Putting the 'super' in superfunds

Joe Dabrowski explains why the PLSA's DB Taskforce is advocating the benefits of consolidating DB schemes

Although most people in the UK find pensions considerably less exciting than the average *Pensions Age* reader, those who have defined benefit pensions feel "quite lucky … because you keep hearing in the press that they're closing … it just makes you feel happy you've got one". This is the sentiment of a pensioner who was interviewed as part of the work undertaken by the Pensions and Lifetime Savings (PLSA) Defined Benefit Taskforce.

However, while members have confidence in their schemes, this may not necessarily be based in fact in all cases. Analysis undertaken by the taskforce suggests that around three million people with final salary pensions may only have a 50:50 chance of seeing their benefits paid in full. This is a significant risk for these individuals and managing these risks as well as the wider challenges facing schemes has important implications for the pension industry.

So how do we manage this and make sure that members have a better chance of receiving their benefits and maintaining confidence in the pension system? This was the question that the PLSA Defined Benefit Taskforce set out to answer and has addressed in a series of two reports, with the most recent being launched at its investment conference in Edinburgh this year.

The second report, *The Case for Consolidation*, outlines how consolidation and the creation of superfunds could tackle many of the issues facing DB pension schemes, alleviating the unacceptable, and mostly unrecognised, risk to scheme members.

Looking at these four different models of consolidation, the report made the case for greater consolidation to return security to DB schemes:

1. Shared services: combining administrative functions across schemes achieving cost savings through economies of scale.
2. Asset pooling: different schemes' assets are pooled and managed centrally while individual schemes retain responsibility for their governance, administration, back office functions and most advisory services.
3. Single governance: different schemes' assets are consolidated into a single asset pool; governance, administration and back office functions are also combined.
4. Superfund, full merger: designed to absorb and replace existing schemes. Employers and trustees are discharged from their obligations for future benefit payments, which would be paid from the superfund.

The case for greater consolidation is clear, particularly for small and medium-sized schemes. Through shared services, schemes could save on aggregate £0.6 billion per year and an estimated minimum of £0.25 billion per year if they pool their assets. If they consolidate their governance, administration, investment and back office functions, a further estimated saving of £0.36 billion would be added, totalling a saving of at least £1.2 billion per year.

These potential savings are worthwhile and should be pursued but won't make much of a dent in the £400 billion DB pension deficit. Superfunds offer a different type of consolidation, with further potential benefit including improving the security for savers in weak schemes by reducing the probability of their schemes failing from 65 per cent to 10 per cent or even less. This goes much further than making schemes cheaper to run, it's about making them last the distance.

So what is next? The PLSA Defined Benefit Taskforce is working on the third report, which will be launched later this year. This will look at the legislative and regulatory changes that are need to make superfunds possible, as well as a more detailed analysis of potential models. The potential impact on key stakeholders and the characteristics of the schemes that would most benefit from participation will also be reviewed.

At the same time, the PLSA will look to tackle many of the familiar issues facing schemes set out in the Department for Work and Pensions (DWP) green paper, such as inflexible and complicated regulation, challenges in scheme governance, funding, and navigating an increasingly-intermediated system.

This will help meet the challenges facing defined benefit schemes and ensure that members can continue to think of themselves as lucky.

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