

Consultation response

# **Authorisation and supervision of master trusts**

Draft code of practice no: 15

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## Introduction

We consulted on the draft **Code of Practice 15: Authorisation and supervision of master trusts** (the code) and the decision making procedure for making authorisation decisions (the procedure) between 27 March and 8 May 2018. This document summarises the feedback we received and changes we have made to the code and procedure as a result.

We received 28 responses from master trusts, representatives, professional bodies and advisers. We are grateful to everyone who responded to our consultation and to those who provided feedback via forums and meetings beforehand.

## The consultation proposal

The Pension Schemes Act 2017 (the Act) and the Occupational Pension Schemes (Master Trusts) Regulations 2018 (the Regulations) ensure that savers are appropriately protected by introducing a new authorisation and supervision regime for master trusts, which account for almost 10 million members in around 80 schemes (as at January 2018).

This new code represents a significant change in the way we regulate, as for the first time we will be directly authorising and supervising master trusts. The new code and related procedure provides master trusts with the clarity they need on how to apply for authorisation and the matters we will take into account in deciding whether they should be authorised and should remain so.

The draft code set out:

- ▶ the process by which master trusts should apply for authorisation
- ▶ the matters we will take into account in deciding whether we are satisfied that a master trust should be authorised at the point of application and throughout supervision
- ▶ the legal requirements that apply once a scheme is authorised, notably in respect of significant and triggering events, and
- ▶ the procedure that will apply in deciding whether or not to grant authorisation.

We asked respondents to complete a three part response form:

- ▶ Part 1 consisted of seven general consultation questions.
- ▶ Part 2 included specific consultation questions on individual sections of the new code:
  - Authorisation criteria: Identifying key roles
  - Authorisation criteria: Fitness and propriety
  - Authorisation criteria: Systems and processes
  - Authorisation criteria: Continuity strategy
  - Authorisation criteria: Scheme funder
  - Authorisation criteria: Financial sustainability
  - Business plan
  - Supervision
  - Application

We also gave respondents the opportunity to make further comments on the consultation if they wished.

- ▶ Part 3 asked questions that were specific to the decision-making procedure.

# Comments received and our response

## Part 1: General questions

### We asked:

- ▶ In your view, are there any barriers to meeting the expectations set out in the new code and if so, what are they?
- ▶ Is the language used in the code clear and unambiguous? If not, what would provide clarity?
- ▶ Do you consider that any important areas of the authorisation criteria have been missed in the new code?
- ▶ Are these the right areas to cover in the first batch of guidance? If not, what additional areas of the authorisation criteria should we consider covering?
- ▶ What other methods should we consider to ensure the information contained in the code is accessible to users?
- ▶ Are there any parts of the code which require additional flexibility because they cover areas which are likely to experience significant change in your business?
- ▶ Is the level of detail we have set out useful? Is further detail needed, and if so, in which areas?

Overall, the majority of respondents felt that the draft code was comprehensive and clear in setting out our expectations in relation to the authorisation criteria. A significant minority provided comments in a number of key areas:

▶ **Timing**

There was a fairly short time period between the publication of the draft code for consultation, supporting guidance and the start of the readiness review period (the period in which master trusts could submit a draft application to us). It was noted by some that draft applications would be prepared and submitted as part of the readiness review before the final content of the code becomes available. There was a general request that changes to the code and feedback from readiness reviews are communicated quickly, in order for master trusts to take them into account before the formal application window opens in October 2018.

▶ **Publication of the authorised list of master trusts**

There was some uncertainty over how and when the list of authorised master trusts will be published.

▶ **Evidence**

Some believed the standard of evidence considered to be 'adequate' in order to satisfy us that the master trust meets the criteria wasn't always clear. This related to both the form of evidence, eg the use of attestation over documentation, as well as the level of detail to include, eg full documents or summary extracts.

▶ **Master trusts with mixed benefits**

Respondents were not always clear on how a master trust with mixed benefits can demonstrate they meet the criteria, particularly in relation to scheme funder and financial sustainability requirements.

▶ **First batch of guidance**

There was a general consensus that the first batch of guidance focused on the right areas (identifying roles, fitness and propriety, systems and processes, and financial sustainability: the basic method). There were, however, calls for further guidance on our supervisory approach, including how to prepare an implementation strategy and guidance on how to follow each of the continuity options.

## **Our response:**

### **Timing**

The new authorisation and supervision regime is expected to commence in full from October 2018, so we have worked to produce and publish content as early as we can ahead of the formal six month application window opening for existing master trusts. We have also provided master trusts with the opportunity to submit a voluntary draft application as part of 'readiness reviews' as a further step to help them prepare for formal authorisation.

