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Merging Super Funds and Operational Risk

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Merging Super Funds and Operational Risk

Overview

As the pace of Successor Fund Transfers of Superannuation funds has revved up, practitioners are faced with unique risks as funds transition and embark on new Business As Usual operations.

Context

In the past two years, increasing numbers of superannuation funds have initiated informal and formal merger discussions. We are seeing merger activities further increase as both the regulatory and political landscape continue to shift in favour of consolidation.

Australian Prudential Regulation Authority's (APRA) 'Strengthening Super Member Outcomes' package released in December 2018 has become the primary way in which the regulator assesses the long-term sustainability of funds. With a focus on poor performance and increased scrutiny over costs and fees, this places real pressure on small to medium funds that are not able to maximise economies of scale.

APRA's engagement with poorly performing funds is now increasingly focused on determining the cause of shortcomings and then requiring them to develop a robust and implementable strategy to address these weaknesses within a very short period. These prescriptive measures can create risks that are difficult to mitigate.

In the Federal Budget handed down by the Commonwealth Treasurer Josh Frydenberg MP in October 2020, the 'Your Future, Your Super' package was announced, placing even more impetus for industry consolidation. APRA will now be "Holding funds to account for underperformance to protect members from poor outcomes and encourage funds to lower costs. The Government is now requiring superannuation products to meet an annual objective performance test." In some cases, weaker market returns under conditions of COVID-19 are tightening the screws on the pressure cooker. Continuation of fund mergers is inevitable.

Accountability

In 2017 ARPA published a 'Successor Fund Transfers and Wind-ups' guide to assist the industry in protecting member interests while keeping regulators happy as they transform their businesses through mergers and wind-ups. The requirements for business transformation and data management represented a significant challenge to Superannuation funds.

Whilst merger business analysis models have developed to assess how commercial interests might stack up for firms and members, the industry has lacked a framework to assess the business risks associated with merging technology. The result has seen some mergers planned to occur over a 6-month period ending up taking between 9 and 18 months to achieve, some with material collateral, commercial and reputational damage. Some have simply been deferred. Successor Fund Transfers (SFTs) are not easy and while scale can bring cost benefits, if not managed well, it can amplify risks and compound operational inefficiencies post-transition.

Operational risk spikes during mergers. SFTs require new thinking around data management, automation and efficiency. The problem lies within two very different operations needing to merge.

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Data

One of the key risks to technology consolidation during the merger period and beyond is retaining effective control over investment data, accounting practices, reporting and regulatory oversight. This is particularly relevant where business practices and systems are categorised by disparity and manual processes. These risks are escalated by simultaneous personnel mergers and cultural upheaval, not to mention the complexity of streamlining investment operations across in-house and external fund managers, multiple custodians, middle-office functions and investment data sources and reporting. The devil is most certainly in the detail and that can often only be discovered once the transformation program has commenced. But trustees and regulators have little patience for errors and omissions due to business change, particularly where it has a material impact on the outcomes of members.

Oversight

Effective oversight during merger operations is the only way to ensure a successful operation that keeps staff, members, and the regulators happy. Automation is key here, as volumes, complexity and quality issues inevitably emerge, while process auditability is necessary.

Tools

Merging Super Funds need simple ways to manage risk across the breadth of investment operations; whether in-house, outsourced or a mix of both. The implementation of an oversight tool can be simple and effective in automatically ensuring that data, accounting, integration, regulatory reporting, and ultimately member reporting are held to a continuing high standard. Funds need to manage by exception rather than access all new and old processes when issues arise. Regulatory and audit scrutiny around the SFT process will only increase.

The InvestPro software from FRS is simple and cost effective to implement as part of the SFT plan. The Oversight module is designed to control the delivery and accuracy of data in an exception-based environment. Further, its accounting pedigree allows contextual analysis, taking the place of analysts and spreadsheets to control processes and ensure accuracy, resulting in a material reduction in risk and manual work.

References

ARPA 'Strengthening Super Member Outcomes'	'Your Future, Your Super'	ARPA 'Successor Fund Transfers and Wind-ups' (SPG 227)

About Financial Risk Solutions Ltd (FRS)

With over 20 years delivering Investment Administration software, Financial Risk Solutions Ltd (FRS) is a trusted technology partner to life assurance, wealth and asset management firms worldwide. Led by an expert team of actuaries, compliance and IT specialists, clients license FRS software to help navigate the ever-changing challenges of growth, regulatory pressures and competition in the industry.

The award-winning* InvestPro™ platform is relied on by blue-chip financial services and BPO clients to reduce operational costs, increase efficiencies and mitigate risk in the manufacture and management of investment products. More than 150,000 funds are managed on the Invest|Pro™ platform today.

Delivered on-premise or cloud-hosted, Invest|Pro™ securely automates multiple complex fund administration processes including unit-pricing, cash allocation and rebalancing; oversight and validation of operational activity performed by outsourced partners; and in Europe monitoring and reporting for PRIIPs, KID requirements, and Pillar III asset reporting for Solvency II.

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22 YEARS

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