Aon Hewitt
Retirement and Investment

Pensions Administration Survey 2015

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Executive summary

The 2015 Pensions Administration Survey paints an interesting picture of the administration landscape.

While over half of respondents still see defined benefit as their organisation's main pension provision, more than two fifths believe that pensions will form a less integral part of benefits overall in the future.

Outsourcing levels, and the perceived quality of pensions administration, whether outsourced or not, remain fairly static, suggesting that the administration market is not currently undergoing radical change.

Cost remains a key driving force for pensions administration decisions, and a major inhibitor when it comes to delivering on priority projects. Among those who have taken the decision to outsource, cost has been the primary driver. And while schemes are clear on their immediate priorities, a limited budget may impact on their ability to deliver on these objectives: a fifth of schemes plan to devote no more than 5% of their administration budget to their priority projects in 2016.

This is not the only disconnect between schemes' aims and the structures they have in place to achieve them. While almost half of schemes want their administration provider to be able to deliver a broader, integrated offering covering other pension services, many are not currently experiencing this. And although nearly half believe there is a correlation between price and service quality in pensions administration, a similar number is not prepared to pay more for a better quality service.

Priorities driven by external influences are evident: GMP reconciliations, in response to upcoming HMRC changes, are the biggest priority project by some way for schemes, although for this and other projects, the quality of scheme data is expected to hinder or increase the cost of delivery.

The new pensions freedoms are also exercising schemes' minds: the majority believe they will fundamentally change the decisions members need to make, although an alarming number of schemes are not planning segmented communications around this – nor are in possession of the membership data to allow them to do so.

With such a lot to focus on, schemes and their administrators have plenty to think about when it comes to administration practice and priorities. We hope that the findings and suggestions here provide some positive direction.

The 2015 Pensions Administration Survey was carried out in Q3 2015, using an online questionnaire. The survey received 243 responses, the majority from those in corporate pension and pension trustee roles, across a wide range of industry sectors.

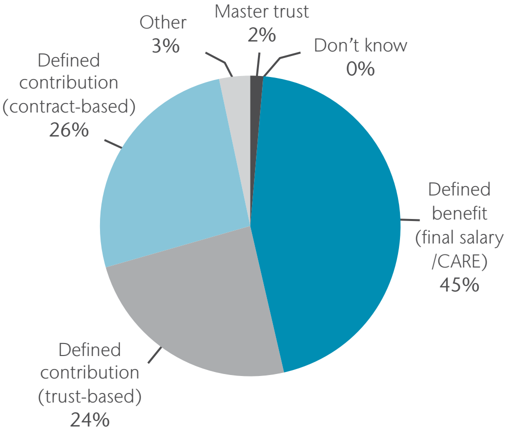
Key findings

- 53% of survey respondents still see their defined benefit (DB) arrangement as their primary pension scheme
- 42% believe pensions will form a less important part of benefits in future
- 70% currently outsource their scheme administration
- 45% want to receive administration from a provider that can deliver a broader, integrated offering, potentially including consulting, actuarial and/or investment advice
- Cost was the biggest driver for those who have outsourced, while control is the largest incentive for retaining administration in-house
- The perceived quality of pensions administration has remained static for the majority (57%) over the last 12 months. This is very consistent with the findings of the last two surveys
- 46% agree or strongly agree that there is a correlation between price and service quality in administration…
- …but 40% are not prepared to pay more for a higher-quality service
- GMP reconciliations are the biggest priority project by some way for schemes (22% say this)…
- …but again budget is an issue, 22% plan to devote less than 5% of their budget to their priority projects
- Data quality is also a major issue – 21% believe the quality of their data will hinder the delivery of GMP reconciliation projects and 20% that it will add to the cost. All priority projects identified by respondents are expected to be negatively impacted by the quality of scheme data
- 60% believe Pensions Freedoms will fundamentally change the decisions members need to make….
- …but 51% do not deliver segmented member communications and have no plans to do so
- …while 31% cannot say what proportion of members will be 55 next year

The pensions landscape

The survey asked respondents about the types of pension scheme their organisation currently offers. The majority of respondents (45%) offer defined benefit (DB) schemes, which we defined as covering both final salary and career average (CARE) schemes. 26% provide a contract-based defined contribution (DC) scheme, with 24% offering trust-based DC.

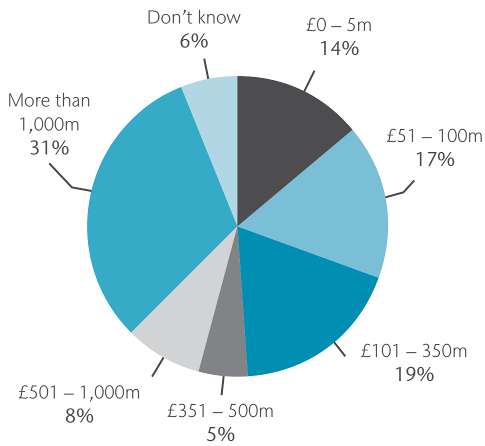
What type of pension scheme(s) does your organisation currently offer?



53% of those responding cite their DB scheme as their organisation's primary pension arrangement; 24% say the same for contract-based DC and 23% for trust-based DC. Schemes' responses to the rest of the survey were in relation to their primary arrangement.

