THE MEMBER BACKING PENSIONS AND LIFETIME SAVINGS ASSOCIATION

October 2022

MASTER TRUSTS

MADE SIMPLE GUIDE

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1. INTRODUCTION

MASTER TRUSTS ARE SET TO REACH £461 BILLION IN ASSETS BY 2029, MAKING UP MORE THAN 40% OF A £1.1 TRILLION MARKET

Broadridge

WITH ANNUAL VALUE FOR MEMBER TESTS ENFORCED ON SMALL PENSION SCHEMES SINCE OCTOBER 2021, AND EMPLOYEE NEEDS NOW EXTENDING BEYOND THE ACCUMULATION PHASE INTO FLEXIBLE ACCESS, WHERE CAN CORPORATES AND TRUSTEES NOW FIND A VIABLE AND COST-EFFECTIVE PENSION SOLUTION THAT HAS A STRUCTURE IN PLACE TO PROTECT THE EVOLVING INTERESTS OF MEMBERS, TODAY AND FOR THE FUTURE?

This question falls against the current backdrop of the government's determination to push through further measures to protect occupational pension scheme members, several of which may have resource and costing implications, alongside increasing inflation, rising interest rates and the steepest annual fall in living standards since the 1950s.

With master trusts set to reach £461 billion in assets by 2029, making up more than 40% of a £1.1 trillion market (according to research by Broadridge), this guide assesses their rising popularity and sets out how trustees should consider whether master trusts are an appropriate solution to deliver value for their members.

WHAT IS A MASTER TRUST?

A master trust is a multi-employer occupational pension scheme, established under trust, where each employer has its own section within a master arrangement. They offer pension schemes the opportunity to join forces and benefit from economies of scale through shared services, such as administration, investment funds, digital offerings, innovation, IT development and governance. They also provide the benefit of being operated by defined contribution (DC) pension experts.

Operated by experienced and independent trustees, supported by a wider governance structure that includes a funder and strategist, master trusts seek to offer enhanced protection to members. This protection comes not only through the governance structure and expert support teams, but also the regulatory capital they hold and their need to develop long-term business plans that are reviewed and challenged by The Pensions Regulator.

The supervision from The Pensions Regulator requires master trusts to have robust systems and processes, credible financial business plans, and continuity programmes to protect members in the event of failure.

At a time when proving value for members has become an annual regulatory requirement for many schemes, master trusts can also offer a refreshingly simple alternative for consideration. Master trusts are commercially driven. To succeed, they need to have the member at the heart of their offering, while continuing to innovate as these needs change. This competitive commercial environment demands more innovation and a focus on how to really look after long-term member needs, compared to historical pension scheme structures.

AUTHORISATION AND SUPERVISION

All master trusts must be authorised by The Pensions Regulator and are under ongoing supervision to retain authorisation. There are five key areas that standards focus on:

1. **Fit and proper** – All the people who have a significant role in running the scheme can demonstrate that they meet a standard of honesty, integrity and knowledge appropriate to their role.
2. **Systems and processes** – IT systems enable the scheme to run properly and there are robust processes to administer and govern the scheme.
3. **Continuity strategy** – There is a plan in place to protect members if something happens that may threaten the existence of the scheme, including how a master trust would be wound up.
4. **Scheme funder** – Any scheme funder supporting the scheme is a company (or other legal person) and meets the requirement that it only carries out master trust business.
5. **Financial sustainability** – The scheme has the financial resources to cover running costs and also the cost of winding up the scheme if it fails, without impacting on members.

2. THE MASTER TRUST MARKET

HOW MANY MASTER TRUSTS ARE THERE IN THE UK MARKET?

As of May 2022, there are 36 UK master trusts that are currently authorised by The Pensions Regulator:

- Aegon Master Trust
- The Aon MasterTrust
- Atlas Master Trust*
- Aviva Master Trust
- The Baptist Pension Scheme
- BCF Pension Trust
- The Cheviot Pension
- Combined Nuclear Pension Plan
- Creative Pension Trust
- Cushon Master Trust (trading as The Salvus Master Trust)
- The Crystal Trust
- Ensign Retirement Plan
- FCA Pension Plan
- Fidelity
- HSBC Tomorrow (Master Trust)

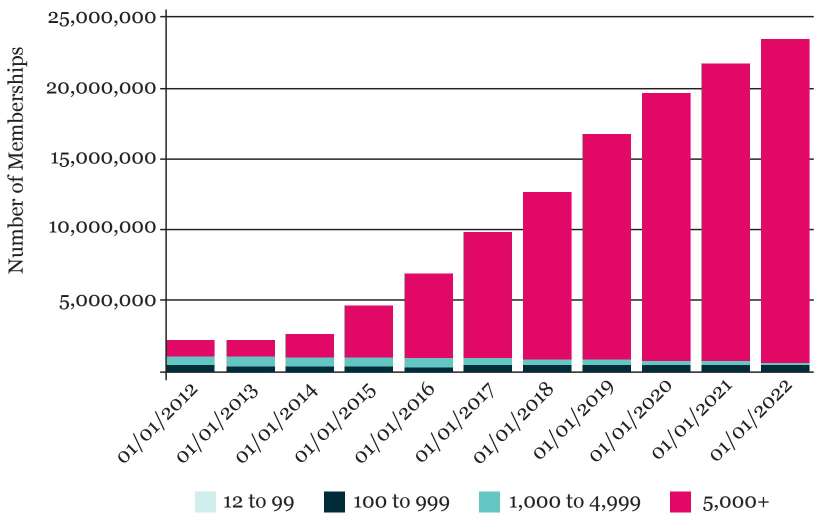
- Industry-Wide Defined Contribution Section (Railways Pension Scheme)
- The ITB Pension Funds
- Legal & General WorkSave Mastertrust
- Legal & General WorkSave Mastertrust (RAS)
- The Lewis Workplace Pension Trust
- LifeSight
- Mercer Master Trust
- National Employment Savings Trust (NEST)
- National Pension Trust
- NOW: Pensions Trust
- Options Workplace Pension Trust
- Smart Pension Master Trust

- Standard Life DC Master Trust
- Stanplan A
- Universities Superannuation Scheme
- The University of Oxford Staff Pension Scheme
- Workers Pension Trust
  Now part of the SEI Master Trust
- The Pensions Trust (TPT Retirement Solutions)
- The People's Pension
- Scottish Widows Master Trust
- The SEI Master Trust

In the past year alone, membership of master trusts has gone up by 10%. According to The Pensions Regulator:

- There are now over 20 million members of a master trust, which account for more than £79 billion of assets (£71.3 billion of DC assets)
- Master trusts hold over £524 million in reserve capital to protect members
- They're set to account for over half of all future workplace pension arrangements.

