

ITM Data Report

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This decade's trend is Fund mergers



Steve Shoreson

Fund Mergers – is Cooper right?

When does “big” become “big enough”?

Consolidation for the industry will be great for ITM’s data migration business but at what point will it stop? What will our industry look like in a few years? Jeremy Cooper has thrown a figure of 27 funds into the ring!

This is my 24th year in the superannuation industry, having started with Colonial/Jacques Martin in June 1986 as a trainee programmer on superannuation systems.

I’ve seen a lot in that time ... the rise of industry super, the demise of DB funds, the introduction of master trusts and the consolidation of third party administrators.

My key observation of our industry is that once a trend starts we’re excellent at making it become a self-fulfilling prophecy. This decade’s trend is Fund mergers!

Why are mergers happening? Is it really all about scale?

There are clearly many pros for the merging of two funds and everyone talks about them. However, very few people are voicing opposition to this particular trend, at least not in public. It was interesting after a recent CMSF session that a number of people made the observation that they weren’t entirely convinced by the “scale” argument.

Administration costs have always been an “insignificant number” when compared to investment returns, fees and charges. In fact, most large funds could meet their entire administration costs by increasing investment returns by 0.1% or less. This fact puts the effort of saving 20 cents a member (by merging the administration) into perspective.

The Vision Super and Quadrant Super initiative recognised this and they chose to collaborate rather than merge. They pooled their assets to create economies but didn’t see the need to physically merge each fund and its administration. The same methodology can be used to create economies by two funds pooling their membership for insurance purposes. Obviously there are other areas where cost savings can be made from a merger, such as rationalising the size of each fund’s secretariat, support and member servicing staff.

For those funds considering a merger, there needs to be somewhere that they can find real quantitative facts and figures. To me, the biggest question that needs to be answered with quantitative facts is ... **When does “big” become “big enough”?**

I don’t completely buy Jeremy Cooper’s 27 funds idea - if scale is the be all and end all, then why not just one Fund. The industry needs to be careful what it wishes for ... it’s not a giant leap in thinking from 27 funds to one National Provident Fund!

Don’t worry though, if we get the one National Provident Fund we can unwind it in another 20 years and start the cycle all over again ☺

Where are the quantitative facts and figures that support mergers?

Are we heading for one National Provident Fund?

Regulating Administrators

Is it just a matter of time before we see Regulations aimed directly at Administration Companies?

One particular coffee-break discussion at CMSF was with regard to when the Regulator will target Administrators. Apparently, this is a move that will be welcomed by many of the larger third party administrators.

In reality this initiative has been a long time coming. As the major supplier of resources and operational expertise to Trustees, Administrators can make or break the Trustees service value chain.

What would such regulation look like? A possible scenario is taking place in South Africa at this very moment. The Financial Services Board is putting in place legislation “in respect of administrators acting on behalf of pension funds”.

The Benefit Administrator must complete:

- an “Application for approval as a Benefit Administrator”
- an “Initial Assessment of Processes and Procedures”
- a “Management representation letter on Application for Registration”

There is an Audit Report on the original application for approval as a Benefit Administrator and everything is repeated annually:

- an “Application for annual renewal of the approval as a benefit administrator”
- an “Annual reassessment of processes and procedures”
- a “Management representation letter on annual renewal”

There are even schedules relating to termination of the administrator! The transferring administrator has to complete a “Schedule for Termination of Administration” and the Board of management (Trustee) has to make a written declaration relating to the “Termination of Administration Services and handover of documents, data and records.”

On first viewing the hundreds of pages contained in the regulations and accompanying schedules it seems a very heavy-handed approach! However, on working through the documents there is very little that seems unreasonable. Here in Australia, we might word things a little differently and perhaps change the focus in a few areas but it wouldn't seem inappropriate if similar regulation was introduced.

After digesting the contents of the South African approach, a few questions are raised:

- Do we need this type of regulation in Australia?
- If we do, should it be as prescriptive and onerous?
- Will introducing such regulation improve the quality of administration?
- If the administrator is regulated, will this de-risk Trustees?
- Will Regulation of this type raise barriers to entry for new administrators?

My personal viewpoint is that the answer to most of the above questions is “Yes”. We know need to bide our time and see what our own Regulators come up with.

For a copy of the proposed South African legislation please email steveshoreson@itmlimited.com.au (email copies only)

The regulation differentiates between “benefit administrators” and “investment administrators”

Upon termination, Trustees have to make a written declaration with regard to handover of documents, data and records.

No comprehensive Data Integrity Audit when migrating data ... High risk !!!

Independent Data Integrity audits are not common place in Australia.

However, there are times for Trustees when the need for an independent data audit is beyond question!

An independent data integrity audit is a must in certain circumstances

Trustees are as responsible for member record keeping as they are for ensuring that investment and insurance offerings deliver as promised. However, as we all know, administration does not receive the same focus at Trustee level. As APRA has recognised, there is too great a reliance on the Administrator doing the right thing. Especially with the current trend for fund mergers the need for high quality data has to be given a higher profile.

Whilst data quality should be considered on a regular basis it often isn't. However, in any of the following circumstances, Trustees must ensure that a thorough independent review of all data is undertaken.

- Fund Merger
- Change of Administrator
- Change of administration platform/system

Such a review must consider 100% of transferring data ... don't ever rely solely on sampling techniques! Sampling is great for finding weaknesses in processes but the random nature of many data errors means that all data needs to be audited. If there is one \$50,000 insurance data error, it is highly unlikely to be found from sampling.

Trustees, if you have recently undergone a system change ... Ask to see the reports detailing the significant data issues

Significant matters to be drawn to the Trustee and Secretariat's attention include:

- Critical data errors
- Financial record-keeping errors
- Member benefit statement issues
- Potential breaches, compliance issues and fraud indicators
- Platform bugs and improvements
- Duplicate members and duplicate data
- Data issues that will cause a Migration to fail

Consider a large fund merging with a smaller one with different administrators and/or different administration platforms. The Trustee, Secretariat and chosen Administrator will be responsible for the quality of the data from the merger date. At the very least, the Trustee must make every effort to identify any data issues with the data that is being transferred into the successor fund.

Specialist services

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Clients

- Trustees & Product Sponsors
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Contact us

Independent Transition Management Pty Ltd (ITM)
Level 2, 480 Collins Street, Melbourne VIC 3000
Tel: 03 8610 6889
Fax: 03 8610 6881
email: enquiry@itmlimited.com.au
Web: www.itmlimited.com.au

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