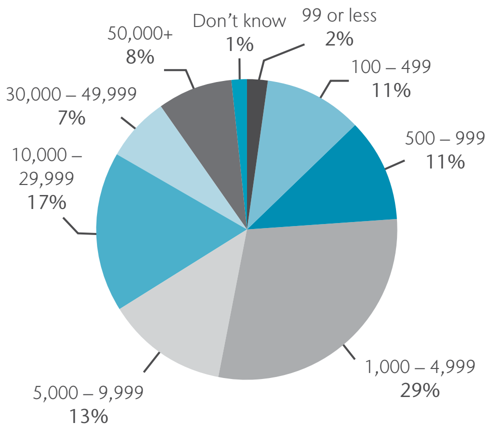
The majority of respondents (31%) have a main pension scheme with assets of over £1000m. 19% of respondents have schemes with between £101m and £350m and 17% have assets of between £51m and £100m.

What is the approximate size of the assets in this scheme?



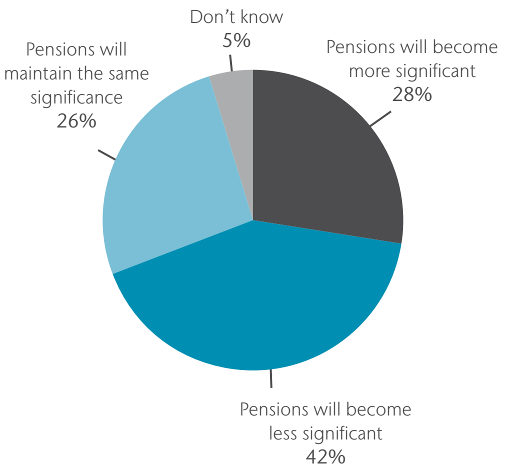
The survey represents predominantly mid-sized schemes in terms of membership: 29% of schemes have between 1,000 and 4,999 members while 13% have between 5,000 and 9,999 and 17% between 10,000 and 29,999. 8% have memberships of 50,000 or more and 2% have fewer than 100 members.

What is the approximate total number of members in this scheme – including actives, deferred and pensioners?



The majority of respondents to the survey believe that pensions will remain an important part of the benefits mix in future; 54% think that pensions will either become more significant (28%) or maintain the same significance (26%). 42%, though, believe that pensions will become a less significant part of overall benefits in the future.

Do you think pensions will become a more or less significant element of overall benefits in the future?



Those who believe pensions will become less significant were asked why this was. 21% believe that there will be a greater awareness and/or perception about the value of alternatives to pensions. 18% think that increases in pensions legislation will cause the change, while a loss of confidence and/or trust in pensions and a decrease in employee engagement and interest in pensions are both cited by 17%.

Wider corporate or economic reasons are given by some respondents: 13% believe a lack of disposable income will decrease the significance of pensions and 10% think that company strategy – for example, around risk reduction objectives – will have an impact.

Aon Hewitt perspective

DB schemes still represent the primary pension provision for just over half of the survey's respondents. While this is the case currently, as DB membership decreases over time and new joiners start almost exclusively on DC plans, we expect to see this situation change in coming years, as DC scheme membership grows.

Similarly, we expect the position with regard to master trust arrangements to change. Master trusts are currently offered by just 1.5% of the respondents to the survey, with none citing them as their primary pension provision – not surprisingly, given that they are a recent addition to the pensions market.

In Aon Hewitt's recent DC survey, also carried out in the summer of 2015, 16% of respondents state that they expect to offer a master trust within the next five years. If, as that survey suggests, master trusts become 16% of the DC market in five years' time, that might amount to assets of perhaps £70bn. Master trusts offer a viable alternative to the traditional DC scheme choices, and are an option that increasing numbers of scheme sponsors will consider as they become more established.

While the majority of respondents believe pensions will continue to make a significant contribution to the overall benefits package in future, a significant minority disagree, expecting the importance of pensions to wane.

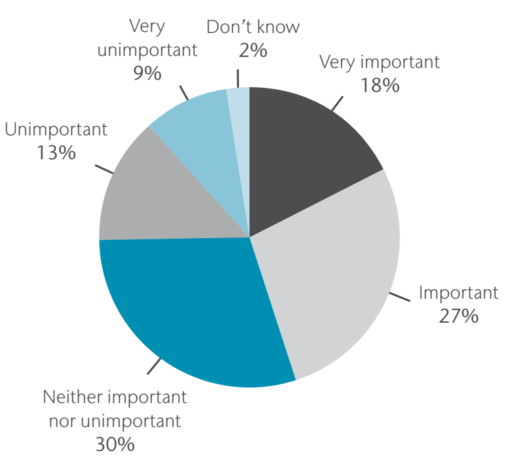
A lack of conviction regarding the pensions system is a clear theme among the reasons given for this, with a decrease in public confidence and/or engagement with pensions (the two being closely linked), and a perception that other investments offer better value, being given by a large number of those who think pensions will reduce in relevance.

Approaches to pensions administration

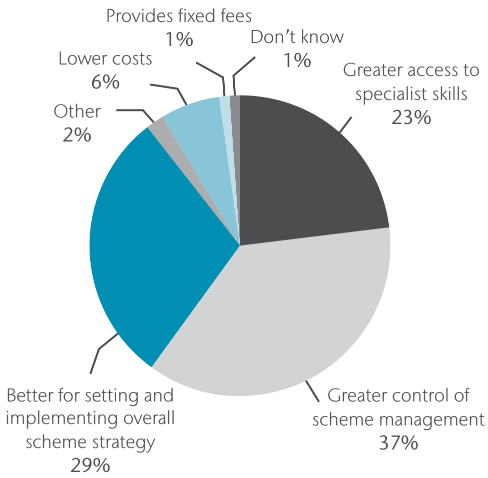
45% of survey participants think it is important or very important that their pensions administration provider can offer administration as part of a broader, integrated offering. This might potentially include consulting or actuarial advice, or investment strategy advice/implementation alongside scheme administration.