Figure 1: Memberships of occupational DC schemes by membership size group (including hybrid schemes) (2012-2022)



Source: The Pensions Regulator (TPR)

	DEFINED BENEFIT	HYBRID: MIXED BENEFIT*	HYBRID: DUAL-SECTION	DC (TRUST)	MASTER TRUST	DC (WORKPLACE CONTRACT)**
Schemes	4,800	220	650	27,050	36	1,870
Open schemes	640	20	280	23,110	48	1,490
Total membership	6,478,000	1,040,000	4,422,000	21,859,000	20,672,000	N/A
Total active members	505,000	243,000	931,000	9,473,000	8.944.000	5,363,000

Source: TPR to end 2021

3. HOW DO MASTER TRUSTS COMPARE TO OTHER DEFINED CONTRIBUTION PENSIONS?

A COMMON GOAL

Whether a master trust, single employer scheme or group personal pension (GPP), contributions made by an employer and worker are invested into a fund or selection of funds, with a goal to grow the value of a plan over time. The accumulated pot is then used to provide the member with cash or an income (or both) when they want to spend less time working or retire completely.

What a member receives from a DC scheme will depend on several factors, including:

- The amount paid into a member's plan
- How the investments have performed
- The age at which the member chooses to access their plan
- The way the member chooses to access their plan, i.e. lump sum, drawdown, annuity
- The tax a member pays when they start using their pension
- Charges deducted by the provider.

DIFFERENT APPROACHES

	SINGLE EMPLOYER TRUST	MASTER TRUST	GPP
Regulated by	Overseen by The Pensions Regulator	Authorised and overseen by The Pensions Regulator	FCA
Regulatory capital required for member protection	No	Yes, used if a trigger event is met New master trusts are also required to hold regulatory capital until they reach breakeven	Yes
Member interests overseen by independent parties	Trustee board usually made up of member-nominated, company-nominated and at least one independent trustee. The board is regulated and with fiduciary duties under the Pensions Act	Independent trustee board, regulated and with fiduciary duties and executive powers under the Pensions Act	Independent governance committee with oversight from the FCA. Unlike trustee boards, IGCs are non-executive. They are responsible only for workplace schemes – employees who leave service may fall outside the IGC remit, depending on the provider's operational processes

	SINGLE EMPLOYER TRUST	MASTER TRUST	GPP
Employer costs	Costs are usually borne by both the employer and member. It is usual for employers to meet the scheme administration, advisory and governance costs, with members meeting the investment costs	None, unless otherwise agreed	None, unless otherwise agreed
Member costs	Subject to agreement with the corporate sponsor, usually investment costs as a minimum	All, unless otherwise agreed	All, unless otherwise agreed
Governance	Undertaken by the appointed trustee board, but the corporate sponsor is responsible for the support of the board and ensuring compliance with governance needs	Undertaken by the master trust. This consists of an independent trustee board, funder and strategist to ensure the long-term success of the scheme. There are usually sub-committees and an executive team to support the scheme	Undertaken by the GPP provider with IGC oversight
Communication	Via the provision put in place by the scheme or HR systems	Via the master trust	Via the GPP provider
Operation of scheme	Via the trustee board but supported with oversight from the corporate sponsor and service providers	Master trust is a bundled provision with service providers overseen and operated via the master trust. The service provision is part of the authorisation process and is monitored by The Pensions Regulator	The GPP is also a bundled provision but overseen and operated by the provider
Value for member	Reported to The Pensions Regulator via the chair's statement annually and made publicly available	Reported to The Pensions Regulator via the chair's statement annually and made publicly available	Reported by the IGC and made publicly available
Structure	Single trust	Single trust structure with separate sections for each scheme	Separate arrangement for each scheme with individual member policies in each

Innovation	As needed or afforded through the budget set by the corporate sponsor. Some schemes – particularly larger ones, are innovating to improve member communications, administration and at-retirement services, but the overall picture is mixed	Commercial success and long-term financial viability needs to be demonstrated to the wider market as well as to The Pensions Regulator. Commercial success drives innovation in a competitive market. Innovations such as personalised communication, enhanced retirement offerings and financial wellbeing are all being offered	Innovation is driven through the service provider and its commercial strategy
Retirement offering	Usually a single cash lump sum or transfer to annuity or drawdown provider	Minimum FCA pathways and ability to take retirement savings flexibly (cash, drawdown or annuity) Value providers will offer ‘to and through’ provision, supported by guidance, modelling tools, holistic view of all wealth to make choices, access to advice and fully flexible choices at retirement	Minimum FCA pathways and ability to take retirement savings flexibly (cash, drawdown after transfer out, or annuity)

4. REDUCING THE EVER-INCREASING GOVERNANCE BURDEN

NEW REGULATIONS CAME INTO FORCE IN JANUARY 2022, WITH THE PENSIONS REGULATOR NOW REQUIRING SOME SCHEMES TO REPORT ANNUALLY HOW THEY ARE DELIVERING AND ENHANCING VALUE FOR MEMBERS. IT'S THE VIEW OF THE DWP AND TPR THAT SMALLER SCHEMES WITH LESS FINANCIAL RESOURCE CAN STRUGGLE TO MATCH THE GOVERNANCE AND MEMBER OUTCOMES THAT LARGER SCHEMES CAN PROVIDE (SOMETIMES REFERRED TO AS THE 'SCALE DIVIDEND').

As a result, schemes that fail to match value-for-member benchmarks will be expected to start the process of transferring to a larger scheme or explain how they plan to improve value, including member outcomes, in the short-term.

Additional regulatory requirements include:

- Annual chair's statement – to include value for member assessments
- Implementation statement – demonstrating how the objectives of the Statement of Investment Principles (SIP) have been achieved over the year
- TCFD reporting – demonstrating the scheme's approach to climate-related risks and opportunities, together with results against core metrics
- Scam prevention intervention and stronger nudges to Pension Wise for pre-retirement financial advice.

Many of the schemes that are subject to the annual value assessment (those with assets below £100 million) will be evaluating and reporting their value metrics for the first time in 2022. The pace at which this will lead to them consolidating into a master trust can't yet be predicted, but there has been a recent trend towards consolidation.

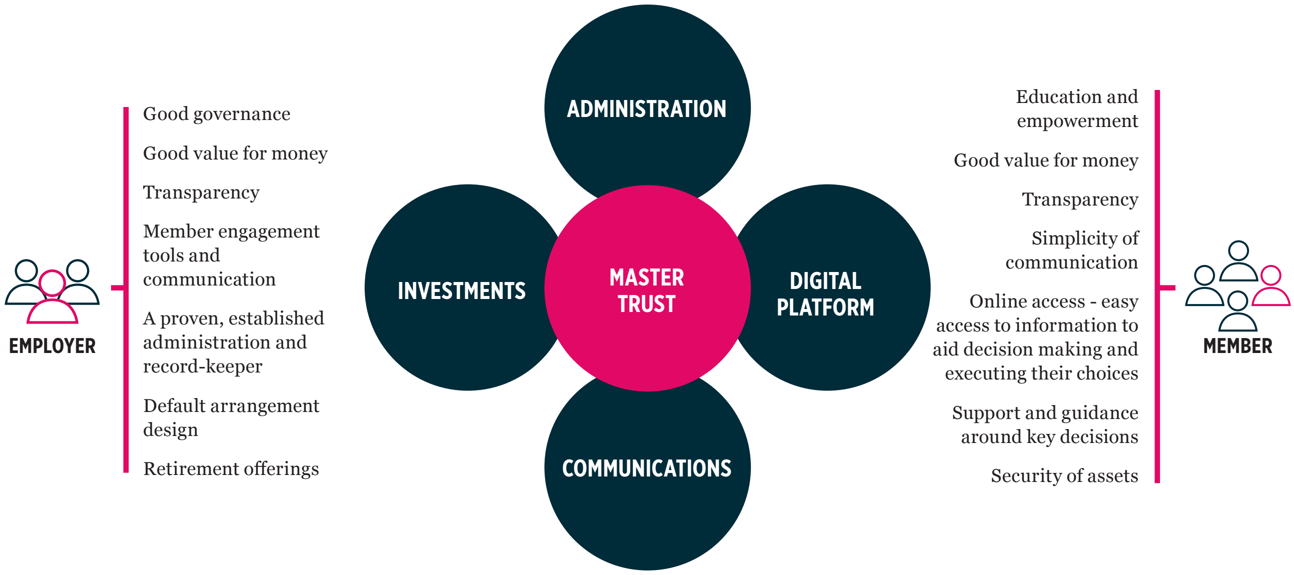
5. ARE MASTER TRUSTS NOW CONSIDERED TO BE THE BEST SOLUTION?

