

Trustee Knowledge and Understanding (TKU)

Revised guidance on the
scope of the TKU requirements

Scope guidance

**Defined benefit schemes with associated
defined contribution arrangements**

2009

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Unit 1:

The law relating to trusts

This includes an understanding of the special nature of a pension trust and the duties, obligations and powers of trustees to operate pension schemes in accordance with the law and the trust documentation.

1a The definition and nature of a pension trust

Including the separation between the scheme and the sponsoring employer and the separation of assets

1b Fiduciary duties

Including the obligation to act prudently, safeguarding the financial interests of all beneficiaries, eg:

- in the choice of investment vehicles (DC)
- in any decision involving the possibility of changing to a different pension arrangement, eg buying out or winding up the current scheme

1c Professional advice and decision-making

Including the need to obtain professional advice (where appropriate) in reaching decisions.

1d The role of advisers and suppliers to the scheme

Including the employment by the trustees of:

- actuaries
- administrators
- auditors
- benefit consultants
- custodians
- financial advisers
- fund managers
- investment consultants
- investment managers
- lawyers
- providers (as appropriate)

1e The particular role and use of advisers in special situations (DB only)

Including:

- actual or proposed corporate restructuring which threatens technical provisions
- any threat to the scheme or to the employer covenant

1f Investment of scheme assets

Including the trustees' responsibility to act prudently and in accordance with the trust documentation, and taking into account the strength of the employer covenant

1g The operation of the scheme in accordance with the trust documentation

Including:

- the trust deed and rules
- any amendments
- the Memorandum and Articles of Association or equivalent documents (corporate trustees)

1h Trustees' powers

Including:

- the power to:
 - *amend the rules*
 - *delegate functions while retaining responsibility*
 - *authorise signatories for payments*
 - *augment benefits (DB only)*
 - *set contributions (DB only)*
 - *exercise certain discretions (eg distribution of death benefits)*
 - *invest scheme assets*
 - *wind up the scheme*
- the limitations and conditions imposed by the trust deed and rules and relevant legislation;
- the effect of legislation

1i The balance of powers between the sponsoring employer and trustees

Including the requirement to consult

1j Conflicts of interest

Including situations which may give rise to conflicts and how conflicts may be managed, eg:

- trustees whose relationship with the sponsoring employer might make it difficult to maintain the interests of all categories of beneficiaries as the prime concern
- trustees required to use their discretion in relation to members whom they may know well
- professional advisers who may be retained by both trustees and the sponsoring employer
- investment advisers running a fund management service

1k Taking office

Including the particular requirements and the implications of joint and several liability

1l Fitness and propriety to act as a trustee

Including the need for:

- an appreciation of the full range of trustee duties
- appropriate knowledge and understanding
- preparation for and regular attendance at meetings
- knowledge of the circumstances in which a person is disqualified from taking office

1m Ceasing to hold office

Including the implications of personal liability for past decisions

1n Protections and immunities offered to trustees

1o Trustees' responsibility for sound governance and administration

Including:

- secretariat functions, eg planning, minutes of meetings, correspondence, complaints
- administration functions, eg record-keeping, payment of benefits, receipt of
- contributions, checks for fraud
- risk management, eg internal controls, contingency planning
- decision-making and delegation

Unit 2:

The law relating to pensions

This includes occupational pensions legislation (in outline) and the key provisions of related legislation that affects pension schemes and impacts on the role and activities of pension scheme trustees.

2a Occupational pensions legislation

Including:

- the key provisions of pensions legislation
- the Pensions Regulator's Codes of Practice and guidance
- Pension Protection Fund (PPF) guidance (DB only)
- the outline of proposals for major legislative change already approved by the Government

2b The tax privileges and requirements for occupational pension schemes

Including the relevant provisions of the Finance Act 2004, eg those which:

- set the conditions to be met by a Registered Pension Scheme
- allow personal pensions and occupational pensions to be run concurrently
- set a cap on contributions (DC only) and benefits which attract tax privileges

2c Pensions related legislation

Including:

- anti-discrimination
- arrangements for giving advice on pensions
- civil partnerships
- compensation arrangements
- data protection
- employment legislation
- money laundering
- parental leave
- pensions sharing on divorce

2d The particular powers of the regulator in relation to sponsoring employers as well as trustees (DB only)

Including the powers to issue contribution notices and financial support directions, and to offer protection from these by clearing corporate restructuring proposals

2e Disputes resolution

Including:

- Internal Disputes Resolution Procedure (IDRP)
- the role of The Pensions Advisory Service (TPAS) and the Pensions Ombudsman

2f Member nominated trustees/directors

2g The law relating to internal controls and sound administration

Including the obligation to administer the scheme in accordance with legal and regulatory requirements

2h The interface between occupational schemes and state pension provision

Including the implications of contracting out and the relationship between pension scheme benefits and means-tested state benefits

2i The obligation on employers to offer a qualifying scheme for all employees from 2012

Including the conditions for meeting the requirements for a qualifying scheme, covering such matters as:

- automatic enrolment of members
- minimum contribution rates
- eligibility for membership
- the definition of pensionable pay
- the power of trustees to modify their scheme rules by resolution to meet the requirements for a qualifying scheme

Unit 3:

The basic principles relating to the investment of assets

This includes the major asset classes and their risk profiles as well as information about other asset classes and the principles of risk and reward.

