SCHEME MANAGEMENT

The incredible shrinking pensions industry

Scheme consolidation is high on the agenda for some European regulators. Maggie Williams **explores what that means for plans and providers**

WRITTEN BY MAGGIE WILLIAMS, A FREELANCE JOURNALIST

In 2007 there were 7,800; now there are 5,588. Back in 1997 there were 1,060, but in 2017 there were 268. Once there were 89, but they have become seven. And at present there are nearly 150,000 but that could soon drop to hundreds. What are they?

Stumped? The number of UK defined benefits schemes paying the Pension Protection Fund levy; pension funds in the Netherlands according to De Nederlandsche Bank (DNB); UK local government pension arrangements; proposals for the Irish pension system.

Based on this brief pop quiz, you could be forgiven for thinking that the European pensions market is shrinking. But it wouldn't take long to put together statistics showing the opposite view: global pension assets under management (AUM) grew 4.3 per cent between 2015 and 2016 according to Willis Towers Watson's *2017 Global Pensions Assets Study.* Over nine million people are now saving into UK pensions as a result of auto-enrolment, and with a similar regime mooted for Ireland there is plenty to be positive about.

"The European pensions market is not shrinking," says Eversheds Sutherland partner and head of pensions Francois Barker. "But there is consolidation, particularly in jurisdictions such as the UK, Netherlands and Ireland as a refinement to a well-established system."

For the most part, the benefits of consolidation are economies of scale, which should lead to improved value for members, and demands for better quality governance. But ultimately pressure from regulators, combined with European-wide directives such as IORP II, have been the bigger drivers.

United Kingdom

Consolidation is a focus for both the UK's defined contribution (DC) and defined benefit (DB) markets. In DC, most of the activity is focused around single-employer trust-based schemes moving into group personal pensions (GPPs) and master trusts. With DC pension scheme bulk transfers set to be simplified from April 2018, transfers into master trusts in particular could accelerate. "Big schemes are also making this move, not just small or medium-sized ones as we might have expected," says Mercer partner and director of consulting Brian Henderson.

But consolidation in DC isn't restricted to single employer trusts. The group personal pension (GPP) and master trust provider markets have also been contracting. Scottish Widows' acquisition of Zurich's workplace pensions business in 2017 is just a recent example of a longer-term trend amongst GPP providers. The Pension Schemes Act 2017, which imposes tougher standards on UK master trusts, will mean smaller, less well-governed providers are unlikely to survive. "We will see the master-trust market shrink to larger, authorised trusts only," says Pensions and Lifetime Savings Association (PLSA) head of investment and governance Joe Dabrowski.

The need to find a workable solution for stressed UK DB schemes has put consolidation in the spotlight. It could be argued that bulk annuity purchases such as buyouts or buy-ins offer a form of consolidation, but at a cost. DB master trusts enable some pooling of assets and back-office administration but not liabilities. Services such as fiduciary management also offer schemes a form of consolidation in asset management.

"Consolidation of assets is the easy part," cautions Barker. The UK has yet to find a way to consolidate liabilities as well. Even the local government pension scheme's merger of 89 UK local authority schemes into seven collective 'pools' has stopped short of combining the underlying scheme liabilities.

A government white paper due in February 2018 could further explore consolidation for DB schemes, but is still likely to stop short of addressing liabilities. "It's difficult to wholly consolidate schemes unless they offer very similar benefits," says Dabrowski. Barker adds that consolidating liabilities will require primary legislation. "That begs the question of whether anyone has the political courage to do this."

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Netherlands and Ireland

Perhaps some answers are to be found in the Dutch market, where scheme consolidation is already a fact of life, as a result of sustained pressure from regulators since 2010. "There has been a concerted effort in the Netherlands to reduce the number of schemes, and even very large plans have been encouraged to consolidate," says Dabrowski. "That's driven better governance and more efficiencies."