SEVERAL ISSUES HAVE ARISEN WITHIN THE WORKPLACE PENSION MARKET IN RECENT YEARS THAT REQUIRE CORPORATE SPONSORS AND TRUSTEES TO REASSESS THEIR OFFERING TO MEMBERS:

- Regulatory requirements are on the rise
- New governance and reporting requirements are creating more cost pressures
- Member needs are evolving as their pots grow over time
- The number of deferred members within workplace schemes is increasing (increasing scheme costs, while simultaneously reducing active member value).

The Pensions Regulator has made it clear that in its view, master trusts are likely to be the most cost-effective and financially viable vehicle to deliver ongoing value. The rationale can be categorised by considering what a good master trust can provide for both members and corporate sponsors:

MEETING EMPLOYER AND MEMBER NEEDS



<table>
<tr><th>CATEGORY</th><th>BASELINE OFFERING</th><th>VALUE-ADDED OFFERING</th></tr>
<tr><td>Governance</td><td>Outsource pension scheme to the master trust, removing the governance burden and future change risk
Pensions Regulator authorised, supported by a strict supervisory regime intended to ensure they remain so
Regulatory Capital reserved for members' protection
Master trust trustee board, funder and strategist
Member and corporate sponsor forum for feedback
Clear communications, i.e. chair's statement with transparency for members</td><td>Can offer dual governance structure to work with corporate sponsor/hybrid scheme structures
Management information (MI) and measurements for effectiveness for corporate sponsor or governance structure</td></tr>
<tr><td>Scale</td><td colspan="2">Scale can bring with it many benefits, including:
More resource and focus on scheme governance/development
Lower costs through higher purchasing power and benefiting from shared or operational synergies
Innovation and development
Choice and scale of offering can be obtainable via scale as the wider infrastructure supports it</td></tr>
<tr><td>Expertise</td><td>Dedicated and experienced trustee board with supporting executive team to operate the master trust. No other schemes to operate and full-time focus of the team is the master trust and its members</td><td>Use of wider corporate teams and resource to support the operations of the master trust and its development, i.e. investment management, risk, legal, compliance, finance, digital, communications etc.</td></tr>
</table>

CATEGORY	BASELINE OFFERING	VALUE-ADDED OFFERING
Retirement offering	At retirement, master trusts usually embrace the full range of Pensions Freedoms options	▸ Guidance and support to help members understand their retirement choices ▸ Communications designed to be personalised and support member decision-making ▸ Consideration of the retirement journey to ensure that members do not lose value by removing, or reducing, movement between funds into and through retirement, and that charges do not vary between the accumulation and retirement phases ▸ Asset allocation is considered regularly by the trustee board and strategist, to limit risk or loss of value for members, avoiding de-risking and re-risking as an example
Financial wellbeing		Value-added master trusts have started to offer financial wellbeing to support member decision-making and engagement within their offering. For some schemes this is simply guidance, while the more developed will offer open banking, savings goals, budgeting tools, wealth tools to view all finances in one place, online tracing and consolidation tools, and extended support for retirement planning.

CATEGORY	BASELINE OFFERING	VALUE-ADDED OFFERING
Engagement	Master trusts must meet basic communication requirements under regulation and law Many master trusts offer more than basic communications which seek to provide targeted information in an effective way to different members	- Some schemes are focused on offering the most effective communications by considering the most appropriate medium and style for different types of members. Offering personalised communications that can be sent via SMS nudges, email, post or via the website/app, and then looking at which language and topics are most appropriate to a member throughout their lifetime, can greatly enhance engagement and therefore member outcomes. - Integrated communications can also be tracked and amended to evolve over time. - Considering member feedback and data can lead to bespoke and targeted campaigns for those at risk or those who require tailored communication. Value-added offerings will provide this service to again drive better member outcomes. - Retirement communications are essential and value-add schemes will offer bespoke communications that evolve according to the stage of retirement and support needed, creating a personalised journey for members, e.g. early retirement vs active retirement, and travelling vs later life.

6. CONSIDERATIONS FOR MOVING TO A MASTER TRUST

THERE ARE SEVERAL DUE DILIGENCE, FIDUCIARY AND LEGAL REQUIREMENTS TO CONSIDER WHEN MOVING TO A MASTER TRUST. CORPORATE SPONSORS ARE RESPONSIBLE FOR THE FUTURE CONTRIBUTIONS OF MEMBERS AND WILL WANT TO ENSURE THEY ARE CONFIDENT WITH THE PROVIDER GOING FORWARD. INCUMBENT TRUSTEES ARE RESPONSIBLE FOR THE LEGACY ASSETS OF MEMBERS WITHIN THE SCHEME AND ARE REQUIRED TO ENSURE CERTAIN OBLIGATIONS ARE SATISFIED, UNDER REGULATION AND LAW, SO THAT MEMBERS ARE NOT LEFT IN A DETRIMENTAL POSITION AND THEIR TRUSTEE FIDUCIARY DUTIES ARE FULFILLED.

Authorised master trusts must go through a thorough evaluation process and – once authorised – are then subject to ongoing supervision. That regime includes a suspension of new business activity if there are any issues which The Pensions Regulator considers to be of concern. The 'safe harbour' approach is further endorsed by DWP regulations on bulk transfers without consent. (This is the most common mechanism by which trustees transfer pre-existing pension assets from one occupational pension scheme to another.) Although some light-touch due diligence is recommended, DWP is satisfied that the regulatory oversight processes are sufficiently strong that bulk transfers to authorised master trusts can avoid much of the time, risk and advisory costs that used to be required.

TRUSTEES' LEGAL REQUIREMENTS

Fiduciary duties

- Trustees must act in the best interest of members. This can relate to ensuring members are not financially disadvantaged by any transfer and that no adverse impact on their benefits takes place as a result of a scheme closure and bulk transfer.
- Trustees need to ensure that the overall benefits provided by a master trust are no less beneficial. Key questions will be:

1. Is the closure/bulk transfer capable of being made in a manner that is consistent with the rules and other legal requirements (i.e. do the trustees have the power to agree)?
2. Should you agree: is it a proper use of the trustees' powers?

