



Department
for Work &
Pensions

Master Trust Authorisation and Supervision Regime

Government response to the public consultation

March 2018

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1. Introduction

- 1.1 The Master Trust market has expanded significantly since the introduction of Automatic Enrolment in 2008. Membership of Master Trust schemes has increased from 270,000 at the beginning of 2012, to almost 10 million this year¹. Both member numbers and assets under management by Master Trust schemes are expected to continue to rise significantly over coming years as individual employer occupational pension schemes consolidate and Automatic Enrolment contributions increase.
- 1.2 There is currently a broad consensus that the existing regulatory controls are insufficient to provide appropriate levels of protection to Master Trust scheme members.
- 1.3 Under the Pensions Scheme Act 2017 (the 2017 Act), existing Master Trust schemes and new schemes wanting to join the Master Trust market will be required to be authorised by the Pensions Regulator (the Regulator).
- 1.4 The aim of the Master Trust scheme authorisation and supervision regime is to ensure that:
 - members of Master Trust schemes have equivalent protections to members in other types of pension schemes;
 - the risks specific to Master Trust scheme structures including the size and scope of schemes, lack of employer engagement, diverse business models and other factors that influence their financial resilience and viability, are proportionately and proactively regulated; and
 - there is an appropriate balance between preventing risks occurring and giving the Regulator powers to intervene when necessary.
- 1.5 The new Master Trust regime will be administered by the Regulator who will produce detailed practical support for schemes in its Code of Practice (Code) and operational guidance. The Code will make clear what the Regulator expects to see from Master Trust schemes if they are to meet, and continue to meet, the authorisation criteria. It will also clarify the expectations on Master Trust schemes when they face a significant change or experience problems that put their members' interests at risk. A draft of the Code will be published shortly and will be subject to a separate public consultation.
- 1.6 This document presents a summary of the responses to the public consultation on the draft Occupational Pension Schemes (Master Trusts)

¹ DC Trust: presentation of scheme return data 2017-18 (TPR, January 2018).
<http://www.thepensionsregulator.gov.uk/doc-library/dc-trust-presentation-of-scheme-return-data-2018.aspx>

Regulations 2018² and the Government's approach to drafting the regulations.

- 1.7 The consultation response has been broken down into four policy chapters:
- Scope and application
 - Authorisation process
 - Authorisation criteria
 - Controls and monitoring

2. The Regulations

- 2.1 The draft regulations set out the details on how the Government proposed to implement the provisions of the Master Trust authorisation regime specified in the 2017 Act. In preparing the draft regulations the Government applied its regulation principles:
- **Transparency** – being open and keeping regulations simple and user-friendly.
 - **Proportionality** – only intervening when necessary, making remedies appropriate to the risk posed, and costs identified and minimised.
 - **Accountability** – the Regulator must be able to justify decisions, and be subject to public scrutiny.
 - **Consistency** – Government rules and standards must be joined up and implemented fairly.
 - **Targeting** – focusing on the problem and minimising side effects.
- 2.2 In developing the draft regulations the views of stakeholders were taken into account as set out in the consultation document.

3. Summary of Key Proposals

- 3.1 Once the draft regulations come into force, all Master Trust schemes, as defined in the 2017 Act, will be required to be authorised in order to operate in the pensions market. If a scheme decides not to apply for authorisation or authorisation is declined, it would need to wind up and leave the market.
- 3.2 Authorisation is a one off process and Master Trust schemes will not have to be re-authorised. The Regulator will maintain a supervisory role to ensure Master Trust schemes continue to meet the authorisation criteria.

² The consultation ran from 30 November 2017 to 12 January 2018:
<https://www.gov.uk/government/consultations/draft-occupational-pension-schemes-master-trusts-regulations-2018>

- 3.3 To become authorised, Master Trust schemes must satisfy the Regulator that they meet the following five criteria:
- The persons involved in the scheme are fit and proper persons;
 - The scheme is financially sustainable;
 - Each scheme funder meets specific requirements;
 - The systems and processes used in running the scheme are sufficient to ensure that it is run effectively; and
 - The scheme has an adequate continuity strategy.
- 3.4 The onus will be on Master Trust schemes to provide the Regulator with the necessary evidence that they meet the required criteria.
- 3.5 The Regulator will have an ongoing supervisory role. To support this, Master Trust schemes will be required to submit annual supervisory returns. These will inform the Regulator's on-going risk assessment of schemes and ensure a routine reporting requirement for all schemes involving at least annual contact.
- 3.6 If a Master Trust scheme experiences a 'triggering event' (an event that puts the future of the scheme at risk) the scheme must already notify the Regulator within 7 days. If a scheme has experienced a triggering event its trustees must submit an implementation strategy (which sets out what it will do to address the event) that includes the statement of its charges to the Regulator within 28 days. The scheme must not take on any new employers or introduce new or increased charges until it has resolved the triggering event, or wound up the scheme.
- 3.7 If the scheme decides to wind up, or is required to wind up, it must transfer the members of the scheme out in accordance with the processes set out in the draft regulations.

4. Consultation Summary

- 4.1 This consultation has been conducted in line with Cabinet Office consultation principles³.
- 4.2 The formal consultation period ran from 30 November 2017 to 12 January 2018. During this consultation period, officials met with stakeholders in the pensions industry to increase understanding of how the draft regulations will impact the Master Trust market. The consultation was launched at a Government event on the 30 November attended by 80 stakeholders. Views expressed at the event as well as at other stakeholder meetings have been taken into account in formulating the Government's response.
- 4.3 62 written responses were received from the trustees of schemes, the key industry representative bodies, those who act as professional advisers to schemes, the scheme employers connected to one scheme and one members' representative body. The organisations who responded are listed in Annex 2.
- 4.4 The consultation document focused on the policy underpinning the Master Trust regime. It asked a number of questions which have been the focus of the responses. These questions are listed in Annex 1.
- 4.5 However, while many respondents did answer some or all of these questions, most addressed other issues instead of or in addition to these questions. Therefore, the Government response follows the same structure as the consultation document and is not limited to solely responding to answers for those specific questions.
- 4.6 The consultation did not ask questions on issues where policy has already been determined. For example, some aspects of the draft regulations are enshrined in the 2017 Act and are not subject to change. Where responses sought clarity on interaction between the draft regulations and the 2017 Act, these have been addressed either in this consultation response or will be addressed in the Regulator's Code of Practice.