With the final code now being laid in Parliament, the final content is available and we will, as part of our feedback, highlight any areas of the code you will need to focus on to help you prepare ahead of submitting your formal application. We aim to give feedback on all draft applications by the end of August 2018, operating on a 'first come, first served' basis.

### **Publication of the authorised list of master trusts**

In relation to publishing the authorised list, we broadly expect to refer applications to the Determinations Panel (an independent decision maker within TPR) in batches in the order they are submitted to us. Our intention is to inform each master trust of an authorisation decision once this has been made by the Panel.

When an authorisation decision has been made by the Panel, we will then look to update the authorised master trust list. We will provide further information on the regularity of hearings held by the Panel, including information on how and when the list will be published and updated before the application window opens in October 2018.

### **Evidence**

We have reviewed how we can be clearer about how master trusts can adequately evidence that they meet the requirements. We have introduced additional text to the application section of the final code to make this clearer. On 25 May 2018, we also updated existing web content to further support master trusts already in the process of submitting draft applications as part of the readiness review.

### **Master trusts with mixed benefits**

For master trusts with mixed benefits, we have, where appropriate, updated the code to highlight additional considerations that apply to schemes offering both DC and DB benefits.

### **First batch of guidance**

In terms of providing further guidance, we intend to publish the broad themes emerging following the readiness review. We also intend to publish our supervision and enforcement policy over the summer for consultation and following this, we will also consider the need for any further guidance.

## Part 2: Section-specific questions

### Fitness and propriety, and identifying key roles

#### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?
- ▶ Does the code provide sufficient clarity on how to identify who carries out the role of strategist and funder within a master trust? If not, what further detail would help?
- ▶ Is there sufficient clarity on the persons to be identified?
- ▶ Does the code provide sufficient clarity on how competence for trustees and strategist will be assessed?

Many respondents did not have significant comments on this section of the code. Those who did said they were satisfied with the content. However, a significant minority raised questions on trustee competence and whether the expectations set out in the code were at the correct level for individual and board level.

Some respondents felt that the expectations for individual trustees should be higher, whereas others felt that an expectation that each trustee has a basic level of knowledge on appointment would deter new trustees. Concerns were also raised that member-nominated trustees could be prevented from acting in a trustee capacity.

A small number of respondents were keen to see that, where a trustee firm was on our list of independent trustees, this would be a proxy for a fit and proper assessment and consideration would also be given to the assurance framework for independent trustees (Assurance reporting on relevant trustees supplement to 02/7<sup>1</sup>).

Some asked for further clarification on how a scheme strategist and scheme funders are identified and for further distinction between what they are and what they have to do. In addition, a small number of respondents asked for further clarification on what it means to be accountable for a business plan and continuity strategy. They were concerned that, where parties were required to agree or provide opinion on these documents, this could make them accountable.

1  
<https://www.icaew.com/en/technical/audit-and-assurance/assurance/what-can-assurance-cover/assurance-reports-on-master-trusts>

## Our response:

We are pleased that a number of respondents found the draft code useful in developing their understanding of how to identify persons who are subject to the fit and proper assessment. We have made a number of minor changes to the code to add further clarity in this area.

Our expectation is that all trustees should be able to demonstrate at least a basic level of knowledge as part of the fit and proper assessment and how that will be developed further. We do not agree that this creates a barrier for member-nominated or newly appointed trustees. We have made a number of amendments to our expectations in assessing trustee competence at board level to replace the minimum of 10 years' experience, with more focus on what is appropriate for the individual master trust. Our expectation is that boards will be able to demonstrate how they have assessed the presence of the right blend of skills and experience needed for their particular master trust.

We do not agree that the presence of a trustee firm on the independent trustee register is a suitable proxy for the fit and proper assessment as it does not have the same focus or breadth. Similarly, while the independent trustee assurance framework provides an assessment of the system and processes in place for the trustee company, there is not necessarily a strong correlation to the fit and proper assessment for authorisation.

We have updated the code to explain what we mean by a person being accountable for producing the business plan and continuity strategy. We do not expect additional persons to fall within the definition of the strategist where they have a separate requirement to formally approve documents.

## Systems and processes

### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?

The systems and processes section of the code was generally well received, and respondents found the code and guidance content useful. However, the vast majority of respondents were unhappy with the six month time limit for external assessment within the guidance and felt it would create additional burden for master trusts and unnecessary costs.

