Summary
• The range of consolidation options for trustees is widening, including better regulation of master trusts and 'superfunds'.
• There are also many ways that schemes can drive efficiencies without consolidation, including investment pooling.
• Consolidating trustee boards and use of sole trustees can also help to streamline governance.

Bright ideas

Maggie Williams looks at the many ways a scheme can streamline its processes

As governance burdens on trustees increase and the cost of running a pension scheme heads in the same direction, all schemes will be looking for more streamlined and cost-effective ways of working.

For some, that will mean consolidation. Speaking at the PLSA's Annual Conference, Department for Work and Pensions (DWP) defined benefit consolidation lead, Des Healy, re-iterated the government's support for consolidation, whether through master trusts (DB and DC) or commercial consolidator 'superfunds' for DB schemes.

However, there will still be trustee boards that don't want to merge with other schemes and are currently unable to buyout, but still need to find efficiencies that ensure their scheme remains sustainable and well run for the long term.

Investment pooling

One well-established option is to pool investment management. Local authority pension schemes have been compelled to carry out investment pooling as part of the radical reworking of their sector – could the same approach work for private sector DB and DC schemes? River and Mercantile head of DC solutions, Niall Alexander, sees fiduciary management as the closest equivalent. "This is the most common method of pooling, which enables schemes to improve the efficiency of their investment returns net of all fees. The LGPS approach uses a similar model."

Willis Towers Watson senior director, Gareth Strange, says that the scale of assets under management at a fiduciary manager should mean savings on asset management fees. "With significantly higher assets under management, fiduciary managers are able to buy assets at significantly lower cost than individual schemes," he says. He adds that fiduciary management also delivers other efficiency advantages such as access to greater innovation and a nimbleness to respond to market changes that standalone trustee boards would be unable to achieve.

However, although it reduces the governance burden for trustees and enables managers to negotiate lower fund management fees, fiduciary management may not always reduce overall costs for a scheme once the fiduciary manager's own fees have been taken into account.

Investment platforms are another option for improving investment efficiency. "Investment platforms have traditionally been thought of in the DC world, where you can achieve buying scale at an individual level. But we are starting to see them being used for DB plans as well," says LCP partner, Jeremy Dell. "Schemes can't pool assets with another scheme unless they merge or use a fiduciary manager, but they can achieve a similar effect using a platform. It offers access to funds and fund management that schemes wouldn't otherwise be able to use."

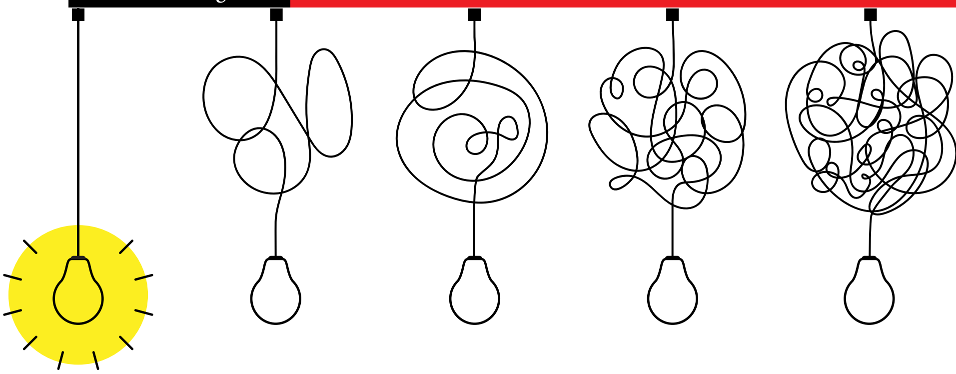
Administration efficiencies

While there are established strategies that enable trustees to benefit from efficiencies of management in their investment strategy, pooling other aspects of pension schemes such as administration, is much harder to achieve. "Each scheme has its own set of rules and benefits, so the efficiencies of pooling administration without consolidating are less clear," says Alexander. Unless benefits are harmonised across schemes – a controversial and costly exercise – there is little potential for pooling administration. "Harmonising benefits might lower costs in the long term, but the communications, actuarial fees and other potential heartache involved in the process mean there is little advantage to doing this," says Strange. He adds that, even after harmonisation, the reduction in ongoing administration cost is likely to be minimal.

