Trustee Guide 2017:

The hot topics facing trustees

Featuring:

- The brace of reforms putting trustees at tipping point
- How real estate investment can beat inflation returns
- Making administration documents accessible to all
- How to help members transfer pensions easily

AEW JLT ORIGO

On the edge

The brace of new reforms puts trustees at 'tipping point', Raji Menon finds

The role of pension trustees is at a 'tipping point', as a raft of new legislation looks set to bring about fundamental changes in the standards and approach required for trusteeship, according to leading industry figures.

The recent BHS debacle has once again shone a spotlight on pension funds and their trustees and with further regulation on the cards, trustees are bracing themselves for a rapid acceleration in expected skills and standards.

The Department for Work and Pension's select committee, led by Frank Field MP, is looking at whether the role and power of pension scheme trustees need to be revisited following the £571 million pensions black hole in the BHS pension fund after the retailer went bust. The committee is also consulting on the relationships between The Pensions Regulator, the pensions lifeboat PPF, trustees and sponsoring employers.

"There's been a gradual ramping up of what is expected of trustees over the last five years, but this has accelerated over the last 12-18 months to the extent where we are now at a tipping point in the trustee function," says PTL managing director Richard Butcher.

Butcher said there were a "number of sources of pressure" besides the DWP select committee's proposed plans, including The Pensions Regulator's discussion paper on trusteeship and fellow regulator FCA's asset management market study, which is proposing that pension trustees be required to report and assess transaction costs in an annual statement.

"It's like we all need a driver's license to drive, but if you ask for advanced driver's license – not many will be able to drive and then if you ask for a super advanced driver's license, there will be even fewer who can do it.

"More regulation is not a bad thing – but it is going to be more difficult to be a trustee," says Butcher.

Piecemeal legislation

In its discussion paper released over the summer, entitled *21st century trusteeship and governance,* The Pensions Regulator said it would consult over whether there should be minimum qualifications for professional trustees or chairs of trustees, and whether chairs should be required to produce a governance statement for defined benefit schemes.

The proposals are part of a package by the regulator to assess how trustee boards can meet the challenge of pension scheme governance in the changing pensions and economic landscape of the 21st century.

And although the regulator has said it is not looking to impose new standards of governance on trustees, experts believe that some of the proposals in the discussion paper will lead to a greater focus on trustee standards and governance.

With the DWP's consultation and

FCA's new proposals, many leading industry figures are questioning the need for further new standards in an industry that has already seen so much incremental change over the years.

"The UK pensions landscape is littered with 'somebody must do something about it' syndrome; but you cannot keep legislating in a piecemeal fashion," says BESTrustees chairman Alan Pickering. "This is a crazy way of building long-term framework."

And rather than further regulation, Pickering favours the campaign to create an independent pensions commission that will take stock of the current landscape.

"However well intentioned, this plan to consider further regulation is yet another example of trying to tackle yesterday's problem today without much thought for tomorrow's solutions," he says.

Mercer principal Mark Wilkinson says that with some 800 different pieces of pensions legislation in force, the focus should be on improving regulation.

"We need to be aiming for lesser complexity, not more," he adds.

Others agree that with increasing demands, it will become increasingly tougher to fill this largely voluntary role.

"It's become nigh-on impossible to be a lay trustee in today's day and age as the role has become very technically complex," says independent trustees Pan Group chief executive Steve Delo.

"Trustee meetings are heavy affairs – the agenda packs for trustee meetings can easily run to 200-300 pages – so trustees need to understand and navigate labyrinthine technical details very quickly," he explains.

To help in their training, The Pensions Regulator has said that it expects completion of its online trustee toolkit – its main training vehicle – to be an absolute minimum level of training for trustees, in the absence of any other formal training.

However, the regulator's own research found that half of schemes with one or more non-professional trustees did not believe that all of these trustees met the expected trustee knowledge and understanding standard and that half of non-professional trustees had undertaken no formal training at all in the last year.

