

Trustee investment governance: A cautionary tale

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Background

The recent collapse of three managed investment schemes has caused heavy losses to some members retirement savings impacting over 12,000 investors, with an estimated \$1.2 billion in losses.

All three of these managed investment schemes, invested via superannuation platforms, were marketed as diversified, stable superannuation products which were promoted to deliver superior returns while maintaining strong liquidity. However, following their collapse, a very different reality has been revealed; the portfolios were complex, speculative, high-risk and illiquid.

The Australian Securities and Investment Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) are now engaged in reviewing shortfalls in the current laws and regulation. Moreover, the various superannuation platform trustees that hosted the managed investment schemes are also under regulatory scrutiny.



Managed investment schemes are regulated by the *Corporations Act 2001 (Cth)* (Corporations Act), ASIC is the regulator responsible administering the Corporations Act and the *Australian Securities and Investment Commission Act 2001* (ASIC Act). These Acts set out the conduct and disclosure obligations of financial services providers, including operators of managed investment schemes. ASIC is currently undertaking various investigations and enforcement actions related to these collapses.

Superannuation products, such as APRA-regulated superannuation funds, are not managed investment schemes. APRA supervises institutions across the banking, insurance and superannuation sectors. APRA's role is to maintain the safety and soundness of financial institutions to ensure confidence in the broader financial system. APRA is currently undertaking a targeted review into the governance and oversight of superannuation platforms.

The investigations are ongoing and likely to take some time, potentially years, and the potential issues are widespread (not just investment-related) including inadequate disclosure, conflicted advice and related-party transactions. The investment-related issues centre around the need for detailed initial and ongoing investment due diligence, appropriate monitoring and oversight of investments, and the importance of accurate and timely asset valuations.

In this article, we summarise the key investment-related aspects that have emerged as critical considerations for trustees of APRA-regulated funds in light of the recent collapses.

What are the key related investment governance obligations for APRA-regulated superannuation funds?

For APRA-regulated superannuation funds, Prudential Standard SPS 530 – Investment Governance sets out the key related trustee requirements to select, manage and monitor investments on behalf of beneficiaries. This includes:

- The role of the Board: The Board is ultimately responsible for selecting, managing and monitoring investments.
- Due diligence: A comprehensive due diligence process is essential to ensure proper investment selection and ongoing monitoring.
- Performance monitoring: Licensees are required to assess and report on investment performance regularly, ensuring alignment with objectives.
- Liquidity management: Effective liquidity management plans, including clear metrics for reporting and oversight.
- Valuation governance: A valuation governance framework must be implemented to ensure accuracy and consistency in valuing assets.

Key learnings and considerations

From these collapses, there are three key investment-related aspects that have been highlighted for trustees.

Do your due diligence

- Trustees must not diminish the importance of initial and ongoing due diligence of investments. It is essential to have processes and criteria for selecting each investment and ensure the due diligence is commensurate with the nature and characteristics of the investment. When offering an externally managed investment option, this includes understanding the asset allocation and underlying investments of that option.
- Trustees have an obligation to make sure what is being offered to members is appropriate, fit for purpose and in their best financial interests.
 - Do you have the appropriate investment governance policy and processes for the selection, management and monitoring/oversight of investments?
 - Do you have the appropriate investment governance policy and processes to ensure appropriate independence and management of potential conflicts of interest?

Trustees cannot outsource accountability

The Trustee is ultimately responsible for the sound and prudent management of the investments, which includes regular monitoring and review of the investment strategy. It has responsibility to ensure its governance of investments supports effective investment decisions.

The Trustee must act in the best financial interests of its members.

The Financial Accountability Regime (FAR) also states accountable persons under FAR may face individual penalties or enforcement action for certain responsibilities within their remit, and they are not allowed to outsource their FAR responsibilities.

- Do you have an appropriate investment governance framework?
- Do you have the appropriate investment governance policy and processes for the regular monitoring and review of the investment strategy?
- Do you have appropriate oversight and reporting mechanisms?
- Does your delegation framework support effective investment decision-making?
- Do you understand your obligations under FAR? Are you an 'accountable person'?

The importance of timely and reliable valuation information

Having a process to maintain reliable valuations is a key fiduciary duty.

Trustees have an obligation to treat all members equitably, so having reliable valuation processes and information are critical in achieving this aim.

An effective valuation governance framework can mitigate potential or perceived conflicts of interest across the valuation process.

- Do you have an appropriate valuation governance framework?
- Do you have an appropriate policy and processes for challenging valuations?
- Do you have appropriate board oversight and management of conflicts of interest as it relates to valuations?

How we can help

Frontier Advisors' Investment Governance Team offers a range of services to assist RSE licensees address the regulatory risk in this area. We can help with:

- Reviewing or developing board approved frameworks and policies to ensure alignment with SPS 530, good governance principles and industry practice.
- Reviewing the investment governance processes and practices to ensure alignment with internal policies and consistency with SPS 530, good governance principles and industry practice.
- Providing independent valuation governance services.
- Reviewing and conducting workshops for trustees and internal staff.

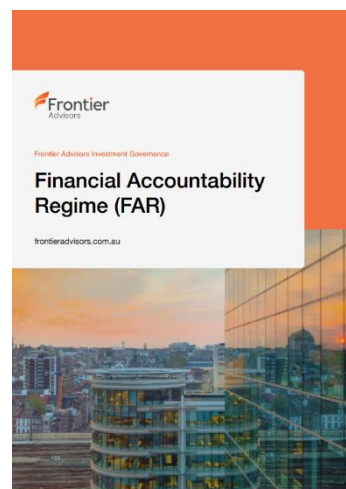
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