These are very similar to the findings from the 2014 survey, when ‘greater control of scheme management’ (60%), ‘greater access to specialist skills’ (54%), and the fact that it is ‘better for setting and implementing overall scheme strategy’ (41%) were cited as the reasons an integrated service was important.

When choosing a pensions administration provider, how important is it to you that a provider can offer administration as part of a broader, integrated offering?



Why is the ability to provide a broader, integrated pensions offering important/very important?



When asked why this was important, control and access to appropriate expertise are the key reasons. 37% feel that receiving a variety of services from one provider would deliver greater control over scheme management. 29% believe an integrated approach would be better in terms of setting and implementing the overall scheme strategy, while 23% cite greater access to specialist skills as a benefit.

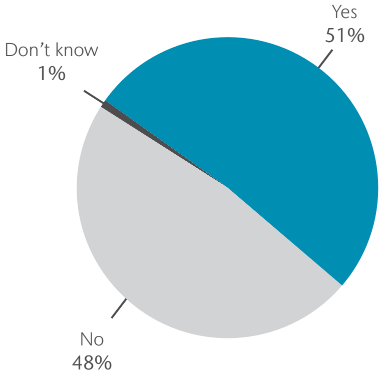
Cost and fee issues are less likely to be identified as benefits of a single, integrated provider, with 6% seeing lower costs as important and just 1% citing the ability to provide fixed fees as a benefit.

Outsourcing vs in-house administration

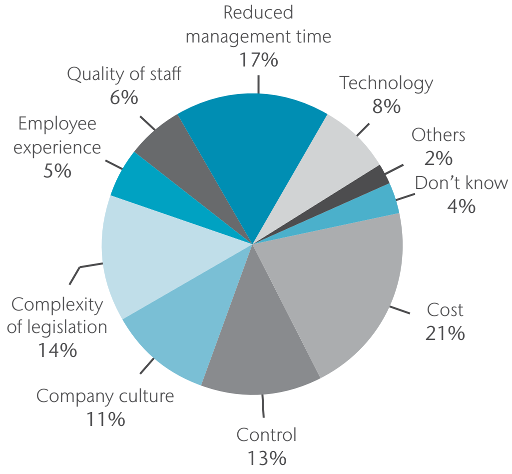
70% of those surveyed currently outsource their pensions administration.

Of those schemes that outsource administration, 51% receive administration services as part of a broader offering, while 48% do not.

Do you currently receive outsourced administration services as part of a broader, integrated pensions offering from a single provider?



What factors led to your organisation's decision to outsource its pensions administration?

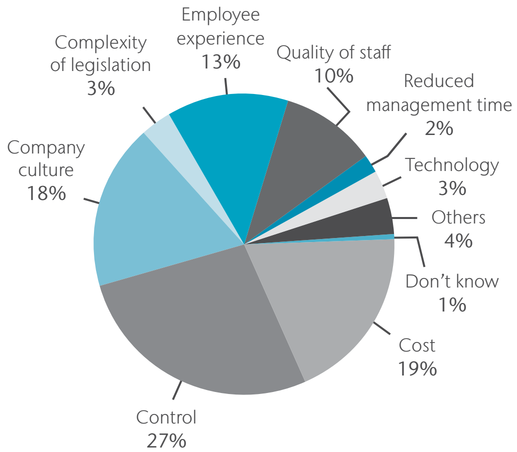


Why do schemes outsource administration?

When asked why they had outsourced their scheme administration, respondents gave a wide variety of reasons. Cost was a driver for 21% of respondents, with reduced management time being cited by 17%. The desire to harness specialist external expertise is implicit in the reasons cited by many, with the complexity of legislation a deciding factor for 14% and the quality of staff for a further 6%. The ability to gain greater control over administration (13%) and the company culture (11%) were also named as drivers.

Respondents who had decided to retain their administration in-house were also asked the reasons behind their decision. Here, control was the biggest factor, with 27% citing this as a reason to continue with in-house administration.

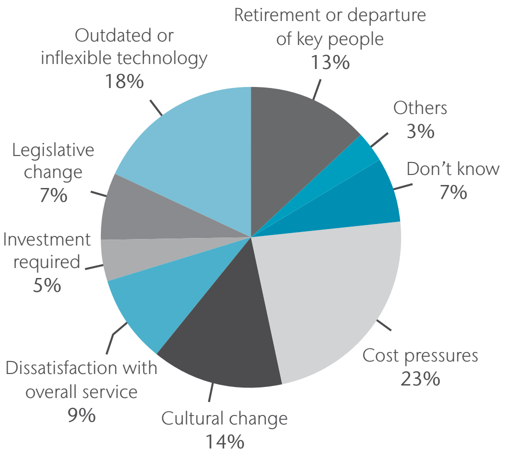
What factors led to your organisation's decision to retain its pensions administration in-house?



Changing administration strategy: what are the drivers?