A much smaller number of respondents asked for further clarity on what was meant by the scope, methodology and supporting evidence for external assessments and questioned if the intent was for us to re-assess the reporting accountant's conclusions

A few respondents asked for further clarification on how a master trust can demonstrate it meets the systems and processes expectations where a third party administrator is used. Clarity was also sought on the requirement for disaster recovery testing and if 12 months would be a more appropriate period.

### Our response:

We understand the concerns raised about the timings outlined in the systems and processes guidance and want to achieve a balance between not increasing burden and the need for current information to be submitted as part of an authorisation application. As the readiness reviews were in progress, we sought to address this issue as quickly as possible and tested a number of amendments with some respondents and we have updated the guidance. Ideally, we would like external assessments submitted to be less than six months old. However, where this is not practical we will want to understand how the trustees have satisfied themselves that no changes have impacted the report's conclusions.

We have updated the code to provide further clarity on our expectations on the scope, methodology and supporting evidence for external assessments. Broadly, our expectation is that we will be able to understand, for example, which control objectives have been assessed, whether a site visit took place and the range of evidence that was taken into account. The presence of an independent external assessment does not provide a proxy for our assessment and we still need to form our own conclusions on the master trust's systems and processes.

We have also updated the code to provide further clarity on our expectations where there is a third party administrator. It is important to recognise that our assessment is focused on the systems and processes for the master trust, whether administered in-house or through an external provider. We understand that there may be practical difficulties where an AAF report may have been undertaken by a third party – for example, the underlying evidence may not be available. In these circumstances, we would expect the trustees to demonstrate how they satisfied themselves that the reporting framework and methodology they adopted meets the needs of their master trust and is fit for purpose.

The aim for trustees should be to demonstrate that a process or IT system feature exists, that it works, and that there is monitoring and governance in place to ensure it continues to work over time. Therefore, the evidence should include the following:

1. The trustees' assessment of the control objective(s) in determining how they satisfied themselves that these meet the needs of their master trust.
2. Details of monitoring and governance processes used by the trustees in ensuring that these remain fit for purpose.
3. Evidence to show the monitoring and governance processes working in practice, eg details of the last review and any action taken.

## Continuity strategy

### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?
- ▶ Are there other ways that the code could allow the legislative requirement in relation to the statement of charges to be met?

Most respondents thought the text was clear in setting out our expectations and the evidence required. However, a significant minority queried the description of the continuity strategy as being a 'high-level and flexible document' given that it needs to include specific information on a wide range of matters.

A number of respondents asked whether key terms used in relation to the statement of charges, such as 'discount level' and 'charge structure' could be clearer. There was also a query on how 'discount levels' manifest in a master trust that uses a bespoke pricing model, noting that there is no basic rate which is then discounted.

One respondent asked whether the continuity strategy could be included as a separate schedule as part of the business plan, as the business plan will need to outline the costs in carrying out the activities identified by the continuity strategy.

Overall, respondents didn't feel there were any significant barriers in being able to meet the expectations around the continuity strategy or statement on charges.

### **Our response:**

The information that must be included in the continuity strategy is set out in section 12 of the Act and regulation 12 of the Regulations. It is important that care is taken to ensure the continuity strategy includes all the required information as set out in Act and Regulations. Not including this information will result in a failure to submit an adequate continuity strategy. Although the legislation covers a range of matters to be included, we do not expect the continuity strategy to be too exhaustive in the level of detail that it is required to set out.

Our expectation is that the continuity strategy should be a high-level but wide-ranging document, setting out the principles and framework for identifying the main actions, decisions and those required to deal with the triggering event and protect members. It should retain enough flexibility to allow the trustees to tailor their approach in response to a specific triggering event that may occur. It should also set out sufficient detail to enable the calculation of the costs identified for the Costs, assets and liquidity plan (CALP). We have reviewed and updated the wording of the code to make this clearer.

In relation to the charges terms used, we have added further descriptions to the 'Need to know' box, including 'discount level', 'charge structure', 'additional charge' and 'third party charge'.

## Scheme funder, financial sustainability and business plan

### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?
- ▶ Does the code provide clarity on how an exemption in respect of a scheme funder carrying out non-master trust related activities will be considered? If not, what more would help?
- ▶ Should use of the basic method be restricted to particular types of master trusts, and if so, why?
- ▶ Should we set out in the code or guidance the factors we may consider in revising the amount used in the calculation of the basic method?

There were no common themes identified by a majority of respondents. However, a smaller number raised some issues.

