Department for Work & Pensions

Better workplace pensions: Putting savers' interests first

Presented to Parliament
by the Secretary of State for Work and Pensions
by Command of Her Majesty
October 2014

Cm 8929

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Contents

Foreword by the Minister of State for Pensions

Four million people have been automatically enrolled into workplace pensions since 2012 – a significant step as we expand retirement saving in the UK. Millions more will be enrolled before 2018 as the workplace market is transformed.

We must make sure workplace pensions are well governed, with competent trustees and managers and members' interests at the heart of everything they do. Today's Command Paper confirms that we intend to place minimum governance standards on all money purchase schemes. The Pensions Regulator and the Financial Conduct Authority will continue working with the DWP to make sure members are protected regardless of the type of workplace arrangement they are saving into.

We will also press on with the charges measures we announced in March – protecting members from high and unfair charges. Today we provide more detail on how these protections will be implemented, along with more information on measures to drive greater transparency, so pension savers and those running schemes know exactly what they are paying for.

Alongside today's Command Paper we are publishing draft regulations on the governance and charges measures that, subject to Parliamentary approval and any changes as a result of this consultation will commence from April 2015. The consultation will last for four weeks and we look forward to engaging with our stakeholders during that period to make sure we get this important legislation right.

This Government is putting savers at the heart of the pensions system. Alongside the flexibilities announced in the Budget, these measures will provide savers with the best chance of securing a financially independent retirement.

Executive Summary

By 2018, 8 to 9 million people will start saving or be saving more as a result of automatic enrolment. This places a new responsibility on government, regulators and the financial services industry to ensure that workplace schemes are well run, in members’ interests. The DWP Command Paper, ‘Better Workplace Pensions: Further measures for savers’, published in March, set out a range of measures to meet that responsibility, including a cap on charges in default fund arrangements, a ban on inappropriate charges and proposals to introduce minimum governance standards and improve transparency across workplace defined contribution schemes.

This paper builds on the March Command Paper by publishing the Government’s response to its consultation on minimum governance standards and on two questions on transparency. It also launches a consultation on draft regulations on governance and charges in occupational pension schemes. Subject to Parliamentary approval, the majority of this legislation will come into force from April 2015, alongside Financial Conduct Authority (FCA) rules in relation to workplace personal pension schemes where appropriate.

This paper will help members of workplace pension schemes, and all those involved in delivering them, understand more about how the Government intends to legislate for the Better Workplace Pensions measures. It includes at Annex C draft regulations which reflect the Government’s policy in relation to occupational pension schemes. The central elements of this paper are:

- The Government’s response to the previous consultation to set minimum governance standards in workplace pension schemes via new responsibilities on those running schemes. DWP regulations will, subject to Parliamentary approval, introduce these requirements for occupational pension schemes. Since this is a response we are not seeking comments on the policy but welcome comments on the draft regulations. FCA rules will place requirements on providers of workplace personal pensions to establish Independent Governance Committees (IGCs) to oversee the minimum standards.

- The Government's response to two specific consultation questions with regard to the transparency of costs and charges in workplace schemes and an update on the Government's wider plans to improve transparency.
- An update on the Government's approach to charges in workplace pension schemes, adding detail to the measures announced in the March Command Paper. Since this paper sets out more detail on how the Government's proposal in relation to charges will work, we are seeking comments on this policy and how this is reflected in the draft regulations.
- More detail on how workplace pensions will continue to be overseen by The Pensions Regulator (TPR) and the FCA across occupational pension schemes and workplace personal pension schemes respectively. Again, we are seeking comments on these proposals in relation to occupational pension schemes since this paper contains a more detailed explanation of how the Government proposes this will work. FCA will shortly commence a separate consultation in relation to personal workplace pension schemes.
- An implementation timetable for the Better Workplace Pensions agenda.

The consultation period will last for four weeks, ending on 14 November 2014. Once stakeholder comments and views have been considered, the Government intends to lay regulations in Parliament for its approval early in 2015.

1 Introduction

1. In March the Government published a Command Paper, 'Better Workplace Pensions: Further Measures for Savers' (henceforth referred to in this document as 'the March Command Paper")[1]. This publication included a range of measures designed to protect members of defined contribution workplace pension schemes, critical in an environment where 8 to 9 million people will have been defaulted into workplace saving by 2018. The Office of Fair Trading's 2013 study of the defined contribution workplace pensions market concluded that there were significant weaknesses that prevented competition working in the interest of consumers.