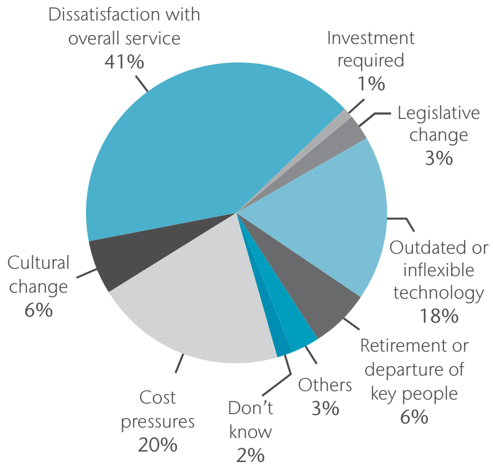
Those with in-house administration were asked what would prompt them to outsource. Cost pressures are the reason given by most (23%), with outdated or inflexible technology the second most-cited reason (18%). People and business continuity issues are also reasons for the decision to outsource, with cultural change cited by 14% of participants and the retirement or departure of key people a reason for 13%.

What might prompt you to outsource your pensions administration?



Of those respondents who outsource their administration, 41% would change provider if they were dissatisfied with their overall service. 20% would change as a result of cost pressures, with outdated or inflexible technology an impetus for change for 18%. The retirement or departure of key people would prompt 6% to look at changing provider, with the same amount citing cultural change.

What might prompt you to change outsourcing provider?



Aon Hewitt perspective

While almost half of survey participants believe it is important or very important that administration providers can deliver scheme administration alongside a broader portfolio of services, 48% currently do not receive this.

The legislative burden continues to grow, and in 2016 we will see even more legislation coming into force. This will impact administrators, whether administration is done in-house or via external specialists. It is therefore unsurprising that the complexity of legislation is cited as a reason for entrusting administration to external experts.

Interestingly, cost is seen as one of the largest drivers both for outsourcing and for retaining administration in-house. It is useful to look at some of the costs that are incurred when outsourcing, against some of those experienced when keeping administration in-house.

The explicit cost of the administration contract is the most obvious one incurred when administration is outsourced. However, looking at the benefits or drivers cited by those who currently outsource, a lot of these deliver savings that may in part offset the out-the-door cost of the administration contract.

For example, 'reduced management time' could deliver significant savings, removing the need for senior business leaders to involve themselves in-depth in pensions administration issues. By outsourcing administration, the role of the business becomes one of setting strategy and overseeing performance in line with company goals, rather than the day-to-day, hands-on management of the scheme's administration.

Similarly, the complexity of legislation has cost implications in terms of the time it takes for in-house teams to familiarise themselves with new requirements, assess the impact and then make the changes needed to respond to them. Most legislative change impacts systems, processes, communications and training. External administrators will be doing the same across their client base, and are therefore able to identify and implement best practice approaches more cost-effectively; again; the only management time needed internally will be that used to define objectives and oversee progress.

In-house administration comes with its own costs too, and it is possible for companies to significantly reduce business overheads by outsourcing its administration, not only against the cost of salaries, property and equipment, but also against IT development and maintenance, legislative compliance and the use of support services.

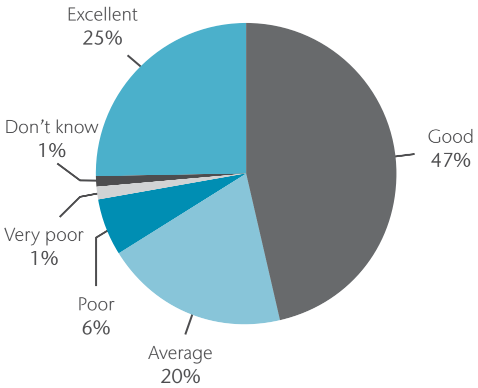
There are also some interesting points to be made by comparing the reasons respondents chose to keep their administration in-house with the factors that might prompt them to outsource. While cost is the second-biggest reason for retaining administration in-house, 'cost pressures' are also the main reason given for a potential move away from internal administration. And while 'company culture' is one of the main reasons for continuing with in-house administration, 'cultural change' is one of the key reasons given for a potential move to outsourcing.

It seems clear that schemes are somewhat confused when it comes to the benefits (or challenges) of outsourcing administration, particularly in relation to cost. It is important that anyone considering their approach to scheme administration looks at the whole picture rather than just the obvious out-the-door cost. In practice, the decision to outsource or retain administration in-house is a complex one, and rarely comes down to one single factor.

Pensions administration standards

25% of respondents would rate the overall standard of their pensions administration service as excellent. A further 47% see it as good, with 20% believing their service is average and 6% poor.

How would you rate the overall standard of your pensions administration service?



Respondents were asked whether their pensions administration has improved, deteriorated or stayed the same over the past twelve months. The overwhelming majority (57%) believe that it has stayed the same, with 23% stating that it has improved. 17% think that service standards have deteriorated. These figures remain almost unchanged over the last three Pensions Administration Surveys we have conducted.

The connection between price and service quality

43% of respondents to the survey agree that there is a correlation between price and quality of service, with a further 3% strongly agreeing. 37% are unsure and only 10% disagree.

When asked whether they would be prepared to pay more to receive a higher-quality service, though, 35% would not. 40% said they would be, with 25% undecided.

Aon Hewitt perspective

Although a large number of survey participants believe there is a link between price and quality when it comes to outsourced administration, almost as many are unwilling to pay more to receive a higher-quality service: their beliefs are out of kilter with their practices.

We believe this is a fundamental flaw in the current administration model. In recent years, some providers have been accused of trying to undercut each other on price in order to win business at all costs, creating a 'race to the bottom'. In some cases, this has led to it being impossible to deliver contracts in a cost-effective way. The result? Schemes either do not get everything they have been promised, or providers are left managing unprofitable contracts as they attempt to deliver on promises made without proper reference to the costs of delivery.