In its discussion paper, the regulator is also asking for views on whether there should be an independent body regulating trustee standards or some form of mandatory qualification for professional trustees.

Funding

Another area for concern for trustees is the level of funding in pension schemes. Over the year, falling yields pushed up pension liabilities to record levels, resulting in widening pension deficits.

Pension liabilities of 5,794 defined benefit schemes increased to £1.6 trillion at end-November 2016, compared to £1.5 trillion in the previous year, according to the PPF 7800 Index.

Pension scheme trustees therefore face the complex and technical task of engaging with their sponsors to assess the strength of the employer covenant, and then working out prudent funding targets and appropriate recovery plans.

These then need to be agreed with their sponsor – who in challenging times is likely to be facing many competing demands for cash for investment, and from shareholders as well as the pension scheme.

The trend towards de-risking through liability-matching strategies and bonds seen over the past 15-20 years has also reduced expected returns, putting ever greater pressure on corporate sponsors.

"So we are now at a situation where since you are not getting enough returns from your assets, you have to get more money from your employer," says Butcher.

"So trustees need to be more careful and perhaps being 'recklessly prudent' is not the most sensible thing," he added.

Hefty challenges

For defined contribution (DC) schemes too, trustees now face several administrative and technical challenges to ensure the the scheme is fit for purpose for the individual investor.

"The task of a DC trustee is now almost as difficult as that of a DB trustee, if not more difficult," says Delo.

"There are several hefty challenges, like getting members to understand auto-enrolment, setting up a default fund and essentially managing against a whole bunch of difficult targets," he adds.

In the summer, The Pensions Regulator published a new code of practice for defined contribution schemes, which set out the standards that pension trustees need to meet to comply with legislation. The regulator also produced a tool to help trustees assess their scheme against the standards in the code, so that they can identify areas requiring improvement.

Key to facing up to these challenges is effective communication, says Delo.

"The actions of DC scheme trustees are now very visible, with chair's statements and value for members' requirements, and given the inherent uncertainty of outcomes at individual member level, clear communications are essential."

"The DC trustee now needs to work hard on their development, getting training and reading widely," he explains.

Butcher notes that trustees also needed to properly engage with members.

"We have to get out of our box and see the world through the members' eyes. We cannot be Luddite or closed-minded when it comes to engagement. But this may require energy that many trustees lack," he says.

Low in energy or not, trustees will need to access new reserves of strength to handle the challenges that lie ahead.

Written by Raji Menon, a freelance journalist

Redefining real estate's role with inflation-beating income returns

Hans Vrensen, AEW's new European head of Research & Strategy, highlights how inflation-beating income returns can be realised by going beyond the traditional investment styles and property types

Liability-driven investors need real income returns

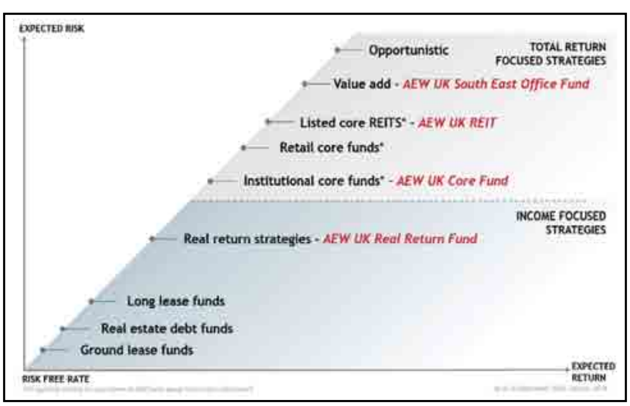
Since the global financial crisis (GFC), we have seen an increase in the number and size of investors looking for low risk and stable income returns in the real estate investment sector. These include pension schemes and insurance companies more focused on fixed income previously. But, as we have seen, quantitative easing has triggered low (or even negative) yields on most government and corporate bonds. With central banks' QE, a lack of bonds in some segments of the market poses an additional challenge. These factors have made it difficult for investors to match their assets to their liabilities. Most pension liabilities are directly or indirectly tied to inflation, making real income a requirement. Due to a reduction of options in other asset classes, this search for income from liability-driven investors has spilled over into the real estate sector. Traditionally, real estate investment managers have focused on achieving total returns, benchmarked against the MSCI/IPD or other relevant indices. However, the volatility of total returns has also forced existing real estate investors to de-risk their real estate allocation to lower risk and more stable income returns, even where schemes have substantial deficits.