³ (Cabinet Office, January 2016)

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/492132/20160111_Consultation_principles_final.pdf

5. Consultation Response

Overview

- 5.1 The Government is grateful to all those who submitted responses to the consultation. The responses were invaluable in helping to develop a deeper understanding of how the draft regulations will impact on the Master Trust sector.
- 5.2 The majority of the responses welcomed the authorisation and supervisory regime and agreed that, overall, the Master Trust market is not currently adequately regulated. There were some challenges on policy approach to some aspects of the regulations, some drafting and minor technical points, and requests for clarification. The draft regulations have been amended where appropriate.
- 5.3 The Government has considered in particular its approach to those responses requiring further policy consideration. These fall into main themes including disapplications (where respondents felt that some, or all of the elements of the authorisation regime should not apply to certain scheme structures), the authorisation fee, definitions of scheme funder/scheme strategist, and details of the business plan. The Government's views on these issues can be found under the relevant Chapter headings in this document.
- 5.4 In developing and finalising these draft regulations, the Government has been mindful that the IORP 2 Directive⁴ is due to be transposed in the UK by 13 January 2019. Where appropriate, the requirements of the Directive have been reflected so that these draft regulations will contribute to the UK's transposition of it. However, these draft regulations are not the only means by which the UK will meet the Directive. Proposals in other areas will be published for consultation in due course.
- 5.5 The 2017 Act and the draft regulations apply to any Master Trust scheme that operates in Great Britain (GB) and which meets the definition in Section 1(1), including that it is an occupational pension scheme. It has always been intended that Northern Ireland would introduce parallel legislation and the Government understands that it will do so, in due course.
- 5.6 The consultation was open to comments from schemes based in Northern Ireland, and some asked how the legislation will apply to them. A scheme that

⁴ This is a revision of the 2003 IORP Directive. It is primarily concerned with improving pension scheme governance and disclosure to members and is largely aligned with the UK's public policy priorities for private pensions. The Government is clear that while the UK remains a member of the European Union we will continue to exercise our rights, and meet our obligations, as members. This includes transposing EU directives into UK law.

is based in Northern Ireland and only open to employers and members based there will be able to continue to operate and will not be required to seek authorisation until parallel legislation is introduced in that jurisdiction. However, a scheme based in Northern Ireland that is open to employers and members based in GB will be prohibited from operating in GB unless it is authorised.

6. Chapter 1: Scope and Applications

- 6.1 Chapter 1 of the consultation paper set out the definition of a Master Trust scheme in the 2017 Act: an occupational pension scheme which provides money purchase benefits and is used or intended to be used by two or more employers, but not only by connected employers, and is not a relevant public service scheme. This definition is deliberately broad in order to ensure the Master Trust authorisation regime captures the full range of relevant structures that exist now and may develop over time.
- 6.2 The consultation document listed the proposals to take certain schemes out of the authorisation regime:
- Certain schemes offering mixed benefits:
 - Closed membership statutory schemes.
 - Defined Benefit multi-employer schemes offering only additional voluntary contributions (AVCs) and/or transfers in for their defined benefit members.
 - Single member and relevant small schemes where specific circumstances apply.
 - Adding to the definition of connected employers in the 2017 Act to exclude more schemes where the risks are similar to single employer schemes.
- 6.3 It set out that the proposed draft regulations would bring certain schemes into the authorisation regime, largely to avoid the development of schemes which adopt a structure that carries the same risks as a Master Trust scheme, but would avoid the need to be authorised. The sort of schemes which were considered to be treated as Master Trust schemes were:
- multiple schemes that are subject to common control as a single 'cluster' Master Trust scheme.
 - parallel accumulation and decumulation schemes subject to common control which will be treated as a single Master Trust scheme.
- 6.4 The consultation also proposed limited disapplications on the requirements of scheme funders for existing Master Trust schemes that offer both Defined Benefit (DB) and money purchase benefits, where the only scheme funders are the participating employers.

Government Response

6.5 Many responses to the consultation were entirely content with the proposals for disapplications and applications and the majority stated that it should be clear to schemes whether they were required to apply for authorisation.

Consideration of further disapplications

6.6 A number of responses expressed a strongly held view that the scheme(s) which they represented, or on whose behalf they were making a collective response, should not be captured by the authorisation regime at all. Some suggested that the definition of a Master Trust scheme (and, therefore, the scope of the authorisation regime) may have expanded beyond the original policy intention, arguing that one or more of the following applied to them:

- they do not face the risks which the regime is intended to address,
- that existing legislation / regulation provides adequate protections (either pensions legislation or Prudential Regulation Authority (PRA)/ Financial Conduct Authority (FCA) requirements)
- the trouble and costs of authorisation would be disproportionate to the increased protection for members.

6.7 Some of these responses stated that the effect of being caught by the regime would be to force a wind up of the scheme or, for mixed benefit schemes, the wind up of the money purchase aspects or section(s) of the scheme. In the case of the latter, this might itself trigger a requirement to also wind up the DB section(s) of the scheme.

6.8 The characteristics of the schemes referred to included:

- Existing non-associated multiple employer schemes, whose responses included mention of one or more of the following characteristics:
 - Not for profit, non-commercial or charitable schemes.
 - Schemes not established by statute, but by employers themselves established by statute or otherwise sponsored by the Government.
 - Industry-wide or multiple employer schemes with a “community of interest” (e.g. church-based, or linked through an association or society).
 - Schemes that do not promote or market themselves beyond the existing employer group.
 - Schemes with highly engaged employers, some of which also emphasised that the number of employers can be small (<10).
 - Schemes with ‘small’ numbers of members (ranging from 20 to 5000) and that are unlikely to grow.
 - Mixed benefit schemes where provision of Defined Contributions (DC) benefits is a minority activity.
- ‘Legacy schemes’ sponsored by a PRA-regulated insurance company and the scheme is not a qualifying scheme for automatic enrolment purposes.