2. The March Command Paper announced measures to address high and unfair charges in qualifying workplace pension schemes and also launched a consultation on the governance of workplace pension schemes, along with two consultation questions on transparency. With regard to occupational pension schemes the consultation sought views on minimum governance standards for trustees and managers. We also consulted on independence requirements for master trusts and the potential benefits of accreditation of scheme administrators.

3. We are grateful to everyone who responded to this consultation. This publication sets out the Government's response to the questions asked on governance and confirms our intention to legislate for minimum governance standards as well as independence standards for master trusts. The new legal requirements for occupational schemes will be introduced via DWP regulations, which will take effect from April 2015, subject to Parliament's approval.

4. The March Command Paper also set out proposals for new governance arrangements for workplace personal pension schemes. The firms that provide these schemes are regulated by the FCA. Between 6 August and 10 October 2014, the FCA conducted a consultation on rules to introduce Independent Governance Committees, also from April 2015.

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/298436/better-workplace-pensions-march-2014.pdf

5. Transparency was a key theme within the proposals on both charges and governance, and the March Command Paper consulted on two specific questions, relating to transparency in defined benefit schemes and unbundled occupational defined contribution schemes respectively. This publication sets out the Government's response to those questions. There is also an update on the Government's wider plans to regulate for greater transparency in workplace pension schemes.

6. The March Command Paper announced a series of measures with regard to charges in workplace defined contribution pension schemes, following a consultation in the Autumn of 2013. These included a cap on charges in default fund arrangements of qualifying schemes, a ban on commission and consultancy charges and a ban on AMDs. This publication describes in more detail how the Government intends to legislate for these measures and how they will apply to trustees, managers and providers, ahead of their planned introduction from April 2015 (and April 2016 for the ban on AMDs and commission and consultancy charges in occupational pension schemes).

7. The policies and principles described in the March Command Paper, and in this document, form the basis of the draft regulations on governance and charges, which the Government is today publishing for consultation. These draft regulations are contained at **Annex C** and information on how to respond to the consultation is contained at **Annex A**. This consultation will last four weeks and will close on 14 November, 2014. **The detailed policy has, however, evolved since the March Command Paper and so we welcome comments on where further policy development has taken place.**

8. The FCA has recently consulted on draft rules to introduce Independence Governance Committees for providers of workplace personal pension schemes. It will also shortly consult on draft rules to introduce the charges measures announced in March and developed in this document. These draft rules will be based on DWP's charges policy as described in both the March Command Paper and this publication.

9. The final chapters of this publication contain proposals on how the compliance regime will operate for occupational schemes and also a summary of the entire package of measures along with an implementation timetable. We seek views on those proposals.

10. The scope of the governance and charges measures is explained in more detail in the section below. That section clarifies certain definitions and terms, and there are further clarifications where required throughout the document. All relevant definitions are listed together in the Glossary to be found at **Annex D**.

The scope of the governance and charges measures covered by the draft regulations

11. As the workplace pensions market has grown over time, along with relevant primary and secondary legislation, terms and definitions have come into common use that don't necessarily have a clearly defined and universally understood meaning. This section sets out how these terms are used in relation to the proposals set out in this paper.

Occupational and trust; contract-based and workplace personal pension

12. All of the measures set out in this paper will apply to occupational schemes. Whilst the majority of these schemes are trust-based, there are some occupational schemes overseen by managers rather than trustees. We refer to "trustees" throughout this paper, and unless stated otherwise

this should be understood to also include managers in the case of the small number of occupational schemes which are not trust based. These measures will also include trust-based stakeholder schemes.

13. The term 'contract-based' schemes is often used to refer to schemes or arrangements offered by insurers where an individual contract is present with each scheme member. In this document we will refer to 'workplace personal pensions' to cover such arrangements.

