

Superannuation technical determination No. 1 of 2023 – Actual and benchmark return formulae modifications

EXPLANATORY STATEMENT

Prepared by the Australian Prudential Regulation Authority (APRA)

Superannuation Industry (Supervision) Regulations 1994, subregulations 9AB.12(4A) and 9AB.14(9A)

Under subregulations 9AB.12(4A) and 9AB.14(9A) of the *Superannuation Industry (Supervision) Regulations 1994* (the Regulations), APRA has the power to modify the actual formula and the benchmark return formula respectively, as APRA considers reasonably necessary, to reflect a change of lifestage for a lifecycle Part 6A product.

On 4 August 2023, APRA made *Superannuation technical determination No 1 of 2023 - Actual and benchmark return formulae modifications* (the instrument) which modifies the actual and benchmark formulae used to conduct the annual performance assessment for MySuper lifecycle Part 6A products. The modified formulae apply where there has been a change in the structure of a MySuper product that is a lifecycle Part 6A product.

The instrument commences on the day after registration on the Federal Register of Legislation and will apply for the purposes of performance assessments from the 2022/23 performance assessment.

1. Background

APRA is required to conduct an annual performance assessment for Part 6A products, which are defined as MySuper products and trustee-directed products: see s 60B of the *Superannuation Industry (Supervision) Act 1993* and regulation 9AB.2 of the Regulations.

The Regulations require the assessment of a Part 6A product's performance relative to a benchmark portfolio created using the product's strategic asset allocation, and administration fees charged in the last financial year relative to the median fee charged for the category of product. The performance assessment is intended to hold RSE licensees to account for underperformance through greater transparency and prescribed consequences for RSE licensees offering products that fail the assessment.

On 4 August 2023, amendments to the Regulations made by the *Superannuation Industry (Supervision) Amendment (Your Future, Your Super – Addressing Underperformance in Superannuation) Regulations 2023* (YFYS Regs 2023) commenced.

The YFYS Regs 2023 inserted subregulations 9AB.12(4A) and 9AB.14(9A) to allow APRA to make a legislative instrument to modify the performance test formulae where there are changes to the lifestages of a lifecycle Part 6A product. This power supplements the existing ability of APRA to make a determination of this type applying to an individual RSE licensee and product under subregulations 9AB.12(5) and 9AB.14(10) of the Regulations. For the first two annual performance assessments (i.e. the 2020-21 and 2021-22 financial years), APRA issued a number of such individual determinations. Given the methodology specified in the individual determinations is the same across all products, APRA considers it appropriate for the modified methodology to be applied via a legislative instrument on an industry-wide basis

for product structure changes where required. Note that individual determinations made by APRA will continue to operate either alone or in conjunction with this instrument.

2. Purpose and operation of the instrument

The purpose of the instrument is to specify modifications to the actual return and benchmark formulae in the Regulations that will apply in circumstances where there has been a change of lifestage for a MySuper product that is a lifecycle Part 6A product. This ensures that any changes to the product are reflected in the performance history used in the performance assessment.

Explanation of each provision in the instrument

Part 1 - Authority, commencement and interpretation

Sections 1 to 4 are the operative provisions relating to the instrument's name, the commencement date, the legal authority under which it is made and relevant definitions.

Section 5 specifies who the instrument applies to, namely, RSE licensees of a superannuation entities that offer a Part 6A product that is both a MySuper product and a lifecycle Part 6A product. A product is a lifecycle Part 6A product if (i) the investments supporting the Part 6A product are divided into categories and (ii) each such category of investments is referable to a lifestage of the Part 6A product: see regulation 9AB.3 of the Regulations.

Part 2 - Determination of modifications to the actual return formula and benchmark return formula

Section 6 details the circumstances in which the altered actual and benchmark return formulae apply, namely where a MySuper lifecycle Part 6A product has experienced a "change of lifestage". A change of lifestage will occur if the product has particular lifestages at the end of a quarter in a lookback period for the product in respect of a financial year, and the product has different lifestages at the end of a later quarter in the lookback period: see definition of "change of lifestage" in section 4 of the instrument and paragraphs 9AB.12(3)(a) and 9AB.14(8)(a) of the Regulations.

Section 7 describes the modifications to the actual return formula in subregulation 9AB.12(2) of the Regulations in order to combine a lifecycle Part 6A product's performance in respect of a quarter during which a "change event" occurs.

Section 8 describes the changes made to the regulations to modify the benchmark return formula in subregulation 9AB.14(2) of the Regulation in order to combine a lifecycle Part 6A product's performance history in respect of a quarter during which a "change event" occurs.