6.9 The Government has fully considered all these representations but does not propose to introduce any new complete disapplications to Part I of the 2017 Act. In making this decision, the following factors have been considered:

- The Government always intended to capture the broad range of multiple employer schemes that provide money purchase benefits. It was never the intention to limit the definition, and thereby the authorisation requirements, to purely “commercial” schemes. Not for profit schemes also need to be sustainable and secure in order to protect members. Similarly, the intention is not to only capture schemes that provide pensions for automatic enrolment purposes.
- The nature of some Master Trust schemes does mean that some of the risks addressed by authorisation are lower. However, it remains the case that these do apply to some degree, again, potentially leaving members exposed to certain risks.
- Existing legislation or regulation does provide some parallel protections, but none provides fully adequate assurance that the scheme is well run and financially sustainable in the manner required by the Master Trust authorisation regime. The 2017 Act and draft regulations allow the Regulator to take such existing protections into account where these are relevant to its assessment of the scheme (see relevant sections in Chapter 3 – authorisation criteria).
- The new requirement for authorisation will require the schemes to demonstrate that they comply with the five authorisation criteria and the Government recognises that this is not an insubstantial hurdle to overcome. However, unless the bar is set at an appropriate level the intended impact of authorisation will not be achieved.

Draft Regulation 3 – connected employers

6.10 Consultation responses suggested that the Government should use the meaning of connected employers as set out in the Occupational Pension Scheme (Scheme Administration) Regulations 1996. However, the 2017 Act refers to a different section of the Companies Act 2006 than the 1996 regulations to establish the basis on which employers are connected. This definition is more appropriate for the purposes of the authorisation regime and means there does not need to be a separate test in relation to partnerships.

6.11 Respondents queried the percentage of voting rights which give rise to employers being connected (set at 33%). The Government has determined that this is the appropriate approach because this is the deemed level for control under the Insolvency Act 1986 and is used for the application (or potential application) of the Regulator’s Moral Hazard powers.

6.12 There were some helpful comments in relation to specific parts of draft regulation 3 and some amendments have been made to clarify the following:

- Operating as a single business; specifically there must be a formal agreement in place between the companies so the position of the shareholders is economically as close as possible to holding shares in one company comprising the combined business.
- The extent to which group undertakings are connected where employers meet the conditions set out in regulations.

Draft Regulation 25 – disapplication for closed membership statutory schemes

- 6.13 Some responses asked for this disapplication to allow such schemes to continue to introduce new defined benefit members where that is being done so that the scheme continues to have a statutory employer for the purposes of section 318 of the Pensions Act 2004. The disapplication is intended to apply only to a small number of schemes where the risks are very low. If the scheme is introducing new members it is required to be authorised.

Draft Regulation 26(1) to (3) – single member schemes and relevant small schemes

- 6.14 The draft regulations were considered to achieve the intended effect for the vast majority of relevant small schemes, often referred to as Small Self-Administered Schemes (SSASs). There were some points raised about how the disapplication might apply to the circumstances of single member schemes and we have amended the regulation to make this clearer.
- 6.15 Some respondents queried how the Regulator would respond to unintentional or temporary changes in a SSAS which might bring the scheme out of the disapplication. For example, a change in the number of members in the scheme which results in less than 50% of the trustee board being members. To continue to qualify for the disapplication for SASSs, the trustees of these schemes will need to address any change to their structure or governance arrangements in a timely manner. However, we recognise this balance may be particularly difficult to achieve where a SSAS has a single member and have amended the regulation to allow for this.

Draft Regulation 26(4) – disapplication to schemes where the only Money Purchase benefits are Additional Voluntary Contributions and/or transfers in

- 6.16 There was general support for the proposal to exempt schemes that only provide AVCs or transfers in. There were some questions as to what is meant by or included within the term “AVC”. The term should be given its plain English meaning:
- “Additional” would be over and above the member’s contributions required to be paid as a condition of membership of the scheme.
 - “Voluntary” would suggest that the member has made an active choice to make such contributions and they are not compulsory.

- 6.17 Some responses asked that the following should also be included in this disapplication and amendments have been made to clarify that they are included:
- Members who are contributing to AVCs, but their participating service in the DB part of the scheme has been capped.
 - Pension Credit Benefits also known as pension sharing on divorce (where the spouse is not an active member of the scheme).

6.18 We also received comments around including matching employer contributions and salary sacrifice. However as these are about how an AVC might be funded, they do not need to be specifically referred to in the regulations.

6.19 A few responses suggested that the disapplication should be extended so that bulk transfers between DB schemes should be available, including to DB consolidators. This disapplication is intended to be a narrow one; to allow DB multi-employer schemes that only offer AVCs and transfers in to continue to offer these benefits to their DB members. The Government considered the merits of DB consolidation in its Green Paper on DB schemes last year and will publish its proposals in a White Paper shortly.

Draft Regulation 27 – disapplication of certain scheme funder requirements

6.20 There was support for the disapplication offered by Regulation 27 to certain scheme funder requirements for existing mixed benefit schemes where the only scheme funders are participating employers.

6.21 A number of respondents asked that Sections 21 and 22 should be disapplied as they create and require notification of the triggering events 4 to 7, which relate to an employer (that is a scheme funder) leaving the scheme due to insolvency or a decision to withdraw. The Government has considered this and concluded that while it is not appropriate to remove the notification and trustee decision requirements for these triggering events, it can disapply requirements for an implementation strategy, freeze on charges and a prohibition on new employers where the scheme can readily resolve the event. Amendments to the draft regulations have been made to this effect.

6.22 There were some requests for additional disapplications of provisions of the Act. These were all considered and the Government has concluded that either:

- A disapplication is not appropriate. For example Schedule 3, paragraph 7 extends the requirement in section 70 of the Pensions Act 2004 to require scheme strategists and scheme funders to report a breach of the law. This is limited to where they have knowledge of a breach and, therefore, it is not unreasonable for this to apply to them; or
- other disapplications have the same effect.