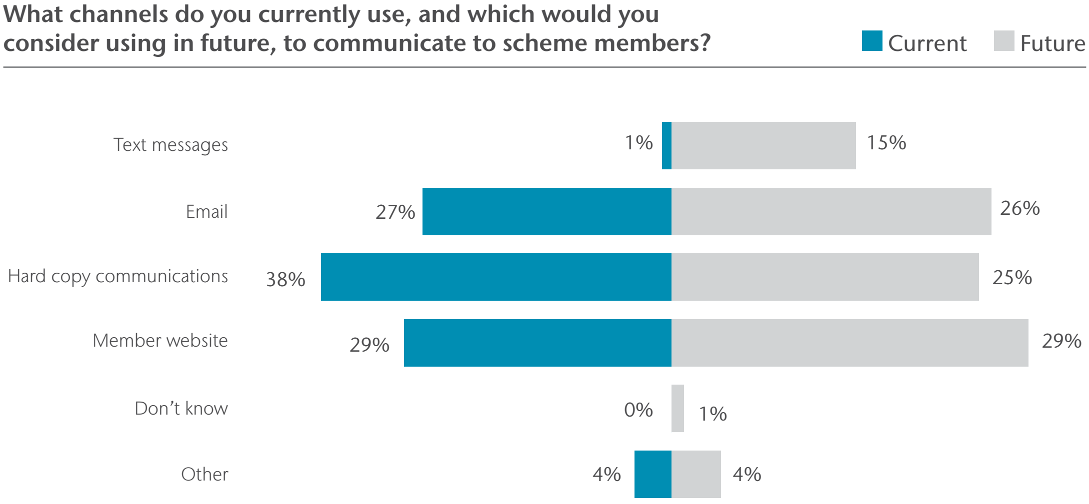
This is a lose-lose situation, and is unsustainable. That is why, at Aon Hewitt, we have been taking a different approach to pensions administration. Both schemes and providers need to be realistic about what can be offered, and what the resulting cost will be. By doing this, schemes can have clear expectations around their administration service, and third-party administrators can offer solutions that are deliverable and sustainable at a fair price.

Pension communications

Hard copy communications are still the most popular method of communicating with scheme members, with 38% currently contacting members in paper form. 29% use a specific website to communicate with members, while 27% use email.

When asked about potential future methods of communication, little change is anticipated, although paper-based communications are expected to decrease in use. 25% expect to use hard copy communications in future, 29% a member website and 26% email. Text messaging, currently only used by 1%, shows the biggest projected increase, with 15% expecting to make use of texts in future.

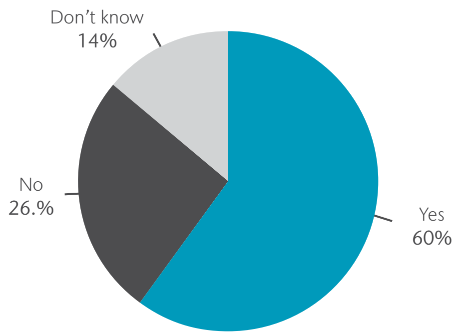
What channels do you currently use, and which would you consider using in future, to communicate to scheme members?



Responding to the new pensions freedoms

The recent pensions freedoms mean that different members have different options at retirement. 60% of those responding to the survey believe that the pensions freedoms will fundamentally change the decisions members make about their pensions.

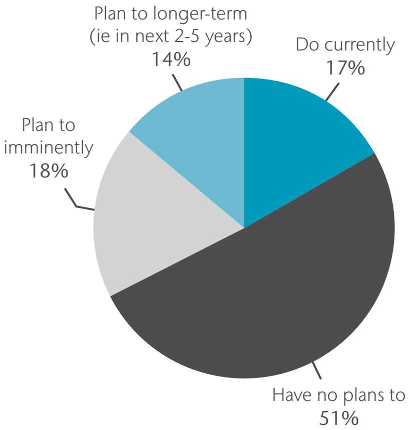
Are you expecting the new pensions freedoms to fundamentally change the decisions members make about their pensions?



With this in mind, respondents were asked whether they currently, or whether they plan to, segment their member communications, communicating different messages to different groups.

51% do not currently segment communications, and have no plans to do so. 17% currently deliver segmented communications to members, with a further 18% planning to implement a more targeted approach imminently. 14% plan to do this in the next two to five years.

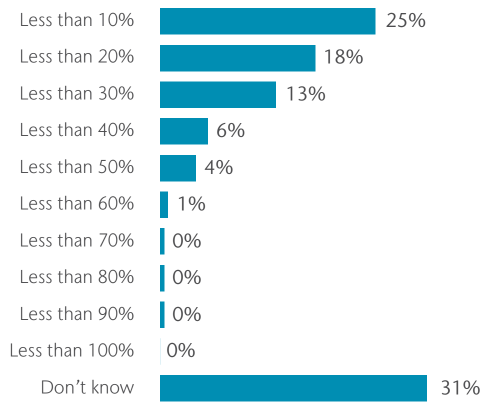
Do you currently, or plan to imminently, segment your member communications?



Segmenting by age or stage of career will be vital to delivering this targeted communication. In light of this, respondents were asked what percentage of their active membership would be 55 next year.