Defined contribution and money purchase schemes; and hybrid schemes

14. The Office of Fair Trading's market study of 2013, the DWP consultation of October 2013 and the Command Paper of March 2014 all referred to 'defined contribution' schemes. 'Defined contribution' is a commonly understood and widely used term. However, currently its meaning in law is insufficiently precise to make it useful for the purposes of these draft regulations. We intend that the governance measures described in Chapter 2 should apply to occupational pension schemes which are money purchase schemes and in certain respects, to schemes which are not money purchase schemes but which provide some money purchase benefits (see paragraph 16 below). The definition of "money purchase scheme" and "money purchase benefits" are in section 181 of the Pensions Act 1993, as amended by section 29 of the Pensions Act 2011. Trustees and providers will need to consider this legislation to determine whether they are within scope of these measures.

15. Some respondents to the March Command Paper and the earlier Call for Evidence on quality standards reported concerns that where schemes have both defined benefit and money purchase benefits there is a tendency for a disproportionate amount of governance time to be dedicated to the defined benefits section at the expense of the money purchase benefits section. Examples of such arrangements include defined benefit (DB) schemes where the DB section is closed to new members who instead accrue money purchase benefits, and DB schemes where members accrue money purchase benefits until they have completed a qualifying period of service and move on to DB arrangements ("nursery schemes").

16. We intend that, in the case of these "hybrid" schemes the governance provisions contained in this paper concerning governance of the default arrangement, the processing of core financial transactions, the assessment of charges and transaction costs, and the requirement that a scheme must not restrict choice of service providers (described in more detail in chapter 2) would only apply in relation to the provision of money purchase benefits. However, the other governance measures, because of their nature, have to apply to the scheme as a whole such as the requirement for a chair, and the independence requirements for master trusts.

The scope of the governance measures

17. There are some schemes that we propose should not be covered by the governance arrangements outlined in Chapter 2:

- small self-administered schemes, which have fewer than 12 members and where all of these members are trustees, and either the rules of the scheme provide that all decisions are made only by the trustees who are members of the scheme and by unanimous agreement; or the scheme has an independent trustee and that trustee is registered on The Pensions Regulator's register of trustees. As all the members are the trustees, they are effectively governing their own savings and we therefore do not think that the same level of governance regulation is required.

- executive pension schemes, where a company is both the only employer in relation to the scheme and the sole trustee, and the members of the scheme are either current or former directors of that company and include at least one-third of the current directors. Again, we would expect members of these schemes to already have a high level of engagement so additional governance requirements are not necessary.
- public service pension schemes, which are covered by the Public Service Pensions Act 2013 (which amends the Pensions Act 2004). Specific governance requirements for these schemes are already set out in legislation.
- schemes which are not covered by the requirement for an annual report and other information, as set out in the Disclosure Regulations[2]. These include occupational schemes which are not tax registered, have only one member, only provide death benefits, are not established in the UK and have no trustee or manager resident in the UK.
- schemes which provide no money purchase benefits other than benefits which are attributable to the payment of Additional Voluntary Contributions (AVCs). In these cases members' money purchase benefits will be in addition to other pension assets where the member bears little or no risk. We therefore think that an additional layer of governance in relation to these money purchase benefits is not needed.

The scope of the charges measures

18. The March Command Paper announced a range of measures relating to charges in defined contribution schemes used as qualifying schemes for automatic enrolment, including a cap on charges in default funds. The charge cap is primarily directed at protecting members who have made no active choices about their investments. These measures will apply to money purchase benefits within these qualifying schemes. In common with the scope of the governance measures this includes money purchase benefits provided in non-money purchase qualifying schemes.

19. In common with the governance requirements, it is our intention to exclude small self-administered occupational schemes and executive pension schemes from the charges measures, according to the definition at paragraph 17.

20. Some schemes that are not subject to the governance measures may still be subject to the charges measures, where they are used as a qualifying scheme and provide money purchase benefits. These include public service pension schemes, schemes which are not covered by the requirement for an annual report as set out in the Disclosure Regulations, and schemes where the only money purchase benefits are attributable to AVCs. This is because members of qualifying schemes should be protected from high and unfair charges regardless of the scheme's disclosure requirements, or the other benefits which are available to scheme members.

21. It is also our intention that stakeholder pension schemes should be subject to all the charges measures when these are used as qualifying schemes. This is similarly in line with the principle of protecting members of schemes used for automatic enrolment from high and unfair charges.