- 6.23 There were some requests to disapply specific references to scheme funders in the draft regulations. Such disapplications can only be made to the Act itself. However, we have made some amendments to clarify the relevant regulations.
- 6.24 Some responses asked if the disapplications in Regulation 27 could be extended to existing MP only schemes, where the only scheme funders are the participating employers. The Government does not consider that this is appropriate. There are a small number of schemes, which have been established relatively recently, as multi-employer MP benefit schemes that rely only on the employers to make up any shortfall in costs. There is further information in Chapter 3 to clarify how the financial sustainability requirements apply to such schemes.

Draft Regulation 28 – application to cluster schemes and to parallel accumulation and decumulation schemes

- 6.25 Responses broadly agreed that multiple single schemes with “persons in common” that face the same risks as Master Trust schemes should be treated as Master Trust schemes and be required to be authorised. The wording setting out the persons in common has been amended to make it clear that where a scheme is not a Master Trust it would be the person performing an equivalent role.
- 6.26 Drafting improvements have also been made to ensure that where schemes are disappplied under other regulations that they are not inadvertently brought back in by this provision. The Government has also specified additional circumstances where the provision in regulation 28(2) to treat two or more schemes as a single Master Trust should not apply.

Clarifications on the scope and application of the Act

- 6.27 A number of points were raised in relation to clarity of the scope of the Act and the disapplications and applications in the draft regulations that will be addressed in the Regulator’s Code of Practice. These are not individually addressed here.
- 6.28 A small number of responses asked for clarification that non-occupational pension schemes, such as Group Personal Pensions, are not within scope. This is the case.
- 6.29 The Government can also confirm that the authorisation regime does not apply to the DB aspects of a mixed benefit scheme. If a mixed benefit scheme meets the definition of a Master Trust scheme it will need to apply for authorisation and satisfy the Regulator that it meets the five authorisation criteria or wind up the money purchase aspects of the scheme. If there is no power to wind up just the money purchase aspects of the scheme, the Master Trust must cease to operate the scheme to the extent that it provides money purchase benefits (the 2017 Act, s39(4)).

- 6.30 When a mixed benefit scheme submits its application for authorisation to the Regulator it should include the information that relates only to the money purchase aspects of the scheme, unless stated otherwise. The exception to this is the scheme accounts which should be submitted as a whole (the 2017 Act, s39 (2)). In a mixed benefit Master Trust scheme where the key people, the systems and process, and the financial structures are common to the defined benefits and money purchase benefits, the scheme will almost certainly need to provide details of the interaction, so that the Regulator can be satisfied that the scheme meets the criteria.
- 6.31 Some existing mixed benefit schemes have been set up on a sectionalised, segregated or split basis. The Government was asked that the draft regulations make provision for the sections of the scheme to be treated as separate pension schemes. The Government has considered this and does not believe it is appropriate. While the funding for these schemes may be sectionalised, the authorisation criteria are wider than this. Assessing the systems and processes as well as the fitness and propriety of those running the scheme, requires a view across the scheme as a whole.
- 6.32 Some respondents raised concerns that winding up the money purchase aspects of a mixed benefit scheme could trigger the whole scheme to wind up. In particular, that this would trigger section 75 of the Pensions Act 2004 and the employer debt requirements would need to be met. The Government recognises that there are cases where it may be appropriate for schemes to enrol individual members in order to ensure that an employer's commitment to the defined benefit part of the scheme is maintained. It is important to strike the right balance between allowing schemes to resolve employer departures and ensuring that wider statutory protections are not undermined. As such, the Government does not intend to build anything into the Master Trust authorisation regime that extends or facilitates these arrangements.

7. Chapter 2: Authorisation Process

- 7.1 Chapter 2 of the consultation paper covered the authorisation process and the requirement for a Master Trust scheme to be authorised in order for it to operate in the pensions market. The Government provided an outline of the principles for the authorisation process.
- 7.2 The Government also announced that a fee would be required to support the application. The fee is necessary to reflect the need for the Regulator to recover the costs of processing applications from Master Trust schemes without directly placing these costs on the wider pension community.
- 7.3 The Government consulted on two levels of fee to represent the different requirements placed on the Regulator for processing applications relating to new and transitional Master Trust schemes. The Government recognised that more work was required to determine a robust forecast of the likely cost of the Regulator's processes, in order to calculate the levels of the respective fees, and, therefore, the figure consulted on was a maximum amount.
- 7.4 Regulation 4(5) of the draft regulations provided an initial indication of the levels of the respective fees based on the operational details of how the Regulator would process applications on a strict cost recovery basis.

Government Response

- 7.5 The Government is grateful for the responses received on this issue. Some questions were raised in respect of the application for authorisation (draft regulation 4) and the information to be included in the application. These primarily related to minor technical points and increasing the clarity of some aspects of the regulation. Regulation 4 has been amended, where appropriate, to address these concerns.
- 7.6 Some common themes emerged from the consultation around the proposed charging structure and, in particular, the level of the fees and their impact on different models of Master Trust schemes. Schemes also questioned why the proposal included two levels of fee and wanted a better understanding of how this approach was justified.
- 7.7 The Government has considered the responses and has concluded that having two fees is the correct approach. Further work has now been completed which provides additional clarity on the Regulator's cost of processing an application. Consequently, the Government with the Regulator has revised the proposal for the fee levels. These will be:
- a flat fee for new Master Trust schemes of £23,000
 - a flat fee for transitional Master Trust schemes of £41,000.
- 7.8 A new scheme is likely to have significantly less evidence for the Regulator to assess. For example, a new scheme is unlikely to have historical company

information, and might not be actively operating the necessary systems and processes. As such, the Regulator's assessment will not be as complex as for an established scheme which is already in operation, and where there will be historical data to review and assess. New schemes will be subject to higher supervision, however, the cost recovery only relates to the authorisation application, therefore, this will not be reflected in the fee. Furthermore, the cost of making a decision is higher for existing Master Trust schemes where the decision sits with the Determinations Panel, an independent committee of the Regulator. For new Master Trusts, the decision to authorise will be made by the executive arm of the Regulator and therefore the process of referring the application and the delegation for approving the decision rests with a single decision maker.