We received strongly argued responses in relation to elements of the haircuts table. In particular, it was felt that the proposed haircuts for scheme revenue and scheme income were too stringent. The original intention was that these haircuts included an allowance for members and employers moving away from the scheme after a triggering event. The responses argued that allowance for this would be better delivered through the continuity strategy and the scheme's CALP.

Some respondents expressed concerns that the financial requirements might cause issues for some master trusts and were wary of the risk of schemes being overcapitalised. One scheme asked whether we could allow schemes to offset scheme revenue and income against financial reserves before they reach sustainable break even.

Some mixed benefit schemes, and schemes with specific rules governing how scheme expenses are paid, asked for clarity about whether the assets of their scheme could be used towards meeting the financial sustainability requirements.

We also asked questions about guidance we had published - specifically, the basic method for calculating a scheme's financial reserves, which is set out in the code. Respondents were broadly supportive of the concept of the basic method, and there was no consensus for limiting access to it, although a number of respondents mentioned they had no intention of using it. Despite this, there was almost universal support for us to provide details of how we arrive at the per-member figure used in the calculation.

Some responses suggested that the current minimum to be held by schemes using the basic method (£75,000) was too low. The opinions about the appropriate figure varied from £100,000 to £4,000,000.

### Our response:

We agreed with respondents' proposals around haircuts and have made some changes to the CALP so schemes will need to provide an estimated income profile for the scheme after a triggering event. This mirrors similar requirements around costs which are already part of the CALP. We have also reduced the haircuts applied to scheme revenue and scheme income. These are in line with a suggestion made in one response and now reflect only the necessary uncertainty in any forecasting.

We have also taken steps to make the haircuts table clearer, and to remove any duplication. As part of this, and to avoid potential confusion, we have set out separate haircut profiles for different insurance policies that may be held by trustees. These now make a distinction between policies held by trustees to cover normal running costs, and policies intended to cover the costs of a triggering event. We plan to provide more guidance on the acceptable characteristics of certain assets within those outlined in the haircuts table - in particular, our interpretation of what is considered 'cash' or 'near cash'.

We continue to believe the code allows flexibility in the way that schemes demonstrate they meet their financial requirements. Therefore, we have not made changes to the code in this area. The draft code allowed master trusts at sustainable break even to count, or 'offset' the scheme income and/or scheme revenue they expect to receive against their financial reserving requirement. These flows of money would be likely to continue immediately after a triggering event and allowances were made for this in the haircuts table. We accepted the argument that those schemes not yet achieving sustainable break even should also be able to partly offset running costs during a triggering event period. Schemes that have not yet reached sustainable break even will be able to offset less than more mature schemes and will still need to demonstrate significant financial reserves.

The code had allowed for mixed benefit schemes to include scheme assets in demonstrating financial sustainability, as it is a recognised feature of scheme rules, but was not explicit on this point. We have therefore added some additional content to make it clearer.

In respect of the basic method, we felt that a minimum expressed in the millions would not be suitable for smaller and less commercial schemes, for which the basic method is intended. However, on further analysis, we recognise that the £75,000 minimum adequate floor may not be sufficient for every scheme.

Taking account of the consultation responses, we have decided to revise the minimum amount up to £150,000 which we believe is a more prudential estimate of costs incurred by master trusts with less than 2,000 members.

We have also made a few minor adjustments to the code to remove duplication between code and guidance.

## Supervision

### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?

The majority of respondents were satisfied that the expectations set out around supervision were clear. However, there was a call for more detail on the supervisory regime, in particular the content of supervisory returns.

Some respondents were concerned with the requirements for triggering events and significant events, including reporting of those events, for master trusts with multiple scheme funders who were also participating employers. The concerns centred on cases where a participating employer who was also a scheme funder may have an insolvency event, but they did not make any material contribution to the overall master trust's financial sustainability. Respondents felt that in these cases the reporting requirements placed undue burden on the master trust and the participating employer. Further comment was made around the proposed timescales for reporting significant events.

## Our response:

We have previously outlined our plan to publish further information on the supervisory regime. We will be consulting on the supervision and enforcement policy with a view to publishing this prior to the 1 October 2018. This will provide master trusts with a more complete picture of the supervisory regime. Following this consultation we will consider the need for any additional guidance.

We are unable to waive or disapply the legislative requirement to notify us of a triggering event or significant event, where it applies. In relation to mixed benefit schemes that have multiple scheme funders that are also participating employers, Regulation 28 provides for a number of easements on the duties placed on trustees following a triggering event – where this relates to a scheme funder related event (items 4, 5, 6 or 7 of the table in section 21(6) of the Act) and the trustees have decided to resolve the event (continuity option 2).

