Summary
- The fiduciary management market has grown by over 100 per cent in the past three years.
- Trustees often worry they will lose control with FM in place. However delegating the investment management work to fiduciary managers does not stop trustees having the responsibility for investment decisions.
- Cost of FM is the biggest concern among the pensions industry and has been rated the top disadvantage in surveys for the past four years.
- Survey results show 99 per cent of pension funds with FM in place are 'satisfied or better' with their arrangement.
- Transparency is highlighted as one of the biggest areas for improvement in the FM market.

Truth or fallacy?

Despite its recent growth in the UK, fiduciary management still raises some concerns among the pensions industry. Lauren Weymouth explores whether these reservations are justified

Like most new solutions to enter the pensions market, the arrival of fiduciary management in the UK triggered a mixed reaction from the pensions industry. The concept of pension fund trustees handing over the management of an investment portfolio to a fiduciary manager resulted in sceptics raising questions about the legitimacy of products with high fees and no proven guarantee of value for money.

However, the last few years have seen the fiduciary management (FM) market develop rapidly. The *Aon Hewitt 2014 Fiduciary Management Survey* found the market has grown by 100 per cent over the last three years. Furthermore, it found that out of 350 respondents – representing 25 per cent of the UK's DB pension market, with 93 per cent using FM – 99 per cent of those under FM are 'satisfied or better' with their fiduciary solution.

Despite results such as this, there are still some market concerns that have been lingering since inception. With a lot of confusion about what exactly fiduciary management is, a myriad of 'market myths' have become widespread.

MN – an FM provider from the Netherlands, where FM originated – has recently developed an arm in the UK. It says some of the issues the firm had to deal with in the early 2000s (when FM was first taking off in the Dutch market), were similar to some of the questions raised in the UK now. Some of the main concerns include whether it is just a fad and whether or not performance will actually justify the perceived increase in cost.

"Whenever you get a new concept or a new service that providers are adding to their suite of offerings, it does take time, both for the market to catch up and for providers to raise their game, as well as for clients to understand the marketplace," the firm's client director Christy Jesudasan says.

Aon Hewitt partner and head of client solutions Sion Cole says the situation in which these concerns have aroused may be partially due to "failings in the partnership and understanding between the provider and scheme – often rooted in the original selection process – and is therefore not actually a failing of fiduciary management itself".

A gradual adoption

There has been a lot of debate about what exactly is the recipe for a 'perfect' partnership between trustees and a fiduciary manager, but there is still no standardised solution for schemes of all sizes. Because of this, when FM first came to the UK market, there was a myth that it was designed for small schemes only.

Cole notes that initially FM was polarised, so very small schemes were opting for full fiduciary management and some of the larger schemes were opting for partial fiduciary management. "Smaller schemes were keen to take up the service as it provides them with access to a full-time professional investment team that can provide a daily focus. However, the growth is now happening in the middle section of schemes between £100 million and £1 billion," he says.

Cardano head of clients Richard Dowell says the firm is also starting to see that schemes of all sizes are looking to adopt FM and the 'size tilt' is likely to be less pronounced over time. "Many surveys have shown that the take up across schemes is segmented by size. Typically, schemes with less than £100-150 million have been keener to take up the service as FM allows access to a full-time professional investment team, which think about the scheme on a daily basis, providing a kind of focus that they may not have received under an advisory arrangement," he says.

"(Fiduciary management's) growth is now happening in the middle section of schemes between £100 million and £1 billion"

Balancing the control

Another common myth about the fiduciary/trustee relationship is that trustees feel FM causes them to lose control over the schemes investment decisions. However, while PTL client director Colin Richardson says losing control is a genuine concern among trustees, it does not necessarily mean it is a bad thing.

"The whole point of fiduciary management is that for the sake and efficiency of better decisions, you are delegating some of the decision making," he points out. "The fiduciary manager is better positioned and has more time to consider certain changes to the portfolio and changes to the balance of the assets and investments employed."

Jesudasan agrees that when fiduciary management is done in the right way, it can actually give control back to the trustee, rather than take it away. "I think there is a certain amount of over-delegation in the market", he says. "People seem to think they can delegate their problem away and someone will solve them. That is a misconception. You can delegate the work, but you can not delegate the responsibility."

One of the key advantages found in this year's Aon Hewitt survey was that FM is a solution to limited trustee time. Almost three quarters of trustees spend no more than five hours per quarter on investment matters, Cole says. Therefore, trustees are continually turning to FM to allow them to focus that limited amount of time on 'key strategic key decisions' and do some of the day-to-day investment decision-making.

However, despite the increased take-up of FM by all scheme sizes, Richardson says from a trustee perspective there is often a concern surrounding overselling by some of the large consultancy firms, where they are pushing to sell their fiduciary management quite heavily. "It is a concern I have heard expressed often, although my own experience is a balanced awareness being brought of the fiduciary offerings available," he adds.

Value for money

The most heavily debated area of FM – and the top disadvantage to have been pointed out by survey respondents for the past four years – is cost and fee structure. Cole admits that in many cases there is "no doubt about it, fees will rise under FM".

"But not in all cases," he highlights. "In some cases, we have seen they have actually fallen under FM. What is important is not the size of the fee, but whether the fiduciary manager is able to demonstrate the fee being paid is value for money. And I think this is where the industry needs to work quite hard and trustees need to establish whether the cost of fees is relative to the benefits."

The cost of FM depends on a number of different elements; the growth/matching split, use of passive/active investments, asset allocation – hedge funds being more expensive than passive equities, for example – and the level of hedging being just a few.

Because of this, Richardson says FM will not become universal among schemes, simply because there is "such a lot of cost pressure on the investment management industry and there will always be a portion of trustees who think it is too expensive or want to take full control of their scheme alone".

Greater transparency

Although busting the myths and controlling cost will always be problematic, Dowell considers the biggest challenge facing FMs to be the lack of transparency. "Schemes are only going to opt for a fiduciary management if they are confident that it will deliver better results. So, it is important that fiduciary managers can demonstrate they can help the trustees achieve their funding goals in a more consistent way," he says.

"Proving this requires all managers to be able to publish their track record or, if not that, join together to publish a combined result. Many excuses are being made as to why results can't be published, which I just don't understand."

Jesudasan agrees that there needs to be greater transparency surrounding achievements and results for FM to keep up with its current success rate. "But that will take time," he says. "As the market opens up and there begins to be more scrutiny, there will be more regulation and new market players will begin to research and monitor fiduciary managers, so we'll hopefully see greater transparency coming through."

Written by Lauren Weymouth