- 7.9 The Regulator will work closely with all Master Trust schemes to ensure that those seeking authorisation are aware of all the requirements to meet the authorisation criteria. The fees have been set at a level to ensure they only recover the costs of processing the application at the point at which the application is received. They will not be used to cover the design of the Regulator's approach to any pre-application work, for example, readiness reviews or future supervision.
- 7.10 Some respondents have suggested a tiered fee should be used where the level of the fee would be determined by the complexity of the application. This approach has been considered by the Government with the Regulator but would bring its own significant challenges. In particular, with this approach, the Regulator would need to pre-determine the complexity of the application prior to assessing it because the fee for authorisation must be paid at the point of application. The Regulator considered whether specific factors, which could be identified at the point of authorisation, pre-determined the complexity of authorisation (e.g. the number of members or employers participating) but could not identify an approach that would provide a direct correlation as these characteristics in isolation did not make the application more or less complex. The Government has concluded that the original approach proposed of having two levels of fee based on whether the scheme is new or transitional is the correct because this is the factor that will clearly drive the cost of processing an application.

8. Chapter 3: Criteria for Authorisation

- 8.1 Chapter 3 of the consultation paper covered the five criteria that a Master Trust is required to fulfil in order to be approved for authorisation by the Regulator. Comments are set out for each of the criteria below.
- 8.2 In addition, some of the respondents set out an intention to apply for authorisation and asked in relation to their specific circumstances how the Regulator would be likely to assess their compliance with the criteria. While the Government is not able to respond to these requests in this response, the Regulator will be providing practical advice on what they will expect to see provided in a successful application in the Code and guidance. Further, the Regulator is offering existing schemes the opportunity to submit a draft application and receive feedback on whether sufficient evidence has been provided in support of the application.

Fit and Proper Persons Requirement

- 8.3 The first of the authorisation criteria is that the Regulator has to be satisfied that those running Master Trust schemes are fit and proper persons. Section 7 of the 2017 Act sets out the roles to be assessed. In addition, the Regulator may assess those who promote or market a Master Trust scheme or other roles. The draft regulations set out that those persons will be subject to:
- an integrity test which covers such issues as criminal convictions and bankruptcy;
 - a conduct requirement which allows the Regulator to take into account previous behaviour and to monitor behaviour in the future.
- 8.4 In addition, scheme strategists and trustees will be subject to a competency test, which will ensure that they have the appropriate knowledge, experience and qualifications to carry out their role.
- 8.5 The framework for the tests was set out in draft Regulation 5 and Schedule 1. The 2017 Act requires that these are the matters the Regulator must consider.

Government Response

- 8.6 Some issues were raised which related to the 2017 Act rather than the regulations, but merit clarification:
- The definition of a scheme strategist can apply to a not-for-profit scheme. The Government intends that “business decisions made in relation to the commercial activities of the scheme”, should be interpreted broadly. A scheme that does not intend to make a profit or to operate in a specific industry only, must still offer an attractive proposition to its employers and members within the wider commercial market in which it operates. It will seek to at least cover its costs, ensure third parties provide value for money and that it is generally run efficiently. The intention is that the

persons that make decisions on such matters have the appropriate knowledge and experience.

- The scheme strategist can be either an individual or a group. The scheme strategist may be separate from or the same persons as the trustees and/or as the scheme funder (or key individuals therein).
- The Government's view is that the requirement that "a person who has a power to appoint and remove trustees" does not include all members in the case of member-nominated trustees. Such a person is usually specified in the scheme deed.

8.7 A large number of respondents asked how the draft regulations could apply to both individuals and corporate entities. The same standards will apply to both individual persons and corporate entities. Schedule 1(2) of the draft regulations allows the Regulator to assess those who fulfil a core function within a corporate entity. It is expected that this will include all relevant Directors, but may not be limited to them. Where a trustee position is filled by a trustee company, it is not expected that everyone within that company will be assessed, only those fulfilling a core role in relation to the specific scheme.

8.8 Some respondents felt that a requirement to complete the Regulator's Trustee Toolkit would not add to the significant experience to which some trustees, such as professional trustees, can refer. The Government agrees and Schedule 1(3)(a) has been amended accordingly. The Government intends that all trustees should have a base level of understanding at the time of authorisation or of the trustee joining the board. We were not persuaded that there is a need for a six month grace period for completing the toolkit, if this is the principle evidence of competence being provided and accordingly have not amended the regulations to provide for this.

Financial Sustainability Requirement

8.9 The second criteria requires the Regulator to be satisfied that a Master Trust scheme is financially sustainable. The policy intent is to minimise the disruption to members' savings which would arise from scheme failure by ensuring that Master Trust schemes are set up with a sound business strategy, underpinned by robust financial planning and a strategy to manage operational risks should they arise. The financial sustainability requirements have been designed to accommodate a range of Master Trust scheme structures and financing arrangements by enabling the Regulator to take account of the specific circumstances of the scheme in its financial assessment. The consultation focussed on asking if there were practical difficulties in meeting the requirements in the draft regulations and what could be done to improve the clarity, coherence and comprehensibility of the information to be provided to the Regulator.