Managers expand beyond traditional total-return strategies

In response to these investors' requirements, the real estate investment management industry has expanded its product offer to include more low-risk, income-focused strategies. We will address the low-risk nature of income-focused strategies shortly. These include real return, as well as long lease, ground lease and debt strategies. In the debt space, there is a broader range of risk-return strategies, with senior, stretched senior and mezzanine included. Many banks are still retrenching after the GFC and debt funds have seen an increase in market share. These income-focused strategies are a refinement from the mostly style-based total return-focused strategies. Risk and returns step up along a generally poorly defined spectrum from Core to Core Plus, Value Add and Opportunistic, as highlighted in graph 1. Depending on their size and requirements, pension schemes can access these investment strategies through a range of structures, including REITs, Limited Partnerships, Club deals and separate accounts.

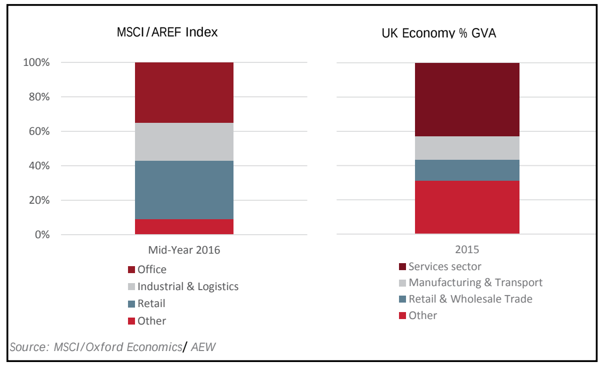
UK real estate to deliver inflation-beating income returns

Since the GFC, we have seen initial yields in both real estate and bonds tighten dramatically on the back of strong investor demand. With risk-free rates at record lows, real estate offers good relative value to mixed asset investors. However, initial UK prime property yields are now at or near historical lows. Further capital value increases are hard to envisage, especially given the political and macro-economic challenges posed by the Brexit referendum outcome.
In fact, the baseline PMA forecast for UK All Property total return is almost identical to the income return over the coming five years, as shown in graph 2. The 4.8% pa average income return on UK All Property is expected to beat 2.6% pa inflation rate by a good margin over the 2016-20 period. This forecast is not unreasonable given the historical precedent

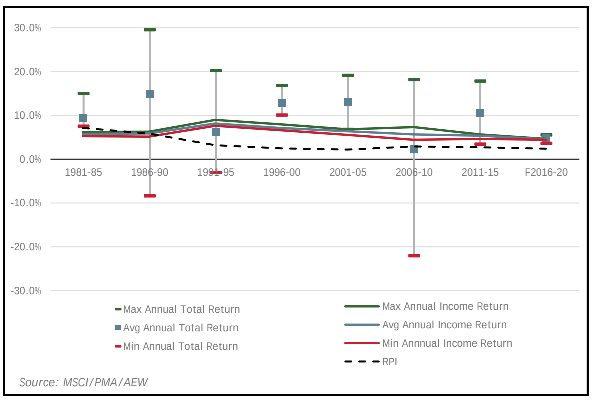


Graph 1

Graph 3



– the average annual income return has beaten inflation for five of the seven five-year periods for which there is data. This should prove attractive to liability-driven investors. The appeal of inflation-beating returns should become stronger with the recent UK and US political events triggering increased concerns for imported inflation. On the other hand, as the bars in graph 2 show, there has been a lot more volatility for total returns. This has been triggered by yield-driven capital value adjustments as investor sentiment pushes pricing.



