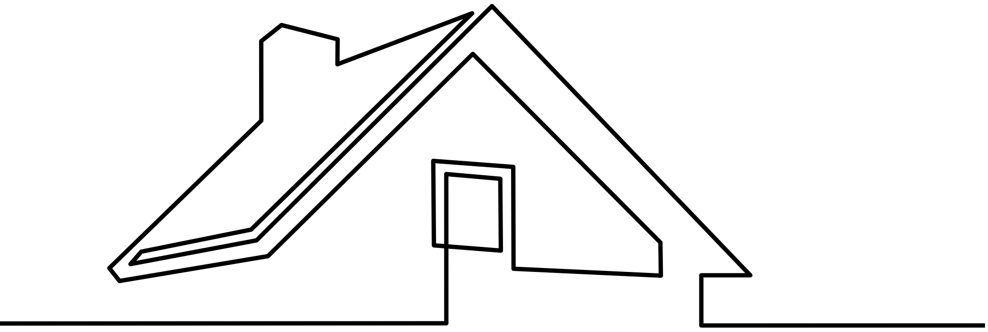

Summary
- The attractions of defined benefit master trusts (DBMTs) include the efficiencies of having a single trustee board and a single set of advisers and suppliers. This should mean lower running costs and higher levels of governance, particularly for smaller schemes.
- Many DB scheme trustees welcome the ability to transfer many of the time-consuming demands of their role to a DBMT, but some are reluctant to accept what they regard as a ceding of control.
- The new pensions bill is expected by many to propose a DBMT accreditation regime, along similar lines to that being introduced for defined contribution master trusts (DCMTs).

Under one roof

Master trusts have proved a successful consolidation option for DC schemes and are now being reviewed by a growing number of DB scheme trustees, reports Graham Buck

With consolidation very much the name of the game, it's a matter of conjecture how many UK defined benefit pension schemes there will be in five, or 10 years' time. How much will the figures have reduced compared with the current total of 5,450 DB schemes?

In recent months, much attention has focused on the two commercial consolidators – aka superfunds – entering the market. Clara-Pensions and The Pension SuperFund offer a further consolidation option for DB scheme trustees, alongside fiduciary investment management, DB master trusts or a buyout.

Mercer head of longevity swap consulting, Andrew Ward, notes that fiduciary investment management represents the 'first level' of consolidation and lately that market has been evolving and growing strongly. Buyouts are too expensive an option for many DB schemes and the number that move to the superfunds remains to be seen, but could be limited – Clara reported last October that it was in talks with "north of 40" DB schemes.

This leaves a further option, that of DB master trusts (DBMT), as an effective solution for scheme trustees seeking to minimise risk. Aon head of UK retirement policy, Matthew Arends, notes that a DBMT has several distinctive features that make it the most appropriate option in various situations.

"Specifically, a DBMT consolidates the governance arrangements of schemes by having a single trustee board and a single set of advisers and suppliers across all of its sections," he explains. "This offers the prospect of reduced running costs and higher levels of governance, particularly for smaller schemes."

DB schemes choosing to go down this route transfer their assets and liabilities when they join, with the current employer maintaining support to the scheme once the transfer takes place. Mercer UK head of fiduciary management, Ben Gunnee, describes DBMTs as the "next step of evolution" after fiduciary investment management by combining its advantages with additional benefits of consolidation, such as improved pricing and better decision making.

"You also get the bonus of professional trustees sitting on a master trust. That's a distinct advantage for many schemes who seek suitably qualified individuals to become trustees but often find no-one interested among the younger members, or ready to take on the many duties and responsibilities."

One-stop shop

Today's more complicated investment environment, coupled with a lack of investment expertise among many trustees is a further reason why DBMTs make sense for many DB schemes, adds TPT Retirement Solutions head of direct distribution, Adrian Cooper. "They can provide access to various asset classes that are attractive but not easy to get into, particularly for smaller schemes – which, in addition, would otherwise find them prohibitively expensive."

TPT, originally established in 1946 as the Social Workers Pension Fund, became The Pensions Trust in the late eighties. In late 2016 it rebranded again, with the aim of doubling its size and becoming the leading DB consolidator.

"There are around 10 DBMTs in the UK and we're the largest with 43 schemes and around £9 billion of assets under management," Cooper adds. "We focus on schemes with between £25 million and £750 million of assets under management and – unlike the superfunds – TPT takes open schemes and not just closed ones."