31% are not able to state the percentage of 55 year olds their scheme will have. 25% state that it will be under 10%; for 18%, fewer than 20% of members will be 55 next year. 13% expect that less than 30% of their members will be 55.

Approximately what percentage of your active membership will be 55 next year?



Aon Hewitt perspective

No huge changes are anticipated in member communications in future, although schemes are clearly alive to the potential of using new approaches to engage members, as seen by the 15% that anticipate using text messaging in future. Our own experience with clients has increasingly seen schemes taking a 'soft' approach to introducing electronic communications, allowing members to opt out of paper communications and payslips rather than imposing the change of delivery media on them, and enabling them to opt back in should they wish.

With the new pensions freedoms comes the need to communicate more clearly than ever with members approaching retirement. Segmented communications, targeted not just by demographics but by members' preferences, risk profiles and past behaviours, will help schemes to ensure their messages are heard and understood. This in turn will help to deliver the better member outcomes that schemes are striving for.

Media such as email, texts and personalised websites are ideal for segmented communications, although printed materials can also fulfil this role, given the ease with which print can now be personalised.

Taking into account the need for customised communications, and the ease and cost-effectiveness of delivering them, it is concerning that over half of schemes do not segment member communications and have no plans to do so. We would strongly advise any scheme sponsors or trustees not looking at this to explore the area of segmented member communications as a matter of urgency. Better member outcomes are a clear objective of the Pensions Regulator, and will only be achieved if members are aware of the choices they need to make and the options open to them. In turn, this will only happen if members are communicated with in a way that makes their choices clear and the potential implications of their actions easily-understood.

With pensions freedoms having been introduced in April 2015, schemes need to be aware of the implications in terms of the actions they need to take. Member communications will need to be targeted to enable those approaching retirement age to make the best decisions for their circumstances.

It is therefore also slightly alarming that nearly a third of survey respondents do not know how many members will be 55 in the next year. Schemes will want to get to grips with this sort of data, as this will enable them to segment their communications to members, ensuring they resonate with each member's aspirations and priorities and deliver appropriate messages at each stage of their membership.

Experience has shown that using segmentation techniques such as those used in consumer marketing – and taking a more sophisticated approach than segmenting just by age – can be very successful in getting members to engage.

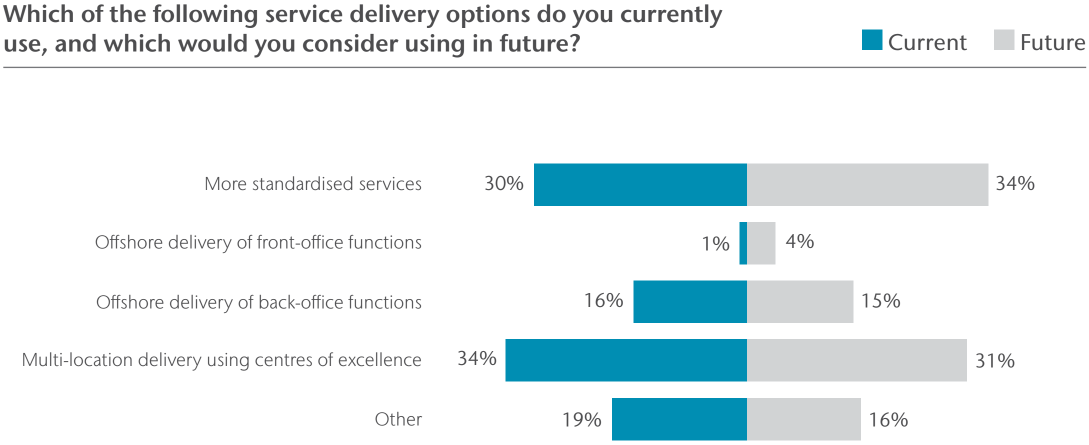
The survey findings indicate that, for over a third of schemes, and probably many more, demographic modelling of members – and the subsequent communications that speak to each group of members – are not currently possible. Schemes need to get a firm grip on the composition of their membership, as this will be key to getting the member engagement outcomes they are looking for.

Service delivery

The survey also looked at service delivery options; those used currently and those schemes expect to utilise in future.

34% report that they currently take a 'centre of excellence' approach to administration, with delivery managed from multiple locations; 31% expect to take this approach in future. A move away from bespoking and towards a more standardised approach is also evident: 30% report that they use 'more standardised services' to deliver pensions administration services to members, and 34% expect to do so in future. 16% currently offshore back-office functions, with 25% planning to go down this route. Offshore delivery for front-office (ie member-facing) functions is less popular, with just 1% doing this now and 4% planning to in future.

Which of the following service delivery options do you currently use, and which would you consider using in future?



Aon Hewitt perspective

No revolutions in service delivery are planned. While a significant minority of schemes are currently happy to offshore back-office functions, and more plan to do so in future, front-office capabilities are set to be retained onshore for the immediate future.

This is closely related to the issues around cost and service quality raised previously. If schemes want to get a reliable service for a low price, alternative delivery models could be the solution for some, as these are often designed with that objective in mind. Rather than choosing bespoke options, accepting standardised service delivery and being open to the advantages of offshoring and the use of service centres (call centres) can enable schemes to benefit from economies of scale – achieving a high quality service at a cost they find acceptable.