Graph 2

Real estate offering a wider range of options than most expect

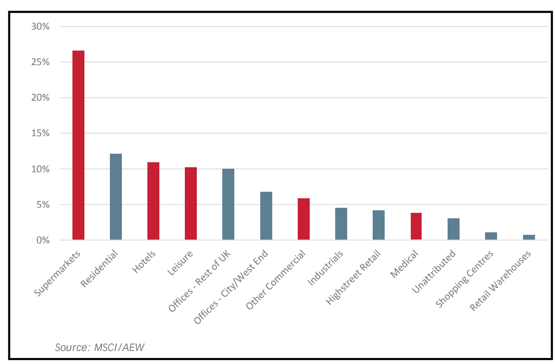
The spread between prime and secondary yields is still well above its historical long term average, offering lots of attractive returns away from prime. Apart from transcending traditional total return-focused investment styles, investors' need for real income can be met by focusing on non-traditional property types. Office, retail and industrial (ORI) are the three property types that dominate the benchmarks used by most traditional investment managers. However, these dominant three property types do not match the UK's economic activity well. Please consider graph 3 opposite. In stocks and bonds, there is a better match between investment opportunities and economic activity. Especially in the 'Other' category there seems to be an opportunity for creative managers to find income-focused returns. Other economic activity includes health care, education, utilities, leisure and entertainment. Each of these activities are performed in facilities not fitting in the ORI universe. Conventional wisdom in the property industry is that these categories of 'other' property require a higher level of operational expertise and careful consideration of the risks. However, for managers that can offer this, there is an attractive opportunity to realise strong income returns. Of course, there are also significant operational risks in retail and office investments as well.

Operators in non-traditional property types prefer long leases

Compared to the rest of Europe, the UK benefits from traditionally long-lease structures. Despite a recent shortening of average leases across the broader market, long leases remain an attractive way to lock in stable income returns. Most operators using non-traditional properties prefer to have long leases. When we take a closer look at the constituent parts of the AREF/IPD long lease funds index, we note that non-traditional commercial property types make up near 60% of the invested long-lease universe. Apart from the sizeable supermarket component, hotels, leisure and other commercial properties offer sufficient choice for investment managers to realise their clients' need for income returns, as illustrated in graph 4.

Long leases are good, but property fundamentals are the key to capital preservation

Whilst property income is capable of beating inflation, it is only one half of the return equation, as there is little point in having real income returns if capital is eroded by falling values and the impact of obsolescence as leases inevitably get shorter. Long income funds offering gilts-based returns have bid up the prices for long leases as gilt yields have fallen; they may also tolerate a degree of capital erosion for the certainty (and reduced risk) of lower relative returns. However by focusing on property fundamentals (as much as sustainable income) AEW believes it is possible to target and achieve higher total returns and preserve capital in real terms, even in the face of the inevitable rise of gilts over the longer term. And for the many pension schemes with substantial deficits the higher returns provide a solution for sponsors to help plug the funding gap.



Graph 4

Written by Hans Vrensen, European head of Research & Strategy, AEW

In association with AEW

Meeting everyone's needs

Changing administration providers is always a tough decision for trustees and sponsors, even more so when they have unusual requirements. Will the new provider really be able to meet them?

This was the challenge that was faced 18 months ago by the RNIB Retirement Benefits Scheme, the scheme for employees of the Royal National Institute of Blind People (RNIB) and of Action for Blind People, part of the RNIB Group. RNIB is the UK's leading sight-loss charity, providing support and advice to over two million people. This is probably well known, but what is possibly little known is that many employees and past employees of RNIB are themselves blind or partially-sighted.