Government Response

- 8.10 The Government has aimed to be proportionate in its financial sustainability requirements, balancing the need for an appropriate level of regulation in this area without stifling the range of appropriate business models and financing arrangements. The draft regulations sought to set the level of detail required in the financial information to allow the Regulator to make an informed decision about a scheme's risks and provisions for its financial security.
- 8.11 There was a general consensus from respondents that requirements for the business plan should be set out in the Regulator's Code. The Government agrees with this, and will be transferring the detailed requirements in relation to the contents of the business plan to the Code, while the draft regulations will set out an appropriate framework in this area. There will be some amendments to the proposed Business Plan requirements in the Code to take account of comments provided to this consultation.
- 8.12 Several respondents set out a strong view that existing financial regulation by the PRA and FCA means that certain schemes should not be required to provide the financial sustainability details specified in the draft regulations. On the other hand, a number of respondents felt that they did not see any particular difficulty with meeting the proposed requirements, subject to some minor issues being addressed. In considering how the regulatory regimes interact it has been helpful that responses set out the various ways in which PRA-regulated insurance companies and FCA-regulated financial service providers can be related to the Master Trust scheme as funders, administrators, promoters or third party providers of services. A scheme may also use insurance products as a means of financing its administration or to provide protection against liability for adverse events, such as those for which the draft regulations require they hold contingency funds.
- 8.13 The introduction of the Master Trust authorisation regime by the 2017 Act is intended to address an existing gap in regulations, whereby members of multi-employer occupational pension schemes that, while regulated by the Regulator, are not subject to similar levels of control as other pension schemes. For example, group personal pensions which are regulated by the FCA. The Government's intention is to ensure that the Regulator has sufficient information and transparency about the particular financial sustainability arrangements for the Master Trust scheme which is applying for authorisation. While evidence that a scheme funder is complying with the existing PRA and FCA regulatory regimes will be strong evidence that any funding arrangements are sound, the Regulator will still need to have sufficient information to understand the specific arrangements for that scheme. The Government has amended some of the references in the financial sustainability requirements (Schedule 2) to clarify that the Regulator will take other regulatory requirements and insurance arrangements into account.

- 8.14 Some respondents felt that Master Trust schemes that rely on participating employers for funds to make up any shortfall in funding to meet the costs required by Section 8(3) of the 2017 Act should not need to demonstrate financial sustainability beyond the employers' commitment. This is an established model. However, it is the Government's view that for money purchase schemes it is not appropriate to rely solely on the employers to meet future wind up costs. This is because a future wind up may be the result of the removal of funding by those employers. In this scenario there is not, as in a DB scheme, the option of using money from the scheme's fund without reducing the funds available to the members (which has the same effect as introducing a new charge on them). This is not an acceptable funding structure for a Master Trust scheme. The draft regulations are aimed at ensuring the Regulator can adequately assess and supervise the financial sustainability of the scheme.
- 8.15 The Regulator's Code will set out how, in practice, the Regulator will wish to see the information presented to it in the Business Plan and accompanying documentation. The Regulator will take into account the objectives of the scheme, its scale and nature and will consider the matters set out in draft Schedule 2 according to relevance and proportionality.
- 8.16 Some of the respondents asked why the effective date of the business plan must not be earlier than six months before application of authorisation. The Regulator may take up to six months to authorise a Master Trust scheme. It could, therefore, take up to a year from the date of the business plan for the scheme to be authorised. The Government's view is that this is the maximum that is acceptable to ensure that the business plan is sufficiently recent and up to date to form the basis for a current assessment. Existing schemes can choose when in the six month application window they will apply, so that the date best coincides with their annual reporting or accounting processes.

Scheme Funder Requirements

- 8.17 The third authorisation criteria set out in the 2017 Act requires that the scheme funder meets certain requirements; firstly that it is a body corporate (section 10(2)) and secondly that its activities relate only to the Master Trust scheme (section 10(3)). An exception to this second requirement is available if the scheme funder's arrangements for financing the scheme meet the financial transparency and disclosure requirements, set out in draft regulation 8.
- 8.18 Draft regulation 9 sets out additional requirements for audits of scheme funders' accounts, including:
- requiring fully audited accounts from all scheme funders regardless of whether exemptions apply to them under the Companies Act 2006, and
 - that auditors include statements as to whether the scheme funder was a going concern and whether it relied on third party funding.

8.19 Scheme funders play a central role in the financing of the scheme. The Regulator needs to be able to assess the arrangements made with the scheme and the financial position of the funder to support the commitments it has made to meet any shortfall of funding. Full transparency is, therefore, required where scheme funders carry out activities that do not relate to the Master Trust scheme. Full audited accounts must also be provided to the Regulator with financial reports and statements that have been independently verified by a third party.

Government Response

8.20 Respondents raised concerns on the information that needs to be provided by a scheme funder that wishes to have an exception from the requirements in section 10(3) of the Act that it only carries out activities relating to the Master Trust (draft regulation 8). In reviewing this information the Government concluded that the decision by the Regulator should be more focussed on whether there is sufficient transparency about the scheme funder's arrangements for funding the scheme rather than the wider requirement that the scheme is financially sustainable. Regulation 8(3)(a) will be amended accordingly. Other minor amendments to the list of information have been made to respond to points raised.

8.21 Concerns were raised from a number of respondents that the Government was placing burdens on auditors which were inconsistent with current standards. The Government is grateful to those who raised this issue and helped suggest a more suitable alternative approach. The draft regulations will be amended to:

- make the necessary amendments to the Companies Act 2006 itself, rather than creating parallel requirements; and
- require the scheme funder to make a declaration in its annual accounts as to whether it is a going concern and whether it relies on third party funding (where these matters are not already dealt with in those accounts) which the auditor will comment on as part of the standard audit process.

8.22 The Government can clarify that where the disapplication under draft regulation 27 applies to Section 10 of the Act, it applies to both requirements. This means that where in a mixed benefits scheme the only scheme funders are the participating employers, those employers do not need to be a body corporate.

Systems and Processes Requirements

- 8.23 Some respondents felt the systems and processes requirements were appropriately balanced, whereas others thought the requirements might be too rigid. The Government has taken these views into account and believes there is sufficient detail in the draft regulations for schemes to be clear on what the Regulator will take into account.
- 8.24 Respondents asked how the Regulator will assess schemes. In particular:
- how will accreditation or other external third party validation be used, including the ICAEW's Master Trust Assurance Framework?
 - Whether a third party 'independent' assessment will be required, either as a mandatory part of the process, or as a non-mandatory way that a scheme could demonstrate compliance with the standard required?
 - How will administration functions outsourced to a third party, such as a specialist administrator, be assessed?

Government Response

- 8.25 The Regulator's Code and accompanying operational guidance will set out how it will assess systems and processes and the evidence that will need to be provided in an application for authorisation. If a Master Trust scheme uses a third party administrator, the evidence may be necessarily different to that of an in house scheme, but the trustees will have to evidence that they meet the same standards set out in the draft regulations and the Code. The Regulator expects that schemes may wish to use third party audits and accreditations as a key part of their evidence and will provide further information on how the relevant frameworks meet the requirements specified in the draft regulations and the Code.
- 8.26 The Government has made a small amendment to draft Schedule 4 paragraph 4(e) to clarify the wording around maintaining members' records relating to decumulation.