22. This is achieved in regulation 11 of our draft regulations by inserting a new regulation 14D into the Stakeholder Regulations (Stakeholder Pension Schemes Regulations 2000 (SI 2000/1403)). Where an occupational stakeholder scheme is being used as a qualifying scheme, and one or more of the funds in the stakeholder scheme meets the definition of the default arrangement set out in these regulations, we propose that the relevant stakeholder regulations on charges (regulations 14 to 14C) should not apply and instead the default arrangement should comply

[2] The Occupational and Personal Pension schemes (Disclosure of Information) Regulations 2013 (SI 2013/2734).

with the charge cap. This is set out in regulation 14D(3). Similarly, in the case where a stakeholder personal pension scheme is being used as a qualifying scheme, and one or more of the funds in the stakeholder scheme meets the definition of the default arrangement set out in the forthcoming FCA draft rules, then the stakeholder regulations will not apply, and proposed FCA rules instead apply. This is set out in regulation 14D(2).

23. Normally where a stakeholder scheme breaches the stakeholder charge cap (1.5% for the first 10 years, reducing to 1% subsequently), it is subject to the stakeholder pension compliance provisions, under which the scheme ceases to be a stakeholder scheme and is removed from the register of stakeholder schemes. We propose that, where the default arrangement of a stakeholder scheme being used as a qualifying scheme breaches the 0.75% cap, TPR will take action against occupational schemes using the compliance measures set out in part 4 of our regulations, and FCA will take action against workplace personal pension schemes using their powers. In these circumstances, the scheme will not cease to be a stakeholder scheme or be removed from the register. Even if a stakeholder scheme is unable to comply with the 0.75% charge cap for default arrangement qualifying schemes we do not think that should mean that it is unsuitable as a stakeholder scheme in other circumstances.

24. The default fund charge cap will not apply to money purchase schemes that contain third party promises (defined in the Pension Schemes Bill 2014). This is because, as the Government recognised in its June 2014 publication 'Reshaping Workplace Pensions for Future Generations', schemes providing promises or guarantees that benefit members may be more complex and involve higher costs than arrangements without any such guarantee or promise. The bans on AMDs, commission and consultancy charges will still apply to such schemes.

25. Although the term 'money purchase' is commonly understood to refer to schemes which offer no promise or guarantee to the member, schemes where the promise or guarantee is provided by a third party are money purchase, because the funding liability falls on the third party not the scheme. As we do not wish to apply the charge cap where there is a promise, we therefore do not propose to apply the charge cap to money purchase benefits where there is a third party promise.

26. The charge cap is primarily directed at protecting members who have made no active choices and who do not have the advantage of any promise. The Government is committed to protecting members of all workplace pension schemes, requiring good governance and fair charges. It will therefore keep the scope of these provisions under review, in order to ensure that scheme members are protected, as intended.

Questions for consultation

Q1. a) Does the definition of "relevant scheme" (regulation 2) meet the policy intention of protecting members of schemes used for automatic enrolment from high and unfair charges?

b) Does the definition of "relevant scheme" at (regulation 13) meet the policy intention of ensuring that workplace schemes are well governed in members' interests?

Q2. Do the draft regulations (regulations 4(3) and 4(4)) meet the policy intention of excluding from the charge cap members of qualifying schemes who have the advantage of a third party promise?

Minimum governance standards in workplace pension schemes

2

Summary

- New quality standards will apply across all money purchase workplace pension schemes, and in relation to the money purchase elements of non-money purchase schemes. These are designed to ensure that people running schemes understand the key components of scheme quality and have members' interests as their priority.
- For workplace personal pension schemes, firms will be required to set up and maintain Independent Governance Committees (IGCs) to provide oversight on behalf of scheme members. Between 6 August 2014 and 10 October 2014, the Financial Conduct Authority (FCA) launched a consultation on new rules to introduce IGCs from April 2015.
- In occupational schemes, governance requirements will be introduced by secondary legislation, which will also give enforcement powers to The Pensions Regulator (TPR). Under these regulations, trustees will be required to design default arrangements in members' interests and keep them under regular review; ensure that core financial transactions are processed promptly and accurately, assess the value of costs and charges borne by scheme members and have a chair of trustees who will be responsible for signing off an annual statement on how the governance requirements have been met.
- Occupational schemes will also be prevented from requiring trustees to use particular service providers and this requirement will override any conflicting provisions of the scheme.
- There will be additional requirements to strengthen the independent oversight of master trust arrangements (by master trust we mean multi-employer occupational schemes, where at least some of the employers are non-associated).
- These schemes must have a minimum of three trustees, the majority of whom – including the chair – must be independent of any company which provides advisory, administration, investment, or other services to the master trust.