There is no one solution to satisfy these questions. However, the DWP offers guidance that suggests that trustees consider the following:

1. Compare the receiving scheme to the existing scheme
2. Not every aspect of the receiving schemes need to be equal or superior
3. Quantitative and qualitative tests can apply
4. Legal review of schemes is an option but not compulsory
5. Investment mapping may also be needed.

Bulk transfers

- Member engagement: there is a 60-day notice period for active scheme members as well as a 30-day transfer notice that the trustee will need to send to members.

DUE DILIGENCE (also see Section 10)

Due diligence can be performed through the help of in-house advisers or external consultants with knowledge of the master trust market. The process can then take place via a market review, legal review, investment review and commercial proposal, or a full tender process via an independent consultant. As noted above, the authorisation process does allow for a lighter-touch due diligence process than was the case in the past.

When undertaking due diligence, the key areas of consideration are usually:

1. **Administration**

   Review of the administration services and processes of a master trust is considered to be part of the systems and processes – a key part of the authorisation process by The Pensions Regulator. This therefore should provide assurance of the provision provided.

   Within a master trust administration can be provided in-house or through a contractual relationship. A master trust should have strict service level agreements (SLAs) that the scheme can review and compare against, as part of the reporting process. These can be enhanced through service credits which incentivise providers to meet those SLAs. As part of the review, the service contract and SLAs can be compared to the current provider within the scheme.

2. **Governance**

   A master trust will have a governance structure that consists of a trustee board, funder and strategist. In addition, there will be sub-committees with supporting policies and processes. This oversight and operational structure protects member interests and ensures the operational efficiency of the scheme.

   A review of the governance structure (which is another core authorisation consideration by The Pensions Regulator) is recommended as part of the provider review.

   Consideration should also be given to how the governance structure of a master trust might work within existing mechanisms of the incumbent scheme.

   Ensuring that governance structures work for the ceding scheme and corporate sponsor is essential. Typically, most value-added master trusts can accommodate them.

3. **Communication tools**

   Member engagement and communication is a key consideration for both trustees and corporate sponsors. In a recent HSBC Tomorrow study, a third of corporate decision-makers wanted to improve their pension engagement with members.

   In the past, communications were led by telephone and post, with members usually either seeking operational help or transactional support. As DC pots grow, member audiences increase and generational needs change, so communication strategies and mediums used to engage members need to continually evolve.

   To effectively communicate with members, the right media and language is needed, especially given how consumers are now continuously bombarded by brands on a daily basis. With many members not used to making financial decisions, several master trusts are turning to enhanced communication strategies that can incorporate personalisation, nudges and other services, like modelling tools, budgeting and short-term savings (financial wellbeing). The purpose is to engage with members via shorter-term topics that will support longer-term savings habits.

As an example, a member in their 30s may be more likely to engage with a campaign that encourages them to budget via open banking so they can pay down debt or save for a mortgage. A platform that helps a member manage shorter-term financial needs like this can also establish a new savings behaviour or habit around their long-term savings (pension planning).

While paper-based regulatory communications may still be required for some members, other engagement campaigns (like the one above) can be digitally delivered, which reduces costs, while also providing a comprehensive communication strategy.

While The Pensions Regulator considers a scheme's overall communication strategy, its focus will remain around regulatory communications (e.g. welcome packs, wakeup packs, annual benefit statements).

4. **Investment offering**

Although there are different approaches to investment strategies, all default investment funds offered by master trusts are reviewed as part of the authorisation process by The Pensions Regulator. All of them are regularly reviewed by investment consultants, whose assessments are readily available. This therefore should provide some assurance of the suitability of the investment solution.

We look in detail at the investment offering later in this guide. However, in relation to due diligence duties, transferring trustees will need to ensure that members are not placed in a detrimental position. This can be translated as assessing that an investment offering offers an appropriate strategy for an employer's workforce demographics, and that appropriate investment governance is in place.

In addition, trustees will need to ensure that all regulatory requirements, such as climate change targets and disclosures, are offered by the master trust.

Some degree of investment mapping is usually undertaken between the current investment proposition and that of the master trust, as well as any other regulatory requirements or aspirations of the ceding scheme. Mapping could be provided by the master trust and then reviewed by the ceding scheme's investment adviser. This process can reduce transition costs (the selling and buying of different investments during the bulk transfer process) where some – Stamp Duty being the foremost – usually come into play.

5. **Retirement and decumulation**

Master trusts can offer an outsourced solution for employers, either as a fully outsourced model or for the process known as signposting at retirement. This is where a particular master trust, working with another scheme that doesn't offer drawdown, can accept transfers purely for the purposes of taking an income. The transferring scheme trustees will undertake and maintain some due diligence of the chosen provider.

At the point of retirement, members of single employer schemes must transfer out of their scheme in order to take income. This can create both increased risk and value loss for members, as they are likely to find themselves with an investment portfolio that needs to be divested before being reinvested into a typically higher-fee fund offering.

It's at this point that members are most exposed to possible scams or value loss due to incorrect or non-decision-making. Indeed, the effect of movement at retirement will often be more penalising than negotiating 1 or 2bps off the annual investment management charges.

Good master trusts seek to provide a 'to and through' experience for members. Members typically have access to retirement support and communications, including education and modelling tools, as well as investment solutions aligned to retirement strategies and lower fees.

Like accumulation, retirement includes multiple phases, which requires understanding to offer members the appropriate services. These include active retirement, retirement and later life. Some members may also find themselves in ill-health that requires early retirement.

Value-added master trusts will offer members support through any and all of these phases, with continued communications, retirement MOTs or check-ins, as well as access to flexible income options.

6. **Charges**

   As an indicator of value, master trust charges are often compared against the incumbent scheme. This can be a challenging comparison due to differences around the service provision, governance and regulatory oversight. However, it can be a useful benchmark.

   The real test is to show that members are not placed in a detrimental position by moving to a master trust. Multiple factors will therefore be considered in determining value. Cost will be one, but ultimately it's about delivering better member outcomes.

7. **Employer support**

   The final consideration will be to what degree the corporate sponsor will be willing to support the ceding scheme. It is not uncommon for corporate sponsors to seek to reduce the cost and governance burden a pension scheme can place on a company, especially now that workforces are becoming increasingly transient and deferred member numbers are rising.

   If a corporate sponsor seeks to remove scheme support and decides to direct all future contributions to a master trust, a different conversation and process emerges for the trustee, as their decision-making will be based entirely around what would become a wholly deferred membership. However, for all of those members still in employment, 'reconnection' with their ongoing contributions will be a material consideration that the trustee will need to consider.

7. INVESTMENTS

MASTER TRUSTS AND THEIR INVESTMENTS ARE SUBJECT TO THE SAME LEGISLATION AS ALL OCCUPATIONAL PENSION SCHEMES AND MUST COMPLY WITH THE PENSIONS REGULATOR'S CODES OF PRACTICE.

Specifically, the Pension Schemes Act 2017 and the Occupational Pension Schemes (master trusts) Regulations 2018 apply to the authorisation and supervision of all master trusts. Additional relevant legislation and codes of practice also apply, including (but not limited to) the Pension Schemes Act 2004 and the Pensions Act 1995.

Within current legislation there are specific requirements relating to scheme investments, governance and reporting, as well as roles and responsibilities with which master trust investments must comply.