So, quite apart from needing reliable pensions administration for their open and complex scheme (including a combination of DB-only members and true hybrid members whose DB and DC benefit split is determined according to a salary threshold), RNIB has a set of essential and challenging accessibility requirements. Indeed, number one in RNIB's list of values is that they are: 'Led by blind and partially-sighted people.' Their other, commendably simple, values are 'Collaborative, Creative, Inclusive, Open'.

This begins to give you a sense of how RNIB needed their chosen administration provider to behave, living up to the RNIB's standards – and if you visit www.rnib.org.uk, one of the quotes you will see is "I honestly couldn't believe how helpful people were in RNIB. They have a completely different way of treating people with sight loss, with dignity." This was how RNIB's pensions administrator needed to behave.

Guided by KGC Associates, the trustees issued a Request for Proposal. This was the first test, as some of the trustees themselves have sight loss and response materials needed to take this in to account. From there, the trustees and sponsor narrowed their selection to a small number of providers who could clearly perform the administration and then set about satisfying themselves that their other needs would be met. These included their 'technical' accessibility requirements, but perhaps more importantly involved assessing the softer skills of the contenders: "Do their people show the empathy and skills we need? Can they prove to us that they will work to our standards and values?" They answered these questions through references, a rigorous site visit and, later, a final meeting and discussion with their selection panel.

Delighted and privileged to have been selected as RNIB's new administration partner, our hard work began. Quite apart from our normal transition, covering a full back-to-source-documentation audit of the administration, data analysis, needs analysis and automation configuration, we needed to:

- Produce all letters and other documentation in a variety of typefaces, font sizes and media (supported as appropriate by the RNIB's excellent Webdocs service, which converts simple documents into Braille and other alternative formats, with more complicated documents being transcribed by a dedicated RNIB team)
- Identify on our systems which members need to receive letters from us in which format (over 10 per cent needed non-standard communications)
- Configure our systems so that when a task is being prepared for authorisation, the system automatically picks up the indicator and produces the output in the required accessibility format or prepares it for immediate transmission to Webdocs or the RNIB team
- Not only train our people in all of the above, of course, but also crucially in dealing with the needs of the blind and partially-sighted members they would come in to contact with (again, in the spirit of true partnership, RNIB helped greatly with this)

Twelve months after the service went live at JLT, is it working? RNIB group director of resources Rohan Hewavisenti sums it up:

"Our demands are very different from those of a typical scheme and so the transition was full of challenges for all parties. A year on, we are very satisfied with our new partner – they have collaborated with us very well and have displayed the other RNIB values that we hold dear. We look forward to a long and mutually beneficial partnership."

Written by Mark Adamson, director, JLT Employee Benefits

In association with JLT

Making it easy

Retiring from an occupational pension scheme needs to be easier. JLT has put in place two key measures to make this simpler for members and more straightforward for trustees

We have launched two initiatives to help members transfer their benefits more quickly and easily, based on the feedback we have received from members and trustees. Transfer of benefits at retirement is an increasingly popular option exercised after the 'freedom and choice' changes.

We are all familiar with the length of time it can take to transfer a pension with various rounds of paperwork, advice and quotations – the Treasury reports an average of 39 days for a transfer of a trust-based pension! Because of this we have worked with Origo to implement their 'Options Transfers Service'.

The Options system applies to DC pensions and JLT was the first third-party administrator to use this automated system for pension transfers.

We use this for selected transfers-in and as a result have reduced the average transfer time for a member to about six days, a whole month quicker than previously!

Secondly, as part of our drive to make things easier for members, JLT has deployed online identity verification for members at retirement. Instead of having the chore of sending in identification documents such as birth certificates, JLT has adopted technology that means we can complete that verification using the information available. This makes the process easier, more secure and less costly for the member, as well as letting them keep hold of these documents in case they need them.

The implementation of online identity verification has been very successful and JLT is currently extending this to other 'member events' such as address changes.