While pooling administration will not be a workable option for most schemes, new technologies offer a raft of other ways to drive efficiencies. Alexander cites tasks, such as maintaining accurate member records and delivering good quality communications, that can be improved substantially through good use of technology.

"Offering DB members access to online quotations is another major way of improving administration efficiency," says Strange. "Most administrators offer a fixed-fee service and then charge per additional activity. As the volume of requests for quotations has increased, so has the additional activity costs for schemes. However, if quotations can be carried out online without the need for extra work by the administrator, those fees will disappear – and the time demands on schemes will also reduce."

Administration is just one way in which technology can drive efficiencies for schemes. It also has a part to play in improving actuarial processes. "Much actuarial work is now commoditised and firms that have invested in technology



are able to deliver services at a lower cost. Schemes don't expect to spend a fortune on actuarial valuations any more as so much of the process is now automated," says Dell. "Across the board there is value-add from using technology, as well as improvements to efficiency for schemes."

Consolidating advisers

Strange argues that using a single consultancy for administration, actuarial and investment services can also bring efficiencies. "Using a single provider can reduce friction and costs," he says. "There's more efficient use of data between systems and the same consultant's investment, actuarial and administration provision should all link up effectively to bring the scheme's strategy together."

"Consolidating advisers and investment managers across schemes means bigger volumes and that drives fees down," agrees Dell. Strange adds that using a single provider for all consultancy services brings efficiency benefits both within a single scheme, and across multiple schemes run by the same sponsor if all consultancy services are run by the same provider.

Consolidating trustee boards

Dell also sees potential efficiencies in consolidating multiple schemes that have the same sponsor. "We see a strong drive from sponsors running many schemes to merge them together, and offering trustees incentives to do so," he says. Dell adds that as schemes become better funded, it becomes easier to achieve this.

While some sponsors might stop short of a full merger of their schemes, Dell says that many are also exploring the idea of a common trustee board across multiple plans. "While the traditional trustee board model has worked well in the past, companies are now struggling with the governance burdens trusteeship demands – and these are increasing further. Sponsors are looking at more streamlined governance and starting to explore consolidated trustee boards for defined benefit," Dell says.

Aon head of DC consulting, Sophia Singleton says that she is seeing a similar trend amongst DC schemes. "There has been substantial regulatory change in recent years and much more is required of DC trustees now. Schemes are asking whether separate boards are driving better value, or whether they are just a governance burden. For many employers with multiple DC schemes, rationalising and consolidating trustee boards is a very sensible move."

Sole trusteeship

Scheme sponsors are also exploring sole trusteeship as a way of improving efficiency. This replaces the trustee board with a single trustee responsible for all governance. "Companies that are struggling to find member-nominated trustees that are still in the business may be looking at more streamlined governance and heading to sole trusteeship," says Dell.

Sole trustees are typically independent professional trustees who will act as a trustee for a number of different schemes. As such, they may also be able to bring economies of scale for all the schemes that they work with. "If a sole trustee works for a professional trustee group, they can hire consultants or fund managers consistently across their whole trustee book and drive further efficiencies through commonality of advisers," Dell adds.

Master trusts

Auto-enrolment raised the profile of DC master trusts and has driven rapid growth for a handful of well-established schemes. That growth means that they now operate on a much larger scale than many standalone trust-based schemes, with the associated efficiencies that brings. As a result, Singleton says an increasing number of DC schemes are now exploring the option of moving their members into a master trust. "Trustees struggle with the time required for DC governance, especially if they are responsible for a DB scheme as well. When they start to look for efficiencies from outsourcing administration, governance and investment – that's really a master trust. There are other reasons to move too, such as better use of technology, future-proofing and scale."

While DB master trusts have been active in the market for many years, there has been very little take up and activity in this area, particularly in comparison to DC arrangements. But with plans in the DWP's pipeline to set up an accreditation regime for DB master trusts, and enable trustees to find a meaningful comparison between a scheme's current situation and how it would fare within a master trust, this could also provide a more wide-ranging choice for DB trustees in the future.

The next year looks set to see the consolidation sector become more structured, with clearer regulation and more choices available to DB schemes in particular. But if master trusts and commercial consolidators don't suit the needs of every scheme there are still plenty of structural changes and outsourcing options available to enable all trustees to improve scheme efficiency.

Written by Maggie Williams, a freelance journalist