Continuity Strategy

- 8.27 The fifth criteria is that the scheme has a continuity strategy, as set out in the draft regulations. There were no significant comments on this element of the draft regulations that required a response.

9. Chapter 4: Controls and Ongoing Monitoring

9.1 Chapter 4 of the consultation paper covered the on-going supervisory regime that will be administered by the Regulator and will ensure that Master Trust schemes continue to meet the authorisation criteria.

Notifications

9.2 The draft regulations explain what Master Trusts must do to protect their members' savings when they do not (or are at risk of not) meeting the authorisation criteria. This includes having to notify the Regulator if the scheme experiences a triggering event, and putting an implementation strategy in place to either resolve the situation or transfer their members to another scheme and wind up. They also provide more detail on the Regulator's powers to intervene should such an event occur.

Government Response

9.3 Some respondents felt that clarification was needed on the timescales for notifications to the Regulator and employers. It was felt that the proposed timescale was too short to allow the trustees or other notifiers time to provide adequate information. The Government has considered these views but has decided not to extend the proposed timescales. These notifications are needed so that the Regulator, employers, and if appropriate, scheme members are aware, and can start considering what if any actions they need to take. Lengthening the timescales could delay the Master Trust scheme taking the necessary actions to resolve the situation, and possibly delay the Regulator being able to intervene.

9.4 The notification requirements will, therefore, be as follows:

- *Triggering events*: notification to the Regulator within 7 days; notification to employers within 14 days beginning with, the earlier of, the date on which the triggering event occurred or when the notifier becomes aware of the triggering event occurring
- *Approved implementation strategy*: this must be made available to employers within seven days from the date trustees are notified it has been approved by the Regulator.
- *Resolving triggering event (Continuity Option 2)*: trustees must notify the Regulator within 14 days from the date on which the triggering event was, in their opinion resolved.

Charges

- 9.5 The provisions on charges cover the information that transferring schemes have to include in their continuity strategy and their implementation strategy, and that receiving schemes have to include in their document. All of these documents have to be provided to the Regulator. The provisions also cover how the restricted charges that will apply during the triggering event period are determined.

Government Response

- 9.6 A change has been made to paragraph 13(2) of Schedule 5 which referred to “the date on which the scheme’s most recent continuity strategy was approved by the Regulator”. Some respondents pointed out that there was no requirement in the Act or the draft regulations for the Regulator to formally “approve” the strategy. To correct this the draft regulations now refer to the continuity strategy submitted by the receiving scheme to the Regulator before the transferring scheme experienced a triggering event.
- 9.7 One respondent suggested that the scheme funder should provide for any shortfall between the administration charges during the triggering event period and increased costs from contractors. The scheme funder already has to cover these costs. The scheme funder is defined as the person who is liable to provide funds to or in respect of the scheme in circumstances where the administration charges from members are not enough to cover the cost of establishing or running the scheme, including during a triggering event period. The financial sustainability requirements are supposed to act as an early warning system to reduce the likelihood of this situation.
- 9.8 A change has been made to “basis” to read “reason for imposing them” (“them” being the charges) in draft regulations 11 and 18, and paragraph 13 of Schedule 5.

Transfers

- 9.9 Schedule 5 of the draft regulations covers the process and requirements for Master Trust schemes that have experienced a triggering event and are pursuing continuity option 1. This includes the process for members to make a choice about where their rights go and the process for trustees to transfer members’ rights where those members do not make their own choice.

Government Response

Interaction with other legislation on bulk transfers

- 9.10 Some respondents asked how Schedule 5 interacts with other legislative requirements for bulk transfers without member consent in the Pension Schemes Act 1993. For example, the required time periods were not aligned and the two routes have different available destinations for members’ funds. Also, one respondent said a buy-out option should be provided in the draft regulations as an alternative to the other legislative provisions.

- 9.11 Under the 1993 Act, the member must no longer be accruing rights and must not have had a crystallisation event. Schedule 5 does not have the same restrictions. The member can use either route, if it is available to them, though for some members only the Schedule 5 route will be available.
- 9.12 In general, under the 1993 Act, a member with money purchase benefits can transfer to an occupational pension scheme, a personal pension or purchase one or more annuities from one or more insurers. The trustees must carry out the member's requirements within 6 months, beginning with the date of the application.
- 9.13 There are differences between the provisions in the Pension Schemes Act 1993 and the Pension Schemes Act 2017. On timing, the 2017 Act gives members 3 months to make an application (the option period) and the trustees 3 months from the end of this option period to make the transfer. Under the 1993 Act, the trustees can take longer as they have 6 months from receiving an application. However, the Government does not want to lengthen the time period in the 2017 Act as it wants the process to be quicker.
- 9.14 The Government recognises that the destination options differ. Under the 1993 Act members can transfer to an occupational pension scheme which is not a Master Trust scheme. Schedule 5 does not allow this. However, as most of the members not able to use the 1993 Act route will be pensioner members this option will not be open to most of them. Therefore, whilst it may not be ideal, the Government has concluded that the difference in available destinations is acceptable.

Timing requirements

- 9.15 There were concerns that the 3 month time limit under Schedule 5 6(2) was too close to the 10 week deadline for employer notifications under draft regulation 5. Respondents were concerned that 3 weeks for schemes to receive information from employers and send out information to members would be too short. The Government agrees and the time period for employers has been shortened to 8 weeks, giving schemes 5 weeks.

Which arrangement members' funds should go into and when

- 9.16 Two respondents asked where members' funds should go in the 8 week period before the provision in draft regulation 10 for funds to go into the default arrangement takes effect. The Government is of the opinion that members' funds should be kept in the default arrangement, and that they should go into that arrangement as promptly as possible. If the member later chooses a different arrangement, the funds would then be moved into that arrangement. The Regulator's DC Code sets an expectation for investment of contributions of three days where there is a daily dealing cycle and 5 days where there is not⁵.

