responsibilities and objectives of the Board;
  - (b) the voting rights and procedures for the decisions of the Board;
  - (c) the Board's policies on:
    - (i) the size and composition of the Board and any Board committees<sup>4</sup>;
    - (ii) Board renewal;
    - (iii) the nomination, appointment and removal of directors, including director tenure and maximum tenure periods;
  - (d) the RSE licensee's policies and processes:
    - (i) to manage risks relating to fitness and propriety of responsible persons<sup>5</sup>; and
    - (ii) relating to the management of conflicts of interest<sup>6</sup>; and
  - (e) a review process to ensure that the governance framework remains effective.

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<sup>3</sup> Refer also to *Prudential Standard SPS 220 Risk Management* (SPS 220) for requirements relating to the management of governance risk.

<sup>4</sup> For the purposes of this Prudential Standard, a reference to 'board committees' is a reference to the Board Audit Committee, the Board Remuneration Committee and any committees which meet the description set out in paragraph 12 of *Prudential Standard SPS 510 Governance*.

<sup>5</sup> Refer to *Prudential Standard SPS 520 Fit and Proper* for requirements relating to the fitness and propriety of responsible persons.

<sup>6</sup> Refer to *Prudential Standard SPS 521 Conflicts of Interest* for requirements relating to the management of conflicts.

**Section B: Board nomination, appointment and removal**

B1. The Board must establish and implement policies and processes for the nomination, appointment and removal of directors. These policies and processes must, at a minimum, address:

- (a) the length of the director's term and the maximum tenure limit;
- (b) how vacancies will be managed, including, where applicable, how the RSE licensee will comply with the vacancy requirements in Part 9 of the SIS Act;
- (c) the process by which a candidate will be nominated for a vacant Board position;
- (d) the factors that will be considered when assessing the suitability of a nominated candidate, including how the RSE licensee assesses the independence of the candidate where relevant and the Board's process for determining which candidate, if any, is to be appointed;
- (e) the process by which a director will be appointed to the Board;
- (f) the factors that will determine when an existing director will be re-appointed, including whether the director has served on the Board for a period that could, or could reasonably be perceived to, materially interfere with their ability to act in the best interests of beneficiaries;
- (g) the process by which the Board will resolve disputes about nominations, appointment, re-appointment or removal of directors;
- (h) when and how a director will be removed from the Board; and
- (i) the Board's policy on voting rights and procedures in relation to nomination, appointment, reappointment and removal of a director.

***Prudential Practice Guide SPG 510 Governance*****Section A: Governance framework**

A1: An effective governance framework includes the oversight of systems, structures, policies, processes and people that underpin accountability within the RSE licensee's business operations. It supports an RSE licensee to make objective business decisions in the best interests of beneficiaries.

A2: APRA expects that a Board would establish a process to ensure that governance risks are properly and regularly evaluated and managed by the Board. Governance risks include, but are not limited to, risks associated with:

- (a) accountability and transparency of decision-making processes;
- (b) delegation of roles and responsibilities;
- (c) remuneration arrangements;
- (d) fitness and propriety; and

- (e) the management of conflicts of interest.<sup>7</sup>
- A3. For the avoidance of doubt, where an RSE licensee already has in place a policy that satisfies requirements set out in SPS 510, the RSE licensee may incorporate such policies by reference into the governance framework. That is, the materials do not have to be duplicated for the purposes of complying with the requirements of SPS 510.
- A4. APRA's view is that a prudent Board would determine a target size for the Board and its committees and reflect in the Board's renewal policy an outline of how the Board intends to achieve and maintain this target size.
- A5. APRA's view is that board size influences a Board's capacity to operate effectively. APRA considers it would be prudent practice for an RSE licensee to periodically review the total number of directors on the Board and assess whether the size of the Board supports the effective functioning and decision-making of the Board. The size of the Board is ultimately a matter for the RSE licensee to set in light of the size, business mix and complexity of their business operations. APRA's view, however, is that there are likely to be very limited circumstances where an RSE licensee would need a Board of more than 12 directors.
- A6. APRA's view is that, when determining the overall composition of the Board, an RSE licensee would ordinarily take into account the RSE licensee's business and strategic plans and the skills and capabilities required to effectively oversee the implementation of that strategy.
- A7. APRA expects that an RSE licensee would establish policies and procedures relating to voting rights which support effective decision-making by the Board. This would be expected to include procedures which ensure that the views of all directors are adequately reflected in all decisions made by the Board.
- A8. It would be prudent practice for the Board to consider using relevant board committees to provide appropriate oversight of key governance matters. Such committees may include a dedicated nomination committee or another appropriate board committee, such as the board risk committee.
- A9. The responsibilities of a dedicated nomination committee might include:
- (a) overseeing the nomination, appointment, reappointment and removal processes for directors of the Board<sup>8</sup>;
  - (b) recommending candidates for appointment to the Board; and
  - (c) overseeing remuneration and performance assessment policies and processes (if these roles are not otherwise performed by the Board Remuneration Committee).

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<sup>7</sup> Refer to *Prudential Standard SPS 220 Risk Management* for guidance relating to governance risk and *Prudential Practice Guide SPG 520 Fit and Proper* and *Prudential Practice Guide SPG 521 Conflicts of Interest* (SPG 521) for further guidance relating to assessments of fitness and propriety and the management of conflicts.

<sup>8</sup> For the purposes of this PPG, 'appointment' encompasses both the appointment of new directors and reappointment of existing or past directors to the Board or board committees.

## Section B: Board renewal

- B1. APRA expects a Board renewal policy would document the maximum tenure period for each director, including the circumstances where the RSE licensee may deviate from the terms of its tenure policy. APRA's view is that long periods of tenure can affect a person's capacity to exercise independent judgement. APRA expects that the length of each director's tenure would be examined at the end of each term served and that there would be limited circumstances in which maximum tenure limits exceeding 12 years would be appropriate.
- B2. APRA expects that an RSE licensee would develop and implement a considered approach for assessing each director on the cessation of their term and, at the end of the RSE licensee's maximum tenure period, to determine whether it is appropriate for the individual to be reappointed. This includes having regard to periods of time served on the Board of a predecessor RSE licensee where a merger has taken place. APRA expects that any circumstances under which a person is reappointed at the end of the RSE licensee's maximum tenure period would be exceptional.

## Section C: Board nomination, appointment and removal

- C1: Achieving overall Board composition which is appropriate for an RSE licensee's business operations provides the foundation for sound governance. The nomination, appointment and removal processes of the Board are crucial to achieving appropriate Board composition.
- C2: APRA's view is that the Board would be expected to have in place robust processes to support the nomination of appropriate candidates for appointment to the Board. This would include processes to support open and effective communication and consultation with organisations with a right to nominate directors for appointment to the Board. APRA considers that it would be appropriate for the Board to have processes in place to respond to the situation where a sponsoring organisation nominates or appoints a director that the Board considers unsuitable for appointment.
- C3: The Board's policy for nominating and appointing directors would be expected to ensure that terms of tenure are staggered to support continuity and the appropriate transfer of knowledge and skills to new directors.
- C4: When considering potential candidates and appointing new directors, APRA's view is that an RSE licensee would assess:
- (a) the current and past associations of candidates;
  - (b) the appropriateness of other directorships held by the candidate director, especially directorships of other RSE licensees<sup>9</sup>;
  - (c) the skills and capabilities of nominated candidates against the role and responsibilities of the vacancy and the Board as a whole, including consideration of committee vacancies; and
  - (d) the fitness and propriety of nominated candidates.

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<sup>9</sup> Refer to SPG 521.