3a Capital markets

Including, in broad terms, the effect of economic cycles

3b The major asset classes and their characteristics

- equities
- bonds
- property
- cash

3c The implications of overseas investment

Including foreign exchange risk and political risk

3d The existence of other asset classes and investment techniques

Including:

- annuities used as an asset class
- default funds and lifestyling arrangements (DC)
- with-profits arrangements (as appropriate)

3e The balance between risk and reward

Including:

- the nature of risk
- risk/reward profile of each major asset class
- basic principles of matching assets to liabilities (DB)
- basic principles of matching assets to pension expectations (DC)
- basic principles of managing risk by diversification of asset classes

Unit 4:

Funding: Defined Benefit (DB) occupational arrangements only

This includes the principles relating to the funding of DB occupational arrangements and the way in which the funding level is dependent upon the value of both the scheme's liabilities and its assets.

4a How the funding for DB occupational pension schemes works

Including different funding bases and the purpose of each

4b How liabilities are valued for different purposes

Including:

- the significance of future cash flows
- the importance of assumptions and their impact
- the volatility of the value of liabilities

4c How the market value of assets is assessed

4d Funding measures

Including:

- the measurement of liabilities (eg technical provisions, buy-out, PPF)
- the setting of contributions (eg recovery plan in the event of deficit)

4e Potential risks to the ability of the scheme to pay benefits

Including:

- the financial instability of the sponsoring employer
- corporate restructuring
- transferring liabilities to a new employer
- unusually high salary increases
- any proposal from the sponsoring employer for the buy-out of scheme liabilities
- the volatility of assets relative to liabilities

4f The importance of complete, accurate and up-to-date data and calculations

Including the need for robust processes and systems

4g The impact of trustee powers

Including the financial impact of exercising discretions (eg augmentation of benefits)

4h The nature and status of professional advice

4i Transfers and bulk transfers in and out of schemes

Including:

- the responsibility of trustees to decide upon the calculation of transfer values
- buy-ins
- buy-outs
- any inducements from the sponsoring employer for members to forego future benefits

Unit 5:

Contributions: Defined Benefit (DB) occupational arrangements only

This includes the principles relating to the setting of contributions.

- 5a The nature of the employer/trustee relationship and the effect of the scheme's funding level on the sponsoring employer**
- 5b The way in which the sponsoring employer covenant reflects its ability to fund the scheme**
Including an understanding of the sponsoring employer's business, its audited accounts and auditor's report and its exposure to risk
- 5c The calculation of regular contributions to fund liabilities for future accruals**
- 5d The setting of special contributions for past service as required**
Including agreement on a recovery plan
- 5e Member contributions**
Including:
 - regular and additional contributions (eg AVCs and salary sacrifice)
 - other concurrent member pension arrangements (eg FSAVCs, personal pensions and stakeholder pensions)
 - the timeliness of payments to the scheme
 - the importance of complete, accurate and up-to-date member records
 - the importance of robust systems and processes
- 5f The role of the sponsoring employer in the calculation and collection of member contributions**

Unit 6:

Strategic asset allocation: Defined Benefit (DB) occupational arrangements only

This includes the principles relating to the suitability of different asset classes to meet the liabilities of the scheme, taking account of the strength of the employer covenant and the trustees' risk profile for the scheme.

6a The process of strategic asset allocation

Including the importance of selecting an appropriate mix of asset classes and taking account of the correlation between them and the trustees' investment objectives

6b The characteristics of alternative asset classes and financial instruments

6c The use of specialised investment techniques

Including liability driven investment arrangements

6d Reviewing asset allocation decisions

Including regular review and the response to any change in the maturity or status of the scheme

Unit 7:

Running a Defined Contribution (DC) occupational arrangement (including AVCs)

This includes the principles relating to the operation of DC occupational arrangements and the risks borne by scheme members.

7a How DC occupational pension arrangements work

Including the payment of fees, charges and expenses, and the operation of a trustee bank account

7b Administration procedures specific to DC occupational arrangements

Including the importance of:

- complete, accurate and up-to-date member records
- the timely collection of contributions and allocation of assets
- regular reconciliations
- the accurate and timely switching of assets when required (eg lifestyling)
- robust systems and processes

7c The role of the employer in the calculation and collection of member contributions

7d The implications of the transfer of risk to members of DC occupational arrangements

Including:

- market risk
- mortality risk
- changes to the legislation or tax regime
- contributions not being paid across to the scheme accurately and on time
- excessive charges and up front charging structures
- ineffective communications between members and trustees
- lack of member understanding of pension funding in general
- insufficient contribution levels
- inappropriate investment choices by members
- inappropriate or uninformed decision-making at retirement

7e The implications of contracting out

Unit 8:

Investment choice and the implications for members: Defined Contribution (DC) occupational arrangements (including AVCs)

This includes the principles relating to the choice of investments to be offered to members.