⁵ See paragraph 76: <http://www.thepensionsregulator.gov.uk/codes/code-governance-administration-occupational-dc-trust-based-schemes.aspx#s22016>.

- 9.17 In addition, the provision on members retaining the charge cap when they move schemes has been amended to cover the “applicable scheme” rather than the “receiving scheme”.

Fraud Compensation

- 9.18 The draft regulations addressed the qualifying criteria for claims on the Fraud Compensation Fund (FCF) by Master Trust schemes, which meant that, in practice, it would be very difficult for Master Trust members to benefit. The draft regulations proposed a 30p per member cap on the fraud compensation levy for authorised Master Trust schemes, rather than the existing 75p per member cap, and the removal of NEST’s exclusion.

Government Response

- 9.19 Some respondents raised concerns about the proposed approach to applying the fraud compensation levy to Master Trust schemes. They argued that instead of having a lower cap on the levy for Master Trust schemes, the fraud compensation levy should be a proportion of the levy charged to non-Master Trust schemes. The Government recognises the arguments put forward and has considered this approach in detail. It has concluded that while the relevant primary legislation does allow for a lower cap to be set for a specified population of schemes, it does not permit for a lower levy that is a proportion of the total levy rate. The Government has, therefore, retained the 30p cap for authorised schemes proposed in the draft regulations. This does not preclude a FCF levy rate for Master Trust schemes being set at a level lower than 30p per member in future years.
- 9.20 One respondent suggested that the fraud compensation regime needs a comprehensive review. The Government believes that the Fund is operating broadly as intended, but recognises that the pension landscape has changed considerably since the Fund was created. Therefore, the Government will consider whether there should be a review of the Fund.
- 9.21 The Pension Protection Fund (PPF) Board has published its intention to collect the fraud compensation fund levy at a rate of 25p per member in 2018, the last year that the levy will be collected before the Master Trust Authorisation regime comes into effect. Alongside work to take forward the review and to take forward any subsequent legislative changes needed to enact its findings, the Government will continue to actively consider the case for a lower rate of fraud compensation levy to be collected from members of authorised Master Trust schemes in each year that the PPF Board deems that it is necessary to collect this levy.

10. Next Steps

- 10.1 The Government would like to thank all those people and organisations who have offered their views and advice in response to the consultation. The Government has deliberated the issues raised and where appropriate has made changes to the draft regulations. The main provisions and overall approach, however, have not been amended. The Government intends to lay the draft regulations before Parliament in time to come into force on 1 October 2018. The Pensions Regulator will be consulting on its Code of Practice separately.

List of questions asked

1. The scope of the authorisation regime is intended to ensure that multiple employer, mixed benefit schemes are captured and that the members are protected by existing pension legislation in respect of any defined benefits and by the Master Trust authorisation regime in respect of any money purchase benefits. Do the disapplications undermine this intention?
2. For all the draft regulations in this section is it clear to the schemes concerned whether they are required to be authorised or not?
3. Is it clear who will fulfil the roles subject to the fit and proper assessment in your scheme? Have we captured the important roles?
4. Are there any significant practical barriers to schemes meeting these requirements?
5. Are there any significant practical issues for Master Trust schemes in providing the information required for the business plan?
6. How can we improve the clarity, coherence and comprehensibility of the list of information to be included in the Business Plan across the spectrum of scheme models?
7. Should the detailed requirements in relation to the business plan be set out in Code of practice rather than regulations?
8. What, if any, other lines of business do scheme funders carry out that do not undermine the transparency of their financial arrangement with the scheme?
9. What, if any, disclosures of the matters in regulation 8, scheme funder requirements would be disproportionate to provide and why?
10. What, if any, alternatives could we consider to make the scheme funder's financial arrangements with the Master Trust sufficiently transparent to the regulator for its financial assessment?
11. Are there any circumstances where scheme funders would not be able to comply with the requirement to submit their accounts no later than nine months after the end of the financial year to which they relate and if so why?

Respondents

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| 1. Aegon | Fund |
| 2. AJ Bell | 33. NAMES Group |
| 3. Association of British Insurers | 34. National Employment Savings Trust |
| 4. Association of Member Directed Pension Schemes | 35. Norton Rose Fulbright |
| 5. Association of Pension Lawyers | 36. Now Pensions |
| 6. Atlas | 37. OPITO |
| 7. Aviva | 38. Pension Quality Mark |
| 8. B&CE Peoples Pensions | 39. Pensions and Lifetime Savings Association |
| 9. BAE Systems plc | 40. Pensions Research Accounts Group |
| 10. Baptist Pension Scheme | 41. Plumbing Pensions |
| 11. Barnett Waddingham | 42. Pension Protection Fund |
| 12. Burges Salmon | 43. PTL |
| 13. CAPITA | 44. ReAssure |
| 14. CITB | 45. Rowanmoor |
| 15. Cognent Skills for Science Industries | 46. Royal Society of Wildlife Trusts |
| 16. Creative Benefits Group | 47. RTITB |
| 17. Crow Clark Whitehall | 48. Sackers |
| 18. Dalriada Trustees | 49. Scottish Electrical Charitable Training Trust |
| 19. Deloitte | 50. Semta |
| 20. DWF LLP | 51. ShareAction |
| 21. Electricity Supply Pension Scheme | 52. Society of Pension Professionals |
| 22. Ensignment Retirement Plan | 53. Squire Patton Boggs |
| 23. Ernst & Young LLP | 54. Standard Life |
| 24. Evershed Sutherland | 55. The Cheviot Trust |
| 25. Fidelity | 56. The ITB Pension Funds |
| 26. Industry-Wide Coal Staff Superannuation Scheme | 57. The Workers Pension Trust |
| 27. Lantra | 58. Unilever UK Pension Fund |
| 28. Legal and General | 59. Universities Superannuation Scheme |
| 29. Lewis Workplace Master Trust | 60. University of Oxford |
| 30. Mayer Brown | 61. Welplan Pensions |
| 31. Mercer | 62. Willis Towers Watson |
| 32. Merchant Navy Officers Pensions | |