Summary

- As of April 2015, amendments to the 1996 Occupational Pension Schemes regulations state that trustees have a duty to calculate charges and transaction costs borne by members each year, and to assess the extent to which costs and charges represent good value.
- Also in 2015, the FCA emphasised the need for the committees to "act in the interests of members in assessing and raising concerns about value for money" when outlining the rules for independent governance committees (IGCs) overseeing contract-based schemes.
- The PLSA recommends that trustees or governance committee members create processes for assessing value delivered by investments, governance, administration and communication.
- The PLSA also stresses the need for trustees to identify the objectives of communication strategies and measure their success in achieving them. They should review the length, style and frequency of communications and the suitability of delivery methods.

Added value

David Adams delves into the industry's developments to enhance value for money on pension fees

One would hope that anyone responsible for the governance of a pension scheme would want to ensure members were getting good value for money. But even if trustees or governance committee members were not doing this as a matter of course, in the post-auto-enrolment world, regulatory obligations have changed.

Good value

As of April 2015, amendments to the 1996 Occupational Pension Schemes regulations state that trustees have a duty to calculate charges and transaction costs borne by members each year, and to assess the extent to which costs and charges represent good value. Trustees must provide details and explain the outcome of good value assessments in an annual governance statement.

Also in 2015, the FCA emphasised the need for the committees to "act in the interests of members in assessing and raising concerns about value for money" when outlining the rules for independent governance committees (IGCs) overseeing contract-based schemes. There is currently no agreed statutory definition of 'good value' in this context, but one starting point is the definition set out in The Pensions Regulator's new draft DC Code of Practice. It states that a scheme is likely to offer 'good value' if "the combination of costs and what is provided for the costs is appropriate for the scheme membership as a whole ... compared to other options available in the market".

The Pensions and Lifetime Savings Association (PLSA) published a good practice guide on this subject in December 2015. It recommends that trustees or governance committee members create processes for assessing value delivered by investments, governance, administration and communication; and for reporting their findings. The guide also emphasises the importance of considering the way scheme costs are shared between the sponsoring employer(s) and the members. The regulator suggests the basis for this cost-sharing should be clearly set out in the trustees' annual good value statement.

At the time of writing, the regulator is still consulting on its draft DC Code of Practice *[the consultation finished on 29 January]*. "Value for money is a concept that applies to all pension schemes," the regulator's executive director for regulatory policy Andrew Warwick-Thompson says.

"We're still in consultation, so have not yet formed a firm policy. But it's clear from the responses we're getting that there's a consensus forming around charging and transaction costs

representing good value if they look good for the member.”

Cost

The regulator plans to put a final draft of the code before parliament in May, with parliamentary approval due to be completed by end of July. Draft guidance will be consulted on in March and April and finalised by July.

Meanwhile, within the industry, one principle upon which many experts seem to agree on is that cost does not determine value. Barnett Waddingham head of DC Mark Futcher believes the pensions world has become “far too focused on cost”.

“We try to encourage trustees we work with to look at everything they pay for and determine whether they want or need it,” he says. “It’s a big exercise to go through, but it’s part of good governance.”

The PLSA recommends benchmarking in some form. While recognising that many schemes face significant practical difficulties in attempting this, the PLSA good practice guide nonetheless attempts to outline the principles to use if it is attempted: access to accurate data and comparisons with schemes with similar cost-sharing models. Like-for-like comparisons may not be available, the guide’s authors admit, but they recommend comparing headline costs, charges and benefits with leading master trusts or group personal pension plans.

In pooled pension arrangements it can be difficult to break down costs and charges for a specific scheme. However, Futcher suggests that a growing number of bundled scheme providers are now trying to make this easier.

This does not mean trustees should always seek to emulate what they see elsewhere, notes NOW: Pensions director of investment and product development Rob Booth. “Some arrangements will have lots of investment funds to choose from, and this, that and the other functionality,” he says. “But it’s really important that value for money in any scheme is measured in the context of the demographics of that scheme’s membership. Are all the bells and whistles appropriate for the membership you have, or are you using them to justify the costs you’re applying?”

When assessing governance the PLSA’s good practice guide recommends looking at the independence and transparency of scheme governance and oversight; and discussing with scheme advisers the practices in place at other schemes for comparison.

For assessing value delivered by administration, the PLSA suggests reviewing objectives and the benefits they deliver to members; alongside administration performance in service level standards and quality terms, the timeliness and accuracy of transactions, quality of scheme data and member feedback.