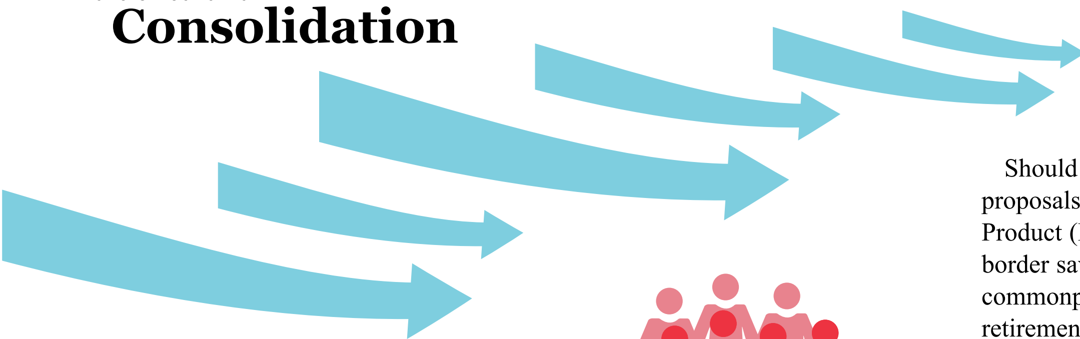
The pressure has paid off. According to DNB, the number of Dutch company pension schemes fell by 70 per cent between 2007 and 2017, with schemes transferring both assets and liabilities to other providers, or carrying out mergers. One recent example is Unisys's €485 million pension fund, which announced plans to liquidate in June 2017 and place the majority of its assets in the APF pension fund.

While DB has traditionally dominated the Dutch market, the €5.2 billion DC-based PPI market has seen significant growth – and also provider consolidation – since 2011. Two providers, Aegon and Nationale Nederlanden, now cover two thirds of the market.

The UK and Netherlands are in the vanguard of scheme consolidation, but Ireland may not be far behind. The country's plans to introduce auto-enrolment is forcing close scrutiny of schemes and providers, driven by its Pensions Authority's 2016 *Reform and simplification of supplementary funded private pensions* paper. "It is a stated ambition in the Irish market to move to a master-trust governance model," says Irish Association of Pension Funds CEO Jerry Moriarty.

"Many of the 148,000 schemes in Ireland are very small," says Tor Financial managing director David Harris. "There is an argument that master trusts are needed in order to help consolidate these and to prepare the ground for auto-enrolment."

"In addition to the drive towards master trusts in Ireland, IORP II will become too much for some schemes



SHOULD EUROPEAN COMMISSION PROPOSALS FOR A EUROPEAN PENSIONS PRODUCT GAIN TRACTION, CROSS-BORDER SAVINGS COULD BECOME MORE COMMONPLACE

to manage," adds Moriarty. The EU directive must be implemented in member states by 13 January 2019 and will introduce stringent new demands, including stress testing. That could prove a further driver for consolidation in many parts of Europe, including Ireland, as schemes struggle to comply.

Cross-border consolidation

The complexities of combining schemes within a single country are as nothing compared to the challenges of cross-border consolidation, where incompatible pensions regimes and legislative requirements have proved prohibitive. But even that is changing. The chemical company Dow announced in January 2018 that it would consolidate its European DC plans into a single cross-border pension based in Belgium. It has already moved its Dutch DC assets into the UnitedPensions scheme and has plans to move its DC assets from the UK, Belgium, France, Germany, Italy and Spain over time.

Should European Commission proposals for a European Pensions Product (PEPP) gain traction, cross-border savings could become more commonplace. PEPPs are a portable retirement savings vehicle which could be used anywhere in the EU. Although they wouldn't replace occupational schemes, they could offer mobile workers an alternative to accumulating small, disparate pension pots in different countries and offer providers a Europe-wide pool of potential customers.

Parts of the European pensions market are clearly consolidating, in terms of the number of active schemes in the market. Regimes such as auto-enrolment in the UK will continue to drive assets into occupational pensions, and will favour economies of scale. But over the long term, these changes will also mean a shifting market for providers. As regulations change to facilitate consolidation, it will be up to providers to respond. There may be fewer schemes, but the governance demands, assets under management and pressure to manage risks and costs will be greater than ever before. ■

Effect on providers

Fewer but larger schemes also mean fewer but larger contracts for advisers and asset managers. The consultancy market has already seen significant consolidation over the past 10 years, and 2017's merger between Aberdeen and Standard Life Investments showed that the asset management market is also undergoing change.

Employee benefits consultants (EBCs), are responding by changing their business models. "EBCs are creating products that drive assets under management," says Harris. "Every major UK EBC now has a master-trust solution, for example. The days of pure consulting without platforms or products is becoming a thing of the past."

Asset managers, argues Henderson, will also need to evolve. "Some fund managers are a fish out of water at the moment in pensions. They need to create attractive, practical offerings for DC, but that will happen over time. These are new environments for people to fit into, and really we should be seeing a renaissance in services."