The definition of "change event" in section 4 of the instrument requires that the following types of a change of lifestage be ignored for the purposes of the instrument: (i) the deletion of a lifestage catering to an older membership cohort due to insufficient members and (ii) the creation of a lifestage to cater for a younger membership cohort. The reason for this exclusion is because these types of change of lifestage are not a structural change to the product made by the trustee – they are instead an expected change arising from the nature of a lifecycle product.

The following example explains the operation of sections 7 and 8 of the instrument in the circumstances where a MySuper product has changed from a single strategy to a lifecycle strategy with two lifestages:

Example: Product A is a single strategy MySuper product (i.e. a MySuper product with one lifestage) that changes to a lifecycle MySuper product with two lifestages (“Lifestage 1” and “Lifestage 2”) effective from 1 March 2023 – this is referred to as a “change of lifestage” in the instrument.

As Product A changed its strategy during a quarter, APRA assesses performance for the March 2023 quarter over two discrete “partial quarter” periods:

- Period A: 1 January 2023 to 28 February 2023 ("**Day X**" in the instrument); and
- Period B: 1 March 2023 ("**change event**" in the instrument) to 31 March 2023.

The instrument modifies the actual return and benchmark return formulae specified in the Regulations to enable partial quarter returns to be calculated for Period A and Period B. These modified formulae are used to calculate the performance measure over the product’s lookback period as follows:

Period A - Partial Quarter Calculation Before Change in Strategy (1 January – 28 February 2023)

Strategic Asset Allocation (SAA) data for benchmark return: Product A is assessed as a product with one single lifestage, using its strategic asset allocation (SAA) from 31 December 2022 (the end of the previous quarter).

Total Investments data for determining lifestage weights in actual return and benchmark return: Calculated with reference to the value of assets in the single lifestage at 31 December 2022 (the end of the previous quarter).

Period B - Partial Quarter Calculation After Change in Strategy (1 March – 31 March 2023)

SAA data for benchmark return: Product A is assessed as a lifecycle product with two lifestages, "Lifestage 1" and "Lifestage 2". The SAA data reported to APRA at 31 March 2023, the first SAA applicable to the two lifestages, is used to create the benchmark return.

The instrument modifies the formula specified in the Regulations to reflect the SAA as at the end of the current quarter ($SAA_{a,j,t}$) instead of the SAA at the end of the previous quarter ($SAA_{a,j,t-1}$).

Total Investments data for determining lifestage weights in actual return and benchmark return: The instrument requires that the product level actual return and benchmark return for each lifestage are weighted using the amount of investments in Lifestage 1 and Lifestage 2 at the end of the current quarter (i.e. 31 March 2023) for the partial quarter after the change in strategy, instead of at the end of the previous quarter.

3. Exemption from disallowance and sunseting

This instrument is exempt from disallowance in accordance with section 44(2)(b) of the *Legislation Act 2003* (Legislation Act) and regulation 9 of the *Legislation (Exemptions and Other Matters) Regulations 2015* (Legislation Regulations) as this instrument is an ‘instrument (other than a regulation) relating to superannuation’.

This instrument is also exempt from sunseting in accordance with section 54(2)(b) of the Legislation Act and regulation 11 of the Legislation Regulations as this instrument is ‘an instrument (other than a regulation) relating to superannuation’.

As the instrument falls within the above-mentioned exemptions from disallowance and sunseting, APRA does not have discretion to subject the instrument to disallowance and sunseting. To mitigate against any adverse impact arising from the above-mentioned exemptions from disallowance and sunseting, APRA undertook consultation on the proposed exemption (refer to paragraph 3 for further details). APRA intends to review the operation of the instrument after each year’s performance assessment to ensure it remains applicable and fit for purpose for the next year’s assessment.

4. Consultation

On 20 April 2023, APRA released a consultation letter requesting feedback on the draft technical determination by 11 May 2023. The consultation letter sought views on moving the determination from an individual to a class basis, and on the drafting of the technical determination.

APRA received one submission, which supported the proposal and suggested some minor technical changes to clarify certain terms used. The submission was made by an industry body which represented part of the superannuation industry.

APRA is satisfied the consultation was appropriate and reasonably practicable.

5. Regulation Impact Statement

The Office of Impact Analysis confirmed that a Regulation Impact Statement was not required.

6. Statement of compatibility prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

A Statement of compatibility prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* is provided at Attachment A to this Explanatory Statement.

ATTACHMENT A

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*

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This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instrument listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* (HRPS Act).

Overview of the Legislative Instrument

The purpose of the Legislative Instrument is to make a technical determination to alter the return and benchmark formulae in the regulations to allow APRA to combine the performance histories of lifecycle Part 6A MySuper products on a class basis.

Human rights implications

APRA has assessed the Legislative Instrument and is of the view that it does not engage any of the applicable rights or freedoms recognised or declared in the international instruments listed in section 3 of the HRPS Act. Accordingly, in APRA's assessment, the Instrument is compatible with human rights.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.