- These independent trustees (or trustee directors where the trustee board is a corporate entity) must be subject to limited term appointments of up to five years with a ten year cumulative maximum (with modifications to this requirement for independent professional trustee firms); the appointment process for recruiting independent trustees must be open and transparent; and trustee boards must encourage members to make their views known on matters relating to the scheme.

Introduction

1. Consultation, research and analysis by the DWP, Office of Fair Trading (OFT), the FCA and TPR has revealed several areas where standards need to be raised, particularly in an environment where millions of people are defaulted into workplace pension arrangements. In July 2013 we ran a call for evidence on quality standards[3] – which covered governance of schemes and investments, administration and scale. The OFT in their market study into workplace pensions[4] recognised the particular importance of good governance in substituting for a lack of employer and employee scrutiny of the wider value for money delivered by pension schemes. With this in mind they recommended that the Government should embed minimum governance standards across all defined contribution pension schemes.

2. Both the OFT's market study and the responses to the call for evidence raised concerns about the quality of the governance delivered in some occupational schemes, particularly smaller single-employer schemes. They also raised concerns about the independence and effectiveness of governance in some models of master trust, particularly those using a vertically integrated provider[5].

3. The March Command Paper set out a range of measures to improve how both occupational and workplace personal pension schemes are governed. For workplace personal pension schemes we set out proposals for new governance arrangements to ensure independent oversight of these schemes in members' interests. These built on an agreement between the Association of British Insurers (ABI) and OFT to establish IGCs on a regular footing. Under these proposals IGCs would assess and report on the value for money of workplace personal pension schemes, and, where necessary raise concerns with the provider of the scheme or the FCA. Providers of workplace personal pension schemes are regulated by the FCA and so they have recently undertaken a consultation on rules to introduce IGCs and how they will work in practice.

4. For occupational schemes, we want trustees to consider and report against key features that determine the value for money delivered by their scheme. The March Command Paper contained a consultation on how to bring that about – setting out minimum governance standards for all schemes to meet. The consultation also sought views on a set of independence requirements for master trusts.

[3] Quality Standards in Workplace Defined Contribution Pension Schemes – Call for Evidence – DWP July 2013.
[4] Office of Fair Trading (OFT), 2013, Defined Contribution workplace pension market study OFT 1505.
[5] A vertically integrated provider is responsible for both the asset management and administration of a scheme/schemes.

5. The majority of respondents to the consultation expressed their support for the proposals on occupational scheme governance, saying that they were a positive change intended to drive the right behaviours. Some respondents thought that some of the standards were too prescriptive and might be better placed in guidance, and suggested alternative arrangements on questions such as the required number of trustees in master trusts. We have assessed these responses and in some areas made changes to our original proposals.

6. In designing these standards we have sought to strike the right balance between regulating on key areas whilst not being overly prescriptive. We recognise that there is a great diversity in scheme structure and what works well for one scheme might not work well for another, so we have sought to avoid prescriptive legislation that might favour one model over another.

7. The Department of Business, Innovation and Skills and DWP tasked the Law Commission to investigate how fiduciary duties apply to investment intermediaries, and whether these duties work in the interests of the ultimate beneficiaries. Since we published the March Command Paper, the Law Commission has published its final report[6] on this issue. We very much welcome this report, in particular the Law Commission's clear guidance that fiduciaries such as pension scheme trustees have a duty to consider factors which are, or may be, financially material to the performance of an investment, including over the long term. The Law Commission's report also signals its support for the Government's reforms to strengthen the governance of workplace pension schemes, and made helpful suggestions about the work going forward. The Government will respond to the recommendations shortly as part of a wider progress report on the implementation of the Kay Review.

8. In the March Command Paper we sought views in three areas in particular; occupational scheme governance, independence requirements for master trusts and accreditation of administrators. In this chapter we give brief summaries of what respondents said and set out our final proposals to improve the governance of occupational schemes.