ROLES AND RESPONSIBILITIES

Trustees retain ultimate responsibility for investments and the governance surrounding them. They are also required to take advice from suitably qualified advisers before making any investment decisions. The law also requires that trustees have knowledge and understanding of pensions and trust law, as well as the general principles of investment.

Trustees may delegate certain tasks and decisions to an investment sub-committee, but they must satisfy themselves that those undertaking the tasks are performing them in accordance with section 36 of the Pensions Act 1995.

Trustees are also responsible for deciding when investment advisers are to be used, depending on their level of knowledge and understanding, as well as the legal requirements under the Pensions Act.

Trustees are accountable for:

- Setting the investment objectives and strategy
- Selecting fund managers and the fund range, including the default fund
- Monitoring, reviewing and replacing funds and/or managers
- Establishing and overseeing the investment governance processes
- Investment communications to members.

GOVERNANCE

Effective investment governance through accumulation and into decumulation is one of the most important factors in delivering good member outcomes. Investment risks must be included in the risk management process, including the identification, measurement, prioritisation and resolution of such risks. This entails ensuring there are appropriate and robust processes to receive relevant data from the investment manager, at least once a quarter.

Investment governance must be documented. This includes recording roles and responsibilities and reporting relationships.

A typical investment governance structure for a master trust may take the following form:

- Trustees set the overall investment objectives and strategic investment decisions, with advice from a legal adviser and investment consultant regarding what key components should be taken into consideration
- Day-to-day investment decisions will be delegated to appointed investment managers
- An investment sub-committee, including independent members, may be used to provide trustee board support and recommendations, as well as ongoing monitoring and assessment of the investment solutions.

Regular reviews must be performed around the investment governance structure, assessment of investment risks, and investment decisions taken.

Such reviews should include assessments of:

- Board performance when setting the strategy and objectives
- How the selected investments have performed against the set strategy and objectives
- Whether the costs incurred in providing investments offer appropriate value for members
- Investment consultant performance against pre-agreed objectives (in line with Competition and Markets Authority requirements).

SETTING OBJECTIVES AND STRATEGY

The Occupational Pension Schemes (Investment) Regulations 2005 require trustees to produce a statement of investment principles (SIP), which sets out the investment beliefs, objectives, strategy and policies of the trustees.

Such policies need to cover:

- Financially material considerations, including ESG and climate change, and how voting rights and engagement activities are undertake
- How members' views on non-financial matters (such as ethical or social impact beliefs) are considered in investment decisions, noting that the trustee retains primacy in investment decisions
- Stewardship policy regarding voting and engagement across the whole investment chain. Where investments are undertaken through pooled investment vehicles it is the investment managers who will undertake voting and engagement. However, the trustee must ensure that actions taken are appropriately aligned to their own objectives and beliefs, and are adequately reported.

Since 1 October 2020, trustees need to produce an annual implementation statement, which sets out how they follow the objectives set out in the SIP. They must also provide examples of how they (or more likely their investment managers) have acted with regards to voting and engagement. This is included in the annual scheme report and is made publicly available on a website.

MONITORING AND REVIEWING STRATEGIES

All investments need to be regularly assessed against their objectives and industry benchmarks. The process is documented and considers all costs and charges, including transaction cost.

Default funds, and their performance, must be reviewed every three years – or immediately if there are any changes in investment policy or the demographic profile of members. Such a review needs to assess the performance against the set objectives.

The SIP must be reviewed every three years – and immediately if there are any changes in investment policy, having received advice from a qualified adviser.

A change in the demographic or behaviour of the membership may result in a decision to change the investment strategy, which would result in a change to the SIP. This would be further reported in the implementation statement.

Longer-term horizon reviews should consider market conditions and evolving products and investment techniques in order to remain at the forefront of investment capabilities. Changing investment strategies and funds should consider potential transition costs and the options available to mitigate them, ensuring positive member outcomes are at the heart of all decisions.

DEFAULT FUNDS

Default investment funds are those into which contributions are placed without the member having expressed a choice, or in which 80% or more of members have actively chosen to invest at any relevant time.

Trustees of a master trust must assess whether any of the scheme assets fall within the definitions, which might include ‘accidental defaults’ (i.e. not those funds which the trustee originally designed as a default).

Accidental defaults can arise through either more than 80% of the members self-selecting the fund, or though the closure of a fund (temporarily or permanently) requiring contributions to be automatically diverted to another fund (recent examples are where property funds have been suspended due to liquidity constraints, with members’ contributions automatically switched into a cash alternative).

Defaults established to comply with automatic enrolment regulations are subject to the legislative charge cap (0.75%, excluding transaction costs, at time of publication [2022]).

KEY INVESTMENT DESIGN PRINCIPLES

Master trusts should have default strategies suitable for the majority of members, while offering alternatives to cater for everyone else (i.e. cash or an annuity, if drawdown is the default position at retirement within the scheme).

An appropriate choice of investments must also be made available to those members who do not wish to invest in the default arrangement. The interests of both active and deferred members must also be considered equally. This includes members in decumulation.

Trustees should engage regularly with members in order to assess their beliefs regarding investments, including on ethical, religious, social and environmental issues. While pension scheme members historically lacked engagement, surveys suggest that investment issues such as these trigger a higher response rate.

Addressing these issues not only helps to inform trustees on their investment strategy on an ongoing basis, but they are also an important step to increasing members’ interest around how their savings are invested.

INVESTMENT DESIGN

Given the long-term nature of pension planning, members are likely to have different needs at different life stages. For example, a member close to retirement is more likely to accept lower investment returns in exchange for lower volatility than a member who is 30 years from retirement and can more easily absorb and accept short-term market volatility.

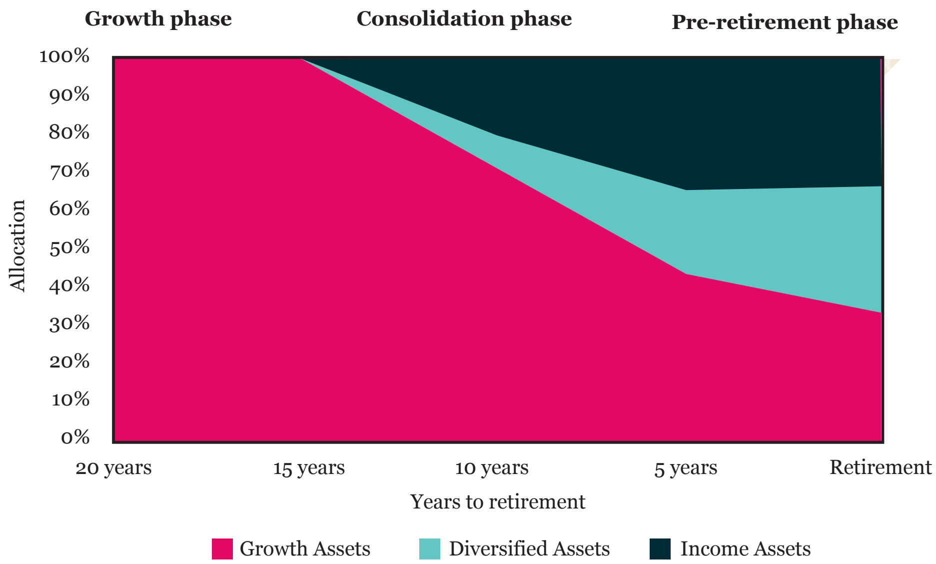
Such considerations have led to most default fund structures embracing a target-based investment approach, where investment strategies gradually de-risk a member’s investment portfolio as they move closer to retirement.