He describes the DBMT as effectively a "one-stop shop" for managing DB schemes. "Many of them have their own fiduciary manager and investment consultant, trustee boards, a scheme secretary and a host of other service providers, which don't make for efficiencies or economies.

"All these services can be transacted by a DBMT and brought together under one roof. So DB schemes have their own trustee boards, whereas we have one overarching board of professional trustees and an executive team to whom authority is delegated.

"With us, the link with the sponsor remains intact. What's more, each scheme in the master trust is ring-fenced from others and has its own separate funding and investment strategy. We review each scheme's funding, investment and covenant, and we also talk with the sponsor to decide an appropriate strategy – for some it will be self-sufficiency, while for others it will be clearing the debt."

However, a note of caution is struck by Lane Clark & Peacock partner, Alex Waite, who comments: "Master trusts for DB schemes are a useful tool in the range of corporate solutions available, as they enable certain aspects to be delegated. But their pros and cons need careful consideration before choosing which solution to apply in specific circumstances."

Colleague Dan Mikulskis agrees, noting: "Master trusts can yield some of the classic benefits of scheme asset consolidation, such as: cheaper asset management fees, access to more sophisticated investment strategies and assets, improved governance to make swifter decisions and address risks.

"However, in some of these areas, roughly equivalent benefits can be gained through other means."

Another consideration is that some scheme trustees, far from welcoming the chance of transferring duties and responsibilities, sometime resent what they regard as ceding control.

"It's a fact of life that consolidation of DB benefits is more likely than not to involve the existing trustees falling out of the picture," notes Sackers partner Eleanor Daplyn. "This is certainly true where the consolidation option is a DBMT.

"Trustees have often been involved with their scheme for many years and rightly feel a sense of responsibility – it's natural to be concerned that another trustee board may not approach things in the same way, have the same priorities or know enough about the history of your scheme."

Daplyn suggests most of these concerns can be allayed by considering that the receiving master trust is run by trustees who share the same fiduciary responsibilities. "Master trust trustees are typically professionals, which means they bring additional expertise to offset their lack of background knowledge with a particular group of members or set of benefits. Longevity and succession are also important – a DBMT can manage succession and ensure a flow of high-quality trustee candidates that most private occupational schemes can only dream of."

Accreditation regime

Concerns could be further allayed by introducing a DBMT accreditation regime. While the Department for Work and Pensions' recent consultation focused principally on the commercial consolidators/superfunds, a broader review of DB consolidation is expected to feature in the new pensions bill. The timing of this legislation is unclear although "we should have a better idea by the early part of the summer", says Daplyn.

"What we have to go on meanwhile is the consultation itself, which envisages an authorisation and supervision regime similar to the one that recently came into force for DC master trusts (DCMT)."

Cooper says that TPT would welcome such a development and has already applied for its DCMT to be authorised by The Pensions Regulator (TPR). "The regulator imposes very rigorous requirements, which for some DCMTs have proved overly demanding. So the number is likely to reduce, although those remaining will be of very high quality."

He highlights several key features that could potentially feature in any DBMT accreditation regime, such as: costs listed on a per member basis arrived at by an agreed formula; details of the mechanism by which trustees can be appointed and removed; historic investment performance; and the scale of funds under management.

While there's no 'burning platform' or compulsion to hasten consolidation, there are several changes that might persuade stakeholders to explore DBMTs, suggests Hymans Robertson trustee secretary and pensions manager Lindsay Davies.

They include: changes in corporate personnel, particularly the departure of a long-server with pension responsibility; the growing challenge of finding suitably qualified trustees and efficiency and economy. For example, DBMT Citrus Pensions believes it can get sections to buyout faster and attain better terms at point of settlement, while there can be concerns about adviser value for money.

Other factors that might lead to funds exploring DBMTs include the option of more innovative approaches, such as the use of digital and capital efficient investments, and TPR's move towards enforcing a stronger "comply or explain" regime for all DB schemes on scheme funding. DBMTs give stakeholders the opportunity to place that responsibility into a strongly-governed arrangement in which effectively meeting that requirement will be the norm for sections and sponsors whose circumstances differ widely.

Written by Graham Buck, a freelance journalist