Investment value assessments should cover fund/investment management and investment consultant fees, ongoing fund charges, depository and custody fees and transaction costs, according to the PLSA. Trustees should consider the suitability of default and other investment funds for the membership, in terms of cost, risk, performance, clarity and measurability of objectives, asset security; and transaction costs.

Members’ needs

But above all, says Nest head of member proposition Matthew Blakstad, all value assessments need to be based on the needs of the scheme’s members. “We would encourage all trustees and scheme sponsors to start with analysis of what members need,” he states. “Try to define good quality around what ‘good’ looks like for them.”

At Nest every member is placed in a target fund based on their target year of retirement. “Because we’ve got a lot of people in those funds we can give them a consistent level of monitoring and decision making,” Blakstad comments. “But also, by having separate funds with slightly different asset allocations we’re able to move assets between different groups without having to buy or sell them on the open market.”

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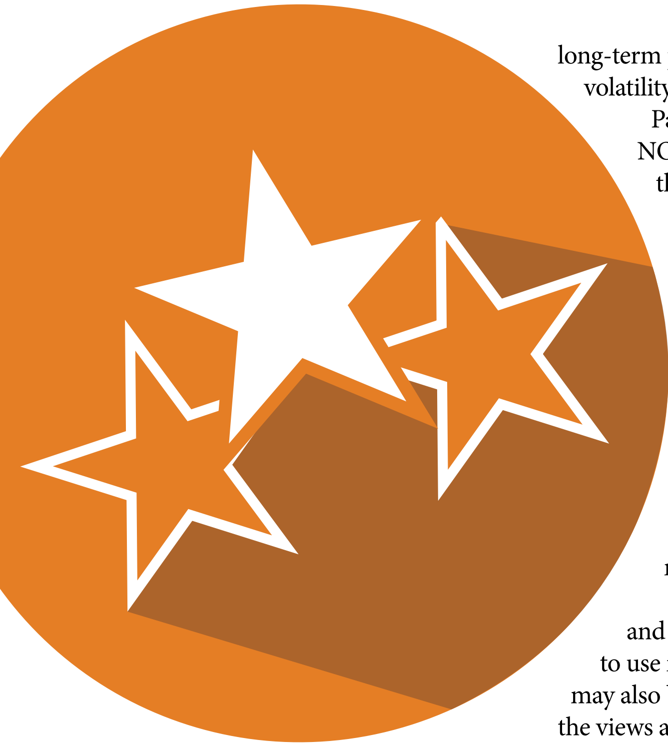

A greater proportion of Nest savers are likely to be median or low earners, younger, more ethnically diverse and female than would be the case in most pension schemes; while members' knowledge and understanding of pensions and investing tends not to be as high as would be the case in some other pension schemes. A majority have opted to stay in the default investment fund.

"So a big part of our strategy has to be to design default funds around managing long-term performance and short-term volatility," Blakstad adds.

Part of the value Nest and NOW: Pensions aim to deliver is the use of user-friendly, easily understood communications. The PLSA stresses the need for trustees to identify the objectives of communication strategies and measure their success in achieving them. They should review the length, style and frequency of communications and the suitability of delivery methods.

One way to assess the quality and clarity of communications is to use member feedback – and this may also be the best way to determine the views among the membership of the value they are getting from the scheme. "In some respects value for money is about perceptions among the members," says Booth. "When a member retires are they saying 'That was a good experience, I got value for money out of that'?"

Finally, where appropriate, the value for money assessments should also incorporate some consideration of the value provided around retirement and beyond. "The duty of the trustees to safeguard the interests of the members lasts for as long as the member is a member of the scheme," points out Warwick-Thompson.

"Within the industry, one principle upon which many experts seem to agree on is that cost does not determine value"

"Where the scheme does offer decumulation options we would expect trustees to test the value for money that the membership is going to get."

But of course, whatever actions trustees or governance committee members take to try to ensure good value for members, they must take care to ensure those actions are proportionate. Larger schemes will have the resources to undertake more in-depth reviews of the value members get in return for the fees they pay, yet smaller schemes will have opportunities to tailor value to suit a smaller, probably less diverse scheme membership. Either way, the hope must be that all the recent regulatory changes help those running and sponsoring schemes to review and ultimately enhance the value they deliver for members of all types of scheme.

Written by David Adams, a freelance journalist