Target-based investment glidepaths will generally consider three life stages:

- **Growth** (typically more than 15 years from retirement and invested in growth funds to provide higher potential returns)
- **Consolidation** (transition from the growth stage to 5 years before retirement and invested across growth, diversified and income-producing assets)
- **Pre-retirement** (the final years before benefits are actually taken and invested more conservatively to manage volatility)

While the timeframes for each phase will vary between different trustee strategies, this de-risking approach is a common feature, aiming to improve member outcomes by offering the greatest growth potential in the early years, together with financial stability later in life.

An example lifestyle glidepath: This glidepath has no specific allocation to cash. Cash is seen in glidepaths to allow access to the 25% tax free cash available to members after 55. Cash itself is not always an efficient asset class for members, as other assets can derive more value especially as we do not know when the member may wish to access this cash allowance. Therefore a liquid asset class that can still offer valuable attributes to the portfolio is preferable and removed from the example portfolio. Research has shown that members do not always retire at the time they say they will and investments are already liquid, meaning that cash can create a negative drag for members' returns – hence it being removed without hindering return or flexibility at retirement.



While a default glidepath would typically target flexible income (drawdown) at retirement, alternative glidepaths are also made available for members to choose, which may target full cash withdrawal or an annuity purchase. Such alternatives can also be made available as the scheme's default fund if the demographic of the membership suggests that it would suit the majority.

ALTERNATIVE INVESTMENTS

While the majority of members in a master trust will fall within the scheme's default arrangement, a range of alternative 'self-select' funds should be made available for those who would prefer to take control of their own investments and/or choose a different glidepath.

Self-select fund ranges vary in number across different master trusts, but best practice would see members given the opportunity to increase or decrease the risk of their portfolio through direct equity or fixed income funds, while providing specialist alternatives to suit their own religious, ethical and/or environmental beliefs.

SECURITY AND LIQUIDITY

Investment portfolios should be structured to ensure assets are secure, have reasonable liquidity, and are of sufficient quality to provide overall profitability. Assets need to be invested predominantly through regulated trading markets. Any deviations should be detailed in the SIP, explaining how their use aligns to the investment strategy.

Trustees of a master trust must consider how the assets of members are protected in case of an asset failure or default, and how such losses might be covered through indemnity insurance and/or the Financial Services Compensation Scheme.

FUND FULFILMENT

Having set a scheme investment strategy and objectives, and designed any required lifestyle strategies, the trustees must select the appropriate investment funds and managers. Within a lifestyle default arrangement there can be many component parts contributing to the overall growth and risk management objectives of each part of the glidepath. Individual fund selection therefore needs to ensure that the collective objectives can be fulfilled.

Analysis of active versus passive asset management and the use of statistical techniques are included in the assessment of the selected funds and managers.

Trustee investment beliefs are set out in the SIP, and it would be expected that any appointed investment manager will operate their mandates/funds in line with such beliefs.

RESPONSIBLE INVESTING

Financially material risks must be considered over the anticipated term of the scheme, reflecting the demographics of the members and potential beneficiaries. ESG and climate change bring both risks and opportunities as the world transitions towards a net-zero carbon economy. But factors such as social impact, waste and water management, corporate governance and board diversity should all be considered in the investment process of a master trust.

Such risks and opportunities need to be viewed in the short and long term: for example, the short-term risks of transitioning to a low-carbon economy can be as impactful as longer-term systemic macro-economic risks relating to global warming.

Most master trusts use investment funds, and the selection of the investment house and manager needs to be considered in light of the trustees' own responsible investing beliefs as well as the fund strategy and underlying assets themselves.

More recent developments include consideration of the 'Just Transition' – meaning how trustees will achieve the climate transition while considering the wider social and societal impact of this transition, such as for workers and communities who are currently reliant on polluting industries. This social impact of the transition needs to be fully considered alongside climate change policies and ambitions.

COSTS AND CHARGES

Evaluation of investments (choice, fees and performance) forms a significant component of the annual value-for-member assessment, which is reported through the annual chair's statement to members, where all member-borne charges are disclosed.

As noted above there is a maximum charge of 0.75% p.a. on any default fund used for automatic enrolment. Legislation also states:

- No commission can be payable relating to member investments.

Investment management charges are discussed in more detail in the PLSA's Cost Transparency Made Simple Guide and include:

- Management fees
- Performance fees
- Transaction costs
- Ongoing charges
- Borrowing and lending fees

8. ENHANCING MEMBER RETIREMENT OUTCOMES

SEVEN YEARS HAVE NOW PASSED SINCE THE PENSIONS FREEDOMS WERE INTRODUCED, HERALDING AN ERA OF PROFOUND CHANGE FOR PENSION SCHEME MEMBERS.

The PLSA would like to see more support on offer from schemes to help retirees access the right products for their circumstances. In *Retirement Choices: The Evolution of Products and Suppor*t, the PLSA evaluates the work being undertaken by pension providers, schemes and master trusts, and aims to assess where these solutions may go in the future.[1]

Many commercial pension providers (GPP providers and master trusts) now offer in-scheme retirement options, with members able to choose how they access their pension savings directly from the schemes they have saved into.

Support for members includes referrals to Pension Wise (compulsory from June 2022), pre- and post-retirement support through educational material, robo-advice, on-line modelling tools (e.g. 'how long will my money last if I continue to withdraw at this rate? How do I make it last longer?'), and targeted nudges.

A scheme that can provide pension income choices (often referred to as a 'to and through' scheme) could provide an easier route to some retirement options over a scheme that can't. An employer's choice of provision is therefore becoming vitally important in achieving both increased value for contributions and greater workforce satisfaction.

TACKLING THE DECUMULATION PHASE

Around 615,000 people have accessed pensions via drawdown since it was introduced, according to the FCA. It seems unlikely that in the foreseeable future we will witness annuity rates rising to a level that will slow the decline of annuity purchases and dampen member demand for low-cost, simple drawdown options.

Value during the decumulation stage should be a vitally important consideration for schemes and savers, which is why the PLSA has published proposals for Guided Retirement Income Choices and an analysis of the state of the decumulation market.

As it stands, if members are required to transfer out of their scheme to another provider in order to gain a drawdown income from their pension, value can be depleted in a host of ways. These include:

- Advice costs
- Transition costs of selling and buying units
- The period when investments are out of the markets
- The fees charged by the new provider

Depending on the severity and permutations of these risks, it is perfectly feasible for members to immediately lose value from their pension. Over time, the higher charges of retail products compared to the charges typical of a master trust can significantly increase the overall value loss to members.

The table on the next page represents a snapshot of research undertaken by Bayes Business School, commissioned by HSBC Retirement Services and Hymans Robertson. It represents two lower- and higher-income baby boomer cohorts at the point of retirement and the impact that transferring out of a scheme can have on pot value and income in the short and long term.