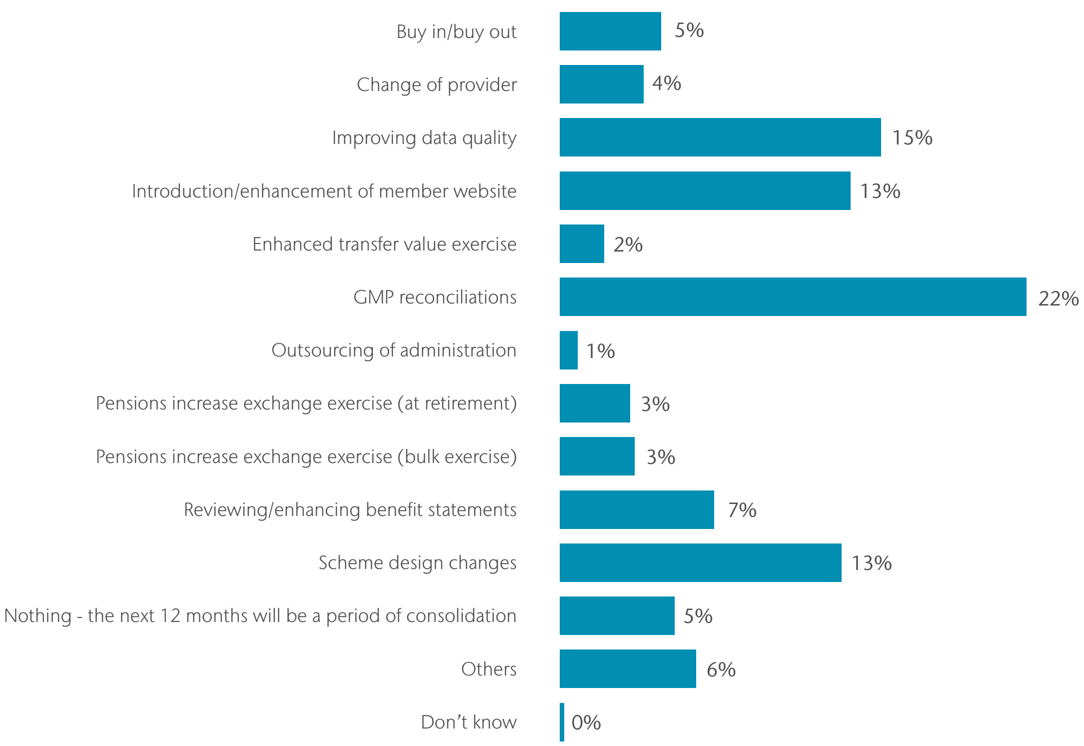
Aon Hewitt's delivery model is very much designed to maximise efficiency while maintaining the desired levels of quality and control. By utilising centres of excellence, both onshore and offshore, we continue to drive consistency and quality and provide value by utilising standardisation wherever possible. We also provide member self-serve options, with functionality that is deployed to meet the needs of the particular membership.

Pensions priorities

The survey explored current pension priorities, asking respondents about their priority projects for the next twelve months. GMP reconciliations are – by a significant margin – the issue most exercising schemes' and trustees' minds: 22% cite this as their priority project. This is a higher priority for large schemes (those with more than £1,000m in assets) than for smaller ones. Improving data quality is a priority for 15%, with the introduction or enhancement of a member website and scheme design changes both planned by 13%.

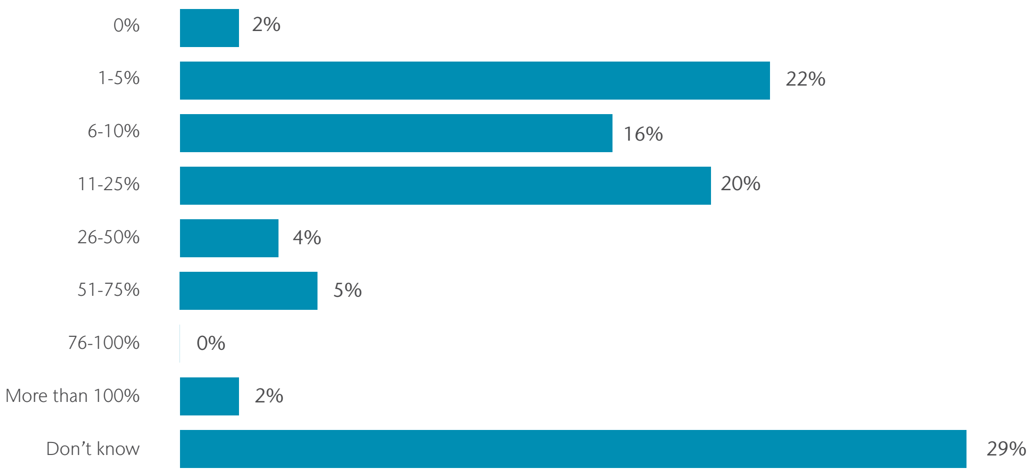
In 2014, too, the largest percentage saw GMP reconciliations as their chief priority (29%). Twelve months ago, there was more of a focus on communication than is evident in the 2015 survey, with 20% citing 'reviewing/enhancing benefit statements' as their focus. This year, just 7% plan to review or enhance benefit statements.

What are your priority pensions projects for the next 12 months?



Schemes may struggle, though, to reconcile their ambitions with their budgets. 22% plan to spend between just 1% and 5% of their budget on their priority projects over the next twelve months, with a further 16% planning to dedicate 6-10% of their usual spend to them. Only 11% are planning to spend more than 25% of their anticipated budget on their priority projects. 67% of schemes with over £1,000m in assets plan to spend none of their administration budget on their priority projects. 29% do not know what they aim to spend on these key areas of concern.