These are just two of the ways we are helping trustees give their members a better experience.

Written by Kenny Tindall, executive director, JLT Employee Benefits

In association with JLT

Automating transfers

Over £100 billion of pensions transfers have been processed electronically and automation is key to improving consumer outcomes, says Paul Pettitt, managing director of Origo

Enabling an average of eight calendar days for pensions transfers, it comes as no surprise that the benefits of Origo's Options Transfers service, provided to both industry and the end consumer, were recognised in the *Improving Pensions and Investment Transfers and Re-registrations* consultation paper published in December 2016.

Since the introduction of pensions freedoms we have seen a subsequent rise in transfer volumes, and so the spotlight has been pointed at the manual processing of transfers.

The ability for people to gain access to cash from their pension and use as they will, as well as the ability to pass on wealth through the pension to beneficiaries, in some cases free of tax, are major incentives for members to switch out of DB schemes – or DC schemes that do not facilitate the freedoms.

Bolstered by high transfer values, it is almost no surprise that recent research among financial advisers found that 75 per cent report a rise in client requests for DB pension transfers, with 40 per cent reporting 'significant' demand for such transfers. Statistics from Origo's industry recognised Options Transfers service has also shown an increase of 115 per cent of transfers into more flexible arrangements, such as SIPPs, since pension freedoms were announced.

At the same time, there has been a noted rise in the number of trustees looking to secure the best value and outcome for scheme members, resulting

in the need for bulk transfers. All of these factors are driving the rising transfer volume trend as people seek the greater control and flexibility available to them in respect of their retirement funds – all while schemes seek to reduce their admin costs and liabilities.

But, as we know, the complexities of transfers are such that the processes involved – not least the increased due diligence and security procedures that providers need to address in order to avoid pension liberation – can be intensely time consuming for end consumers, advisers, pension schemes and third party administrators (TPAs) alike.

This is exacerbated in some areas, such as bulk transfers, where often the traditional transfer processes still largely rely on manual keying and rekeying, and the use of unsecure spreadsheets to pass data between the ceding and receiving parties.

However, while some parts of the process, by necessity, are highly detailed and time consuming, other areas can be improved to speed up the process.

This is where technology can be brought to bear to create greater efficiencies in the process, making it faster for the member and also more cost effective for ceding and receiving schemes. The latter is where it can become most interesting for trustees and TPAs. To help inform decision making and assess where efficiencies can be achieved, Origo has developed a bulk transfers cost calculator that shows 'Pound and Penny', the bottom-line cost savings that automation of bulk transfers can bring to one organisation – visit www.origo.com/bulkcalc

In addition to securing and speeding up of the transfer process, whether it be for one or more members, Origo's Options Transfers service provides tracking and full recording of the start-to-finish transfer process, providing valuable performance and so audit Management Information (MI) for administrators.

This is an important point, as MI was highlighted in the consultation paper as an absolutely key element in driving 'better behaviour' among industry participants, as well as continuing to deliver improved outcomes for members.

By necessity, the pension transfer advice process will take time, but where the process can be accelerated it makes sense to do so. Despite growing transfer volumes and having processed over £100 billion of automated pensions transfers, Origo's Options Transfers service consistently delivers an average transfer time of eight calendar days for its 90-strong participating financial brands and, more importantly, their customers. It is clear that automation is central to progressing the pensions transfers process and improving the outcome for all involved.

Written by Paul Pettitt, managing director, Origo

AEW

Founded in 1981, AEW has over 30 years investment experience specialising in real estate. It is one of the largest investment managers in the world with circa €55 billion assets under management in North America, Europe and Asia.

The UK team has been providing solutions for pension fund investors for 20 years and has developed a range of funds and segregated accounts to meet their differing needs, from value add strategies to traditional core style total return and latterly a real return strategy.

The AEW UK Core Property Fund was launched in Q1 2012 and is the top performing fund in the AREF/IPD UK Quarterly Property Fund Index – All Balanced Property Fund Index – weighted average over three years.