1. https://www.plsa.co.uk/Policy-and-Research/Document-library/Retirement-choices-the-evolution-of-products-and-support

	AVERAGE PENSION POT VALUE	AVERAGE PENSION INCOME	AVERAGE ISA INCOME	FAILURE RATE AT 90 (%)	ANNUAL INCOME LOSS AT NRA*	ANNUAL INCOME LOSS AT 90
Lower Income Baby Boomer						
Transfer to retirement within existing provider i.e. master trust	£33,062	£800	£342	4.4		
Transfer to external master trust at retirement	£32,040	£787	£335	6.7	-£89	-£181
Transfer out via passive IFA	£31,311	£787	£332	12.2	-£246	-£500
Transfer out via active IFA	£30,448	£779	£329	15.3	-£296	-£602
Higher Income Baby Boomer						
Transfer to retirement within existing provider i.e. master trust	£135,113	£3,291	£1,402	4.7		
Transfer to external master trust at retirement	£131,828	£3,262	£1,385	5.3	-£336	-£683
Transfer out via passive IFA	£127,848	£3,243	£1,370	12.8	-£1,116	-£2,269
Transfer Out via active IFA	£124,810	£3,235	£1,350	16.1	-£1,305	-£2,653

**This data is based on the assumption that in both cases the member draws down 4% of the initial value of their pension, a 25% tax-free lump sum taken that sits in a tax-free ISA, that withdrawals rise 3% annually and that annual fees are 0.35% p.a. and 2% p.a. respectively.*

***NRA – Normal retirement age*

Indeed, the research indicates that lower-income baby boomers who are forced to transfer are up to three times more likely to face pot exhaustion by the time they reach the age of 90 compared to those who have the choice to stay in and withdraw an income from their current scheme.

9. ENGAGING TO DELIVER BETTER OUTCOMES

A NEW KIND OF ENGAGEMENT CHALLENGE

The success of automatic enrolment has created a seismic shift in pension scheme membership in recent years – from 49% of employees in the financial year 2012 to 2013 to 75% of employees in the financial year 2019 to 2020, according to government statistics.

However, aligned with the success of automatic enrolment is the three-fold problem of continued member preconceptions, in-action and indifference around pensions and long-term financial planning:

- Low savings and trust in industry: Most members (69.8%) forecast that they will have slightly or much less than they need in their pension pot to retire comfortably, with almost a third of pension scheme members (31.5%) saying they have “no or very little trust” in the industry, according to a 2021 report from pensions administrator Trafalgar House.[2]
- More pressing financial concerns/prioritisation today: We have been faced with an unprecedented set of events over the last two-and-a-half years creating financial, emotional, social and political stresses. Members still seek to prioritise their short-term financial needs over their long-term ones, and there is the ongoing challenge of effective engagement.
- Transient workforce: Automatic enrolment has undoubtedly increased membership, but with people now having around 11 jobs during their lifetime, the number of workers with small pension pots under £1,000 has surged. At the same time, it’s estimated that up to 1.6 million workers have now lost track of their workplace pensions, according to the Association of British Insurers.[3] This can lead to data issues, as member data is out of date and due to a lack of engagement with pensions providers members do not seek to update their details. This is why regular engagement on a wide array of financial subjects that are personalised or relevant to members is key.

WHAT CAN MASTER TRUSTS OFFER?

As the pensions market evolves, a central issue to consider is what members need both now and in the future.

How do we envisage members engaging with their pension in five to 10 years? As pot sizes grow, due to the undoubted success of automatic enrolment, while membership attention turns to rising living costs, a solution that can help them manage their day-to-day finances, short-and medium-term savings and longer-term financial plans (like pensions) in one place could be a more attractive proposition.

Historically, a holistic solution like this has proved difficult to deliver, due to a corporate sponsor or trustee’s remit stretching only so far as an occupational pension. However, the rising popularity of master trust solutions is already helping to bridge this gap, providing more value and relevance to a member’s pension saving, while ensuring the same levels of protection as other pension providers.

Broadly, this type of offer could be bundled into a financial wellbeing solution, but it can be more than that. As an example, a master trust operated by a bank or insurer could join savings accounts, current accounts and budgeting tools with long-term savings, insurance and wider wealth.

Through regular interactions with a member on their financial matters, master trusts potentially have a better chance to change perceptions and drive behaviours around saving for the longer term.

2 Trust & Confidence Index 2021 | Trafalgar House Pensions Administration
3 Thousands more make contact with long lost funds - GOV.UK (www.gov.uk)

10. MOVING TO A MASTER TRUST

FOR THE TRUSTEE TO AGREE A MOVE TO A MASTER TRUST PROVIDER VIA A BULK TRANSFER, THEY NEED TO ENSURE THAT THERE IS NO DETRIMENTAL IMPACT TO MEMBERS – IN SHORT, THAT THE TRANSFER IS IN MEMBERS' INTERESTS. WHILE THERE IS NO TEMPLATE FOR THIS PROCESS, IT TYPICALLY LOOKS TO VALUE FOR MEMBER AND IS THEREFORE FOCUSED IN THE KEY AREAS BELOW, WITH ADDITIONAL DETAILS ON THE BULK TRANSFER ARRANGEMENTS INCLUDED AT THE END OF THIS DOCUMENT. AS PART OF THE TRUSTEE DUE DILIGENCE AND TO ALLOW THAT THEIR FIDUCIARY DUTY CAN BE HANDED OVER, THE KEY AREAS OF CONSIDERATION TYPICALLY ARE:

- Conversation has taken place between corporate sponsor and trustee to understand what is wanted from the move and any changes to circumstance. This will help understand what 'value' means to a scheme
- Appropriate due diligence has taken place on the market. This can be an RFP but it can also be a market review
- Understanding of the investment proposition and any changes or costs associated with this, in association with the scheme investment adviser
- Review of current scheme legal documents against that of a master trust to understand any differences and ensure alignment where needed
- Retirement provision, support and costs
- Governance arrangements for the scheme going forward and reporting requirements
- Financial strength of the master trust funder
- Future innovation and alignment to regulatory requirements.

When the above requirements are met and a provider is selected, a transition can take place. This is the process of moving the relevant data and records held by one administrator to a new administration platform, while simultaneously moving the assets and ensuring that the right investments are allocated to the right members.

The timetable to move to a master trust will vary depending on the ceding structure and speed of all parties involved. It can typically take three to six months, with quicker moves for GPPs and longer timetables for trust-based schemes.

DEDICATED AND EXPERIENCED TRANSITION TEAMS

Master trusts employ transition teams that can project-manage the whole transition process from start to finish – and indeed into the post-project reconciliation and wash-up activities.

Master trusts' competence to transition-manage is assessed by The Pensions Regulator as part of the authorisation process and is monitored under its supervision regime.

For any transition project, an appropriately qualified project manager will be allocated, whose role is to ensure that:

- The project team is appropriately budgeted
- The project team is appropriately resourced, with full stakeholder representation
- It is collectively competent to carry out the programme tasks (or has access to such competent resource)
- Everyone understands their role, what is expected of them and when
- The transition timetable is achievable, considering any other scheme events that may be scheduled

- Member communications are regulatory-compliant, accurate and user-friendly
- That key documents (such as transfer deed and deed of participation) have the requisite legal approvals
- Payroll interfaces and automatic enrolment compliance are in place, with training where required
- Third-party resources are primed and ready, and there are no contractual impediments
- All third parties are aware of (and committed to) the programme and the timetable
- There is appropriate authority for the final go/no go decision

ROBUST PLANNING

Transition plans comprise two core components: data transition and investment transition.