8a The implications for members of the investment strategy adopted by trustees

Including:

- whether or not trustees offer investment choices to members
- the range of investment choices where they are offered
- the suitability of the investments for the membership
- the implications of a default investment fund
- the implications of lifestyling as a default option

8b The importance of member understanding of investment risk

Unit 9:

Fund management

This includes the principles of fund management and how the performance of fund managers can be measured.

9a The structure of investment portfolios

Including such matters as:

- active v passive management
- pooled funds v segregated portfolios
- rebalancing portfolios
- investment style

9b The selection of fund managers

9c Investment mandates

Including an understanding of the nature of the contract between the trustees and their asset managers, and the fee structures and charges

9d Measurement of performance using indices, benchmarks and targets

9e The mechanisms for monitoring investment arrangements and fund managers

Including:

- reports from fund managers
- implications of changes within the fund manager's organisation
- compliance with the statement of investment principles (SIP)
- the completeness and accuracy of records
- the completeness and accuracy of calculations (DC)
- the calculation and the impact of charges and fees
- management of any transition of assets between one manager and another
- robust processes and systems

9f The importance of sound custody arrangements

Including adequate monitoring and correct record-keeping

9g The importance of responsible ownership of assets

Including:

- the extent to which social, environmental and ethical considerations are taken into account when making investment decisions
- the corporate governance of the companies in which the trustees invest
- the extent to which (if at all) they will exercise their voting rights

9h The Myners principles for the governance of the investment decision-making process

Unit 10:

A working knowledge of the scheme's own trust documentation

This includes any subsequent amending documents.

10a The duties, powers and discretions of trustees

10b The balance of powers between the sponsoring employer and trustees

Including, for DB only:

- the appropriateness of exercising trustee powers, especially where the scheme of the sponsoring employer is under threat
- the overriding legislative requirement to consult
- and, for DC only:
- the size of contributions, investment decisions and the calculation of contributions

10c Categories of membership in the scheme

Including eligibility for membership

10d Benefits offered (DB)

Including the circumstances, both current and historic, under which benefits are payable, how they are calculated and the way in which payment is made

10e Decumulation of pension funds (DC)

Including the ways in which funds can be converted into benefits (decumulation), any default arrangements and the way in which payment is made

Unit 11:

A working knowledge of the scheme's Statement of Investment Principles (SIP)

11a Roles and responsibilities for preparing the SIP

11b The scheme's investment objectives and asset allocation strategy

11c The contents of the SIP

Including legal and regulatory requirements covering the contents of the SIP

11d Monitoring and updating the SIP as appropriate

Unit 12:

A working knowledge of the scheme's Statement of Funding Principles (SFP) (DB schemes only)

12a Roles and responsibilities for preparing the SFP

12b The scheme's statutory funding objective

12c Contents of the SFP

12d Monitoring the SFP

Including regular monitoring and special review in the event of a change in the status of the scheme and/or the strength of the employer covenant

Unit 13:

A working knowledge of the scheme's other relevant documents

These include:

- 13a Scheme booklet, announcements and other member communications**
Including the popular report and accounts for members
- 13b Principal contents of the most recent actuarial valuation and subsequent actuarial advice (DB only)**
Including the valuation report and recovery plan (if appropriate), and summary funding statement
- 13c Minutes of meetings**
- 13d Regular stewardship reports**
Including compliance issues
- 13e Schedule of contributions (DB) and any payment schedule (DC)**
- 13f Internal audit reports or reports of alternative internal checks**
Including checks on the adequacy and robustness of systems and on calculations used in individual member communications
- 13g Annual report and accounts for the scheme and for the sponsoring employer**
Including any audited reports
- 13h Any significant contract in respect of scheme assets**
Including contingent assets or guarantees and insurance policies
- 13i Any other significant agreement or contract**
Including those with delegated authorities, professional advisers and suppliers of services, eg contracts of appointment, service level agreements
- 13j Any trustee approved procedures**
Including documentation relating to the:
 - Internal Disputes Resolution Procedure (IDRP)
 - appointment of all classes of trustees
 - appointment of the chair
 - policy to manage conflicts of interest
 - review of the risk register
- 13k Statement of compliance with the Myners principles (where appropriate)**

- 13l Terms of reference of any sub-committee (where relevant)**
- 13m Memorandum and Articles of Association (or equivalent documents) of the corporate trustee (where applicable)**
- 13n The scheme's business plan**
Including a schedule of meetings and a timetable for anticipated agenda items
- 13o Job descriptions for the chair and for the trustees**
- 13p Trustee skills audit, training needs analysis and training log**
- 13q The whereabouts of all original documents and the arrangements for their custody, safekeeping and access**