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Sixty second summary

Fiduciary management in the spotlight

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Use of fiduciary management has grown substantially over the last decade, sometimes for the right reasons and sometimes for the wrong ones. We believe it is important that all trustees understand the principles of fiduciary management so they are able to make an informed choice on whether it is right (or wrong) for them.

What is fiduciary management?

Fiduciary management is an arrangement whereby trustees delegate certain investment decision-making powers to a third party. While the full fiduciary model would delegate all but the most important investment decisions, in practice there is a wide variety of different models and the level of delegation can be tailored to a particular trustee's requirements. The following table compares the decisions which trustees delegate under a traditional advisory model against the full fiduciary (and an example partial fiduciary) model.

INCREASING DELEGATION

DECREASING IMPORTANCE

The various levels of delegation Which decisions do trustees delegate?	Advisory	Example Partial Fiduciary	Full Fiduciary
Objective setting e.g. Achieve full funding by 2030 on gilts +0%	✗	✗	✗
Strategy setting e.g. We need our assets split between 30% growth, 30% income and 40% protection	✗	✗	✓
Structure: choosing the best asset classes e.g. To generate income we'll use investment grade credit	✗	✗	✓
Dynamic asset tilts e.g. 30% income is our long-term target but given the current market, 35% is better	✗	✓	✓
Manager selection e.g. We'll choose Schroders over BlackRock to manage investment grade credit	✗	✓	✓
Stock selection e.g. We won't hold Apple stock because we think it's overvalued	✓	✓	✓

Pros and cons

Proponents of fiduciary management argue that a key benefit of delegation to an expert third party is increased speed and ease of implementation of investment changes. For example, a scheme's asset allocation can be quickly de-risked when a pre-agreed trigger is hit, because the intermediate step of a trustee discussion is removed. Changes can also be made without the need for trustees to sign instruction forms which reduces the administrative burden on the trustees and the scheme secretaries/pension managers who support them. On the other hand, these benefits can come with drawbacks: loss of operational control can sometimes mean that the pace of change is too fast and trustees find a new asset class or manager is introduced to the portfolio with little or no discussion beforehand. The benefit of less administration might be counteracted by less flexibility in the choice of investment solutions if the fund choice is limited to fiduciary products offered by the manager.

Benefits of delegation	**Drawbacks of delegation**
Clear responsibilities (from the delegated mandate design)	Trustees delegate authority but not accountability
Quicker decisions and implementation	Loss of operational control
Single manager relationship	Concentration of risks with single manager and potential conflicts of interest
Greater diversification and wider opportunity set for small schemes	Excessive diversification or complexity can create unnecessary costs and make exit more difficult
Standardised, yet sophisticated, solutions for small schemes	Performance less transparent (oversight alleviates this)
Fiduciary manager can access lower underlying fund fees	Additional layer of fees

In general, most benefits have corresponding drawbacks to consider. We've outlined some of the most important points in the table above. Lastly, trustees should consider their journey to de-risking: as schemes mature and move to 'steady-state' portfolios, the need for dynamism and diversification across asset classes tends to diminish, making fiduciary management less relevant.

Fees and costs

Fees and costs are a key consideration whatever the arrangements. While in the past fees for fiduciary arrangements may have seemed high relative to the traditional advisory alternative, the Competition and Market Authority's decision to require competitive tendering for fiduciary mandates has led to a surge in tender activity and a fall in the cost of fiduciary arrangements, making cost comparisons much more finely balanced.

Conclusion

As noted above, we believe it is important that all trustees understand the principles of fiduciary management so they are able to make an informed choice on whether it is right (or wrong) for them. This should be considered in the wider context of all governance solutions currently available, including master trusts, insurance solutions, commercial consolidators and others.

A periodic review of governance solutions should be on all trustees' agendas. If you'd like to know more about the pros and cons of fiduciary management specifically or other governance solutions more generally then please talk to your consultant.

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