- Data transition ensures that the transferring and receiving platforms can safely and securely identify and transmit data. Systems are checked for compatibility, data quality is evaluated, and (if appropriate) rectification plans evolved. Pre-transfer tests will be undertaken ahead of the full transfer.
- Investment transition seeks to minimise any costs involved in switching assets from the transferring scheme to a master trust. There are numerous permutations of how and when such costs can be incurred, influenced by the similarities or dissimilarities between investment strategies. Ahead of any transition programme the transition project will identify their likely magnitude, and identify strategies that can be used to minimise them. These include pre-funding to avoid the risks of members missing investment opportunities (the 'out of market risk'), re-registration of assets from one trustee/platform to another, and in-specie transfers where close asset-match opportunities are identified to defray the costs of selling and buying.

For both transition components, post-transfer reconciliations are an inherent part of any project.

11. CONCLUSION

HALF OF UK COMPANIES NOW CONSIDER A TRANSITION TO A MASTER TRUST TO BE THE BEST SOLUTION TO REDUCE THE TIME AND RESOURCES SPENT RUNNING A PENSION SCHEME RELIABLY, ACCORDING TO A SURVEY COMMISSIONED IN 2022 BY HSBC TOMORROW MASTER TRUST.

As scrutiny around delivering value for members becomes more intense, employers are said to be “crying out for new ideas”. However, the risks that businesses, especially large companies, face when seeking to introduce a new offer remain.

But while change harbours risk, so does doing nothing. Consider ESG – this is a risk now widely understood, firmly embedded in the investment decisions we make, and carries with it regulatory support. Indeed, many bodies are actively seeking metrics to proactively manage future risk.

Master trust membership is increasing by 8 to 10% annually, suggesting that employers see any risks of transition being mitigated by multiple factors:

STRUCTURE

Essentially, the more a master trust can encourage its members to save for a better retirement, the more assets they hold. So, unlike other DC pension offerings, a member’s ability to financially flourish in the future becomes a mutual goal that both they and the master trusts want to reach.

A FUTURE-PROOFED PROVISION

With regulatory requirements on the rise, new governance and reporting requirements, and an increasing deferred membership with small pot values, the scale and structure of a master trust could help alleviate increasing cost pressures.

MEMBER SUPPORT

The scale of a master trust and its need to be commercially competitive ensures ongoing investment in value-added services to enhance their offering and member experience. This will often include financial wellbeing tools, engagement, protection against scams, decision-making assistance or digitalisation, to reduce risk and cost to members.

The transition from accumulation to an income fund or retail offer is now identified as one of the biggest risks to a pension pot and value, potentially costing members over 1% of their pot and leaving them open to sequencing risk and scams. Master trusts have both a business and regulatory interest to deliver a seamless and cost-free journey to, through and into retirement.

REGULATION

Master trusts operate under strict regulatory structures that are managed by experienced, professional and independent trustees, with rigorously defined support roles provided by a funder and strategist. The regulatory capital a master trust is required to hold, and the legal obligation to develop long-term business plans, which are reviewed and can be challenged by The Pensions Regulator, provide member security.

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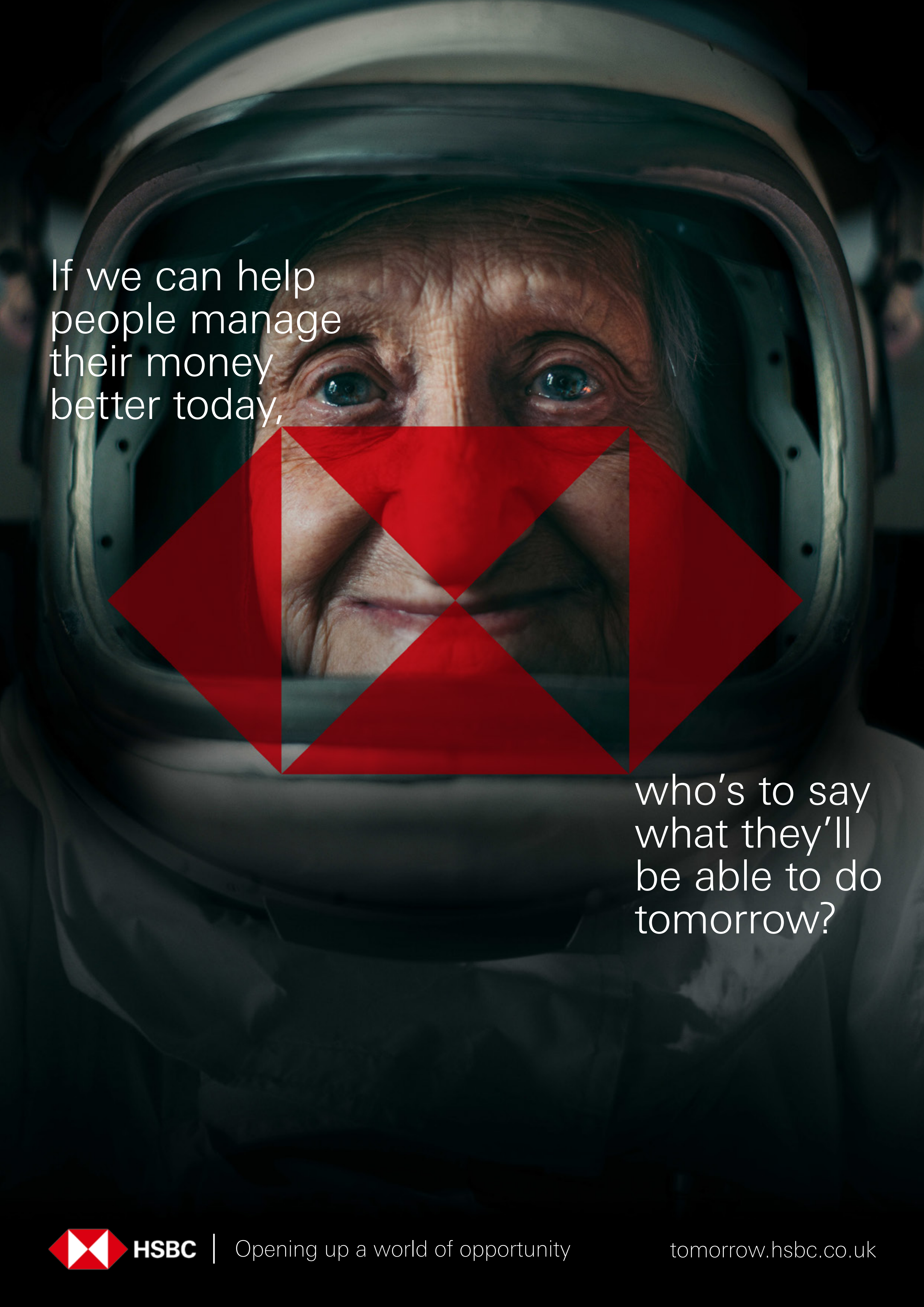
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