At the start of 2016 the AEW UK Real Return Fund was launched largely as a solution for the increasing number of defined benefit schemes needing higher yielding real returns to match their cash flow liabilities and help scheme sponsors plug any deficit in funding that may exist.

For DC pension schemes and the increasing amount of private wealth money now classified as retail, the AEW UK REIT was launched in May 2015, to effectively replicate the core fund strategy in a listed company, as an alternative to daily dealing open ended retail funds.

Ian Mason, Portfolio Manager, AEW UK Real Return Fund

AEW

JLT Employee Benefits

JLT Employee Benefits has been providing employee benefits advice and related services to companies, pension trustees and individuals since 1982.

We are committed to working with our clients to gain a deeper insight and understanding of your business and your workforce to develop solutions that help your organisation to thrive.

Our success comes from being bold in our thinking and proactive in the advice we give. We understand the importance of innovative products that anticipate your needs while challenging ourselves to reach ever higher service standards.

With over 2,300 professionals across a network of 16 offices, our specialist teams work with you to create the right future for your business, your pension scheme and your individual retirement plans across the following products and services:

- Pensions administration (including Governance and Communications)
- DB scheme de-risking
- Actuarial services
- Investment services for private clients and corporates (consulting, fiduciary and asset management, discretionary management)
- Workplace Pension, savings and benefits consulting
- Wealth management

JLT

Origo

Origo is a not-for-profit, fintech company dedicated to improving the financial services industry's operating efficiencies, lowering costs for market participants and improving outcomes for consumers.

Origo is the catalyst that brings different industry organisations and groups together including; product providers, third-party administrators, employers, banks, platforms, tracing services, advisers, portals, software companies, and others to collaborate on identifying and addressing cost and efficiency issues in a non-competitive environment.

Always working in collaboration with the industry to solve common problems that no one individual organisation can solve in isolation, Origo continues to provide and develop valuable services.

Faster, safer transfers through Origo's Options Transfers service.

The Options Transfers service from Origo is the industry's only complete transfers service. Options Transfers enables scheme administrators to; remove paperwork (including discharge forms), significantly reduce transfer times from months to a handful of days, and analyse performance through on-demand Management Information including full tracking of transfers from start to finish. The Options Transfers service supports a full range of transfer needs as well as facilitating both individual for DB to DC and DC to DC transfers and multiple (bulk) member transfers.

Options Transfers is a tried, tested and trusted industry service that has been successfully operating since 2008. Enabling over 90 leading UK brands including names such as; JLT and The People's Pension, to provide their members with a safe and faster transfer experience, the Options Transfers service has securely transferred over £100 billion in pension funds since its launch.

For further information please visit: origo.com/options

ORIGO

Pensions Age

Pensions Age is the leading title targeting UK pension funds and their consultants. Published monthly in print since 1996, and daily online, we invest heavily in our circulation and content to ensure we are the clear market leading title. Our in-house editorial team of Francesca Fabrizi (Editor in Chief), Laura Blows (Editor), Adam Cadle (Deputy Editor), Natalie Tuck (News Editor) and Talya Misiri (Reporter) ensure we cover the latest news and topical industry issues to help our readers make the best informed decisions.

www.pensionsage.com is the leading website for pension funds, and we look to cover the breaking stories as they happen. With over 24,000 subscribers to our email newsletter service; we offer our readers an unrivalled service. At the core of this is high quality news-breaking journalism combined with in-depth knowledge of the target market and heavy research into data.
Pensions Age also runs highly successful conferences, and the Pensions Age Awards.

We also publish *European Pensions*, which targets pensions funds across Europe, as well as running the European Pensions Awards, Irish Pensions Awards, and Pensioni & Welfare Italia Awards. We also run an Italian language e-newsletter and website, and run an annual Nordics roundtable.

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Company Profiles