We would, however, highlight to trustees that it is in their interest to take reasonable steps to ensure those associated with their master trust are aware of their duties, and understand what action they need to take within the context of their master trust.

## Application

### We asked:

- ▶ Does the code make our expectations clear?
- ▶ Is it clear what evidence is required to meet our expectations?
- ▶ Are there any particular barriers to meeting the expectations in the code?

The 'Applying for authorisation' section of the code was generally well received. The majority of comments echoed respondents' general concerns around the standard of evidence considered to be 'adequate' in order to satisfy us that the master trust meets the criteria, and the short time period in which applications need to be prepared.

One respondent felt the code was not clear around the extent to which we would raise any issues identified when considering an application, and whether we would allow changes to be made or additional evidence to be provided.

### Our response:

We have set out our response to the issues of evidence and timing of applications in section 1 of this document. In relation to the 'Applying for authorisation' section of the code, we have introduced additional text to clarify how master trusts can adequately evidence that they meet the requirements.

## Part 3: Decision-making procedure questions

### We asked:

- ▶ Does the proposed procedure provide sufficient and clear information, and if not, how could it be improved?
- ▶ Are there any areas not covered by the procedure (taking into account any guidance on the application process) that you think should be included?

The majority of respondents felt the information provided on the decision-making procedure was clear and sufficient, covering all the relevant areas.

There were a small number of respondents that highlighted the need for having an open dialogue with us throughout the application process and allowing master trusts to clarify, review or provide additional information where deficiencies in the application have been identified.

One respondent emphasised the importance of providing clear reasons for any decision to refuse authorisation of a master trust and felt there should be a right of appeal. Another commented that they were uncertain about the two week timescale for making representations and how this interacts with attending an oral hearing by the Determinations Panel.

## Our response:

It is in the interests of the trustees to ensure they do all they can in order to provide a quality application from the outset, particularly given that it is at our discretion whether to accept any changes or additions to the application. However, we acknowledge there may be circumstances where it may be appropriate to provide new or revised information for an application that has already been submitted. This may include where we are considering a recommendation to refuse authorisation, or where something significant happens that impacts the master trust's ability to meet the requirements.

Following receipt of an application, we will engage with the master trust during the application process to seek clarification where needed about their application submission, the information provided and/ or evidence.

It is important that any new or revised information that is provided to us after an application has been made is submitted expediently, given that we are required to make our decision within a six month statutory timeframe from the date the complete application is received. We will decide whether to accept new or different information based on whether it is fair and reasonable to do so. We are more likely to accept changes or additions where they are submitted earlier rather than later in the process or where the cause is not within the trustees' control. If a scheme's authorisation is refused by the Determinations Panel, the reasons will be set out in a Notice of Refusal of Authorisation and can be referred to the Upper Tribunal as permitted under section 6 of the Pensions Schemes Act 2017.

In recognition of the comments over timings, including dates of oral hearings, we plan to publish a process map alongside the procedure on our website, which we think will help clarify these points.

## Next steps

With the code of practice now published and laid in parliament, and other legislation already in place, master trusts, their advisers and the wider market have a solid base on which to continue to develop their applications for authorisation, while better understanding the new authorisation and supervisory regime.

Over the summer we will be consulting on the supervision and enforcement policy. The final policy will be published for the start of the application period. We will be publishing checklists for the business plan and continuity strategy to help schemes review these documents before applying for authorisation. We will also be considering the need for any additional guidance.

As well as providing feedback to every scheme that submitted a draft readiness review application, we are also looking to publish feedback on the broad themes emerging from the process before the application period starts on 1 October 2018.

## Appendix: List of non-confidential respondents to the consultation

Association of British Insurers  
Aegon  
AON  
Association of Professional Pension Trustees  
Atlas Master trust  
cefni (on behalf of Workers Pension Trust)  
Creative Benefits Group  
Eversheds Sutherland  
ICAEW  
JLT Benefit Solutions Limited  
Lifesight Master Trust (Willis Towers Watson)  
Linklaters LLP  
Mercer  
National Employment Savings Trust Corporation  
NOW: Pensions  
University of Oxford Staff Pension Scheme B&CE (The People's Pension)  
PLSA  
Pensions Management Institute  
Pensions Research Accountants Group  
The Society of Pension Professionals  
Squire Patton Boggs (UK) LLP  
Standard Life Assurance Ltd  
TPT Retirement Solutions  
Willis Towers Watson

A further three respondents requested confidentiality.

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### **Authorisation and supervision of master trusts**

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