Approximately what percentage of your regular annual administration spend are you planning to devote over the next 12 months to your priority projects?



Participants were also asked to do a bit of daydreaming, and say how they would spend an unlimited budget for pensions administration, if they were given one. The answers were open, giving respondents the opportunity to provide their own suggestions as to how they would spend this money. Communications were by far the biggest priority for this imaginary spend, with the vast majority of answers referencing communications, member education or projects to increase member and employee engagement. Other – though far less popular – options related to improving administration technology and increasing administration quality or service levels.

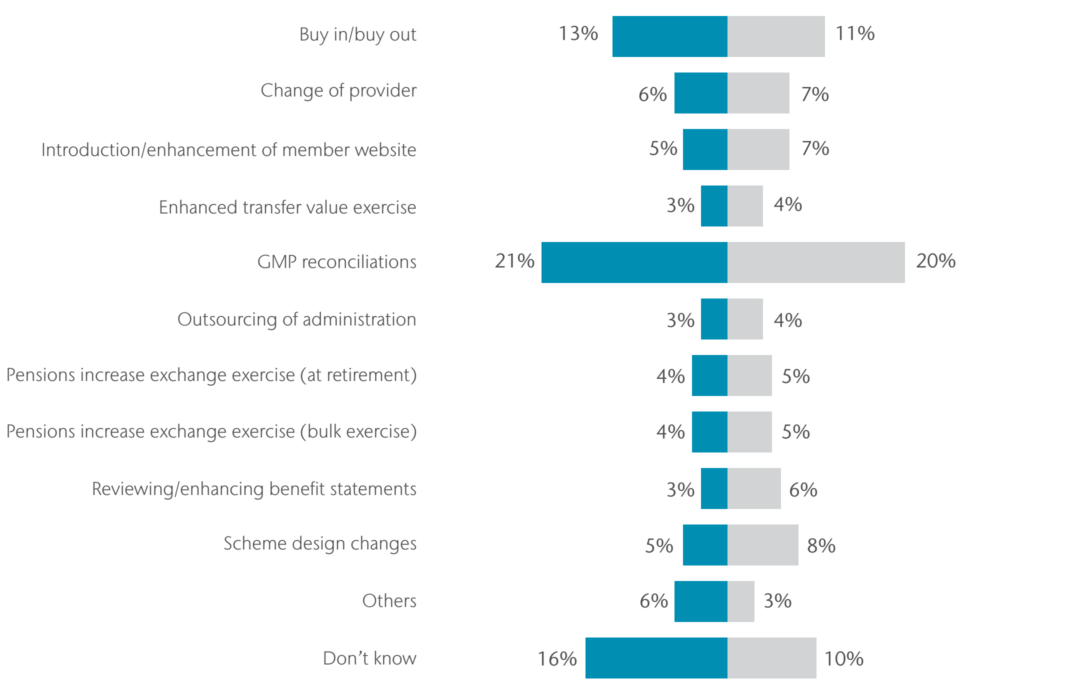
Data quality

The quality of a scheme's data can have a profound impact on its ability to run efficiently and cost-effectively. With this in mind, the survey asked whether respondents anticipated that the quality of their scheme data would either hinder their ability to deliver their priority projects, or increase the cost of delivering them.

GMP reconciliation – the project schemes see as their highest priority for 2016 – is also the most likely to be negatively impacted by poor data. 21% believe data quality will impact their ability to deliver the project, with 20% expecting that it will increase the project cost. 13% expect poor data to hinder their ability to deliver buy in or buy out projects, with 11% expecting it to increase costs. Larger schemes (those with more than £1,000m in assets) are far more likely than smaller ones to believe that quality of their scheme data will hinder or increase the cost of their priority projects.

In spite of the recognition that data will impede planned projects, however, only one person answering the free-text question above around mythical administration budget said that they would spend it on a data clean up.

Do you think that the quality of your data will either hinder your ability to deliver these projects or increase the cost of delivering them?



Aon Hewitt perspective

Pension priorities are largely unchanged since the previous survey in 2014, with GMP reconciliations unsurprisingly still a major focus. For DB scheme trustees, GMP reconciliation remains a hot topic. HMRC is due to begin winding up its reconciliation service from April 2016; by April 2018, support for schemes will be very limited. We would urge any scheme that has not yet started work on a GMP reconciliation project to talk to their administrator about this.

For many, the final stage of a GMP project will be the discovery of members who need a correction due to an incorrect GMP figure. For most pensioners, this requires a recalculation of benefits, often resulting in a reduction in overall pension – in other words, the scheme frequently has a positive outcome in terms of cost from doing the GMP exercise. A GMP project can also deliver other positive side effects, including more accurate actuarial valuations, reduced data risk premium loading if considering a buyout, and GMP data being ready for the inevitable GMP equalisation requirement. We therefore believe that the costs of GMP exercises are outweighed by the benefits they deliver.

However, schemes need to dedicate appropriate resource to the project in the first place in order to achieve these benefits. The first step in such a project is often a data exercise to ensure that scheme data is up to date and accurate. As the survey shows, many schemes anticipate this not to be the case, with data quality expected to hinder and/or increase costs across all the projects schemes hope to undertake.

A data cleansing exercise is therefore a cost-effective and very necessary action for almost all schemes. We would recommend that any scheme that hasn't undertaken a data cleanse in the last 12 months should do so. This will ensure that member data forms a solid and accurate foundation for the projects that follow, many of which depend on this accuracy for their success.

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