

Is good governance only for large pension schemes?

By: Natasha Browne | 26 Jun 2015

The Pensions Regulator (TPR) has been very vocal in its opinion that employers should auto-enrol through master trusts or group personal pensions (GPPs).

Executive director for defined contribution (DC) Andrew Warwick-Thompson has said the regulator is not "sufficiently confident" that quality will be assured in the small scheme market. In regulator-speak, this is pretty strong stuff.

Publishing a report on how well trust-based DC schemes were meeting its 31 quality features, the watchdog discovered over 85% of large schemes and master trusts had been reviewed against the features. However, that figure plummeted to 39% for small schemes.

The study also showed over half of small schemes knew little or nothing about the quality features, while 22% said they were not aware of them at all. No master trust or large scheme admitted they knew nothing, and the majority said they knew at least "quite" a lot.

Warwick-Thompson said TPR accepted that many small schemes would never achieve its governance standards. And these standards have been raised in recent months, with increased governance requirements and the 75 basis points charge cap applied to schemes in April.

Trustees also have to confirm through the newly introduced chair's statement how their schemes are meeting the governance objectives or risk a fine of between £500 and £2,000, explains Veratta chief operating officer Monica Cope.

She says: "The governance requirements represent the standards that trustees are expected to attain, and these standards shouldn't be proportionate to scheme size."

Faye Jarvis (pictured), of counsel at Hogan Lovells, only sees governance requirements becoming more stringent in future. She says: "It's likely there will be greater regulation so this challenge isn't going to go away."

Silverman Sherliker head of pensions Jennie Kreser is not surprised that small schemes are lagging behind. She says: "They are probably less able and/or willing to pay for advice."

"I think the recognition that they are not going to be able to reach the heights of perfection that the regulation universe has suggested, is just a good recognition of that fact."

Punter Southall head of DC consulting Alan Morahan adds: "For particularly small schemes it often isn't financially viable to spend the time and money needed to comply with the DC code."

"It therefore makes sense for trustees to consider alternative vehicles, such as master trusts and GPPs, and we are seeing evidence of this."

Nick Cook, a senior DC consultant at Towers Watson, says it is only logical for the regulator to signpost employers to master trusts and GPPs if it has accepted that small schemes will always struggle.

He adds: "Pension schemes should be able to justify their own existence in terms of how well members are being looked after and what the alternative would be."

Cope agrees that TPR is right to propose alternatives. She says: "Trustee boards must comply with governance standards to ensure the sound administration of the scheme and to protect the benefits of pension scheme members."

"If there is evidence to suggest that small schemes are failing to meet minimum governance standards, then TPR is absolutely justified in recommending master trusts and GPPs that can conform."

Jarvis thinks the new legislative requirements fall more acutely on small schemes, however. She says: "Things like assessing whether the charges in transactional costs provide good value for money are quite a challenge."

"There's a lot of debate in the industry about what is good value for money. If you're a lay trustee of a small scheme where perhaps you're less plugged into the industry, carrying out an assessment is going to be quite difficult."

"You may find you have more cost restraints in terms of the advice and assistance you can procure."

Is bigger better?

The regulator measured performance against a code of practice that was developed before the pension freedoms, Towers Watson's Cook highlights. He thinks the reforms could be another push towards consolidation.

He says: "For example, however well designed a default investment strategy is, there will be more members whose choices at retirement will make it unsuitable."

"This puts more onus on schemes to help members understand their options and engage with them. Some employers will want their own schemes to do this; others may look to outsource their pension arrangements."

"However, 'bigger' does not always mean 'better'. If the resources are there to do things properly, there can be advantages in a bespoke approach; where they are not, employers may be better finding a provider who can do it for them."

Large schemes have the benefit of scale, which often helps them secure lower charges. But master trusts or GPPs lack that employer/employee relationship that can be highly valued by a workforce, according to Jarvis.

She says: "I think there are advantages to trust-based schemes and I do feel that it's a bit harsh to just say 'they'll never comply, that's it' and then have a push to join a master trust. It's a bit of a cop out."

"I appreciate there are probably constraints on the regulatory budget for that sort of thing, and it is easier to regulate a smaller number of larger schemes."

"But that said, I don't know whether there's scope to design a training programme for trustees of small schemes on good governance, that focuses on the issues they're likely to be facing."

Jarvis says there has always been debate on trust-based versus contract schemes. She adds: "I think certainly with some of the bigger schemes there's a lot of innovation going on in terms of member engagement and that sort of thing, because it's all tailored to their particular workforce."

"I think you probably have more chance of getting people to engage because it's specifically linked to your employer and the kind of things you are doing in your workforce."

"The communications are sort of designed around that and I think that is probably something that big contract-based schemes can't necessarily always do."