The March Command Paper: our proposals for occupational scheme governance

9. In the March Command Paper, we proposed that trustees should be required in legislation to:

- Ensure their default arrangement strategy is designed in members' interests, and that the strategy and net performance of underlying funds are regularly reviewed;
- Ensure that core scheme financial transactions are processed promptly and accurately;
- Assess the value delivered by charges levied on members in their schemes;
- Assess the value delivered by transaction costs within the scheme;
- Have a chair of trustees with responsibility for reporting on how these standards have been met by way of an annual statement ('the Chair's Statement'); and
- Have, or have access to, all of the knowledge and competencies necessary to properly run the scheme.

[6] Fiduciary Duties of Investment Intermediaries – Law Com No 350 – June 2014.

10. We proposed that trust deeds and rules must not require trustees to use particular investment or administration providers or to make particular investments. We also proposed that the chair must produce an annual report covering how the above quality standards have been met.

11. We sought views on:

- the set of quality standards for occupational schemes outlined above, and whether these were the right standards to be set in regulations;
- whether occupational schemes should be required to have a chair of trustees; and
- whether the proposed reporting requirements would help drive compliance with the standards and regulation of these.

Default arrangements – strategy and reviews

12. We estimate around 80 per cent of members of workplace pension schemes are currently invested in default arrangements and we expect this figure increase as more people are automatically enrolled into a pension scheme.

13. Trustees have a fiduciary duty to all members of their scheme, regardless of whether or not they have made an active choice about their investments. However, we think the lack of active choice that most members of the default arrangement will have made, combined with the number of members we expect to use the default, means that trustees should pay particular attention to the design of their default arrangement and the performance of the funds used to deliver it.

14. Chapter 4 sets out what funds or arrangements will be caught by the definition of default arrangements within a qualifying scheme for the purposes of the charge cap. We propose to apply the same broad definition of default arrangement for the purposes of the governance measures relating to managing default arrangements.

15. However, unlike the charges measures, the governance requirements apply to all workplace money purchase schemes, not just those being used as qualifying schemes. Where a scheme is not being used as a qualifying scheme it will not be subject to the charge cap.

Designing the default arrangement strategy

16. Most respondents to our consultation agreed that the default arrangement should receive particular attention from trustees.

"We have long maintained that ensuring the default fund is fit for purpose is imperative as 98% – 100% of members will be auto enrolled into default funds. The structure of these funds will have a significant bearing on members' future retirement income."

Now Pensions

17. Some respondents did however question whether new requirements about the design and review of the default were needed, given trustees' existing obligations under the Investment Regulations[7] and their general fiduciary duties to members.

[7] The Occupational Pension Schemes (Investment) Regulations 2005. SI 2005/3378.

18. The Investment Regulations require trustees of schemes with more than 100 members to ensure that the scheme's investments are invested in the best interest of members, and to prepare and review a Statement of Investment Principles (SIP) setting out the trustees' approach to investments across the scheme as a whole.

19. We do not propose to amend the provisions about SIPs in the Investment Regulations. We do however think that a new specific requirement about the design of default arrangements has value, and that this should be applied to schemes of all sizes. The extra focus on the default arrangement is consistent with the existing approach in the Investment Regulations, but will ensure that particular attention is paid to the design and review of the default arrangement.

20. While trustees' fiduciary duties provide an important protection of members' interests, the application of these duties can be unclear (as set out in the Law Commission's report on fiduciary duties). We think that a requirement to ensure that default arrangements are designed in members' interests, and that this is documented, will provide greater clarity about trustees' particular responsibilities regarding default arrangements.

21. At Budget 2014[8], the Government announced a fundamental reform to the way people can access their pension savings, by abolishing the effective requirement to buy an annuity, and announcing plans to give savers greater freedom over how they access their pension savings. A number of respondents commented on the impact this will have on designing default arrangements. In particular, they said that lack of certainty about how savers will access their pension savings will make it more challenging to design appropriate default strategies.

"The design and governance of default funds can no longer always take the position that individuals will secure an annuity or indeed that they would take all savings at a selected retirement age."
Standard Life

22. We recognise that the new flexibilities will bring new challenges for those designing default arrangements. However, we do not think this affects the importance of ensuring that defaults are designed in members' interests. Our regulations will not be prescriptive about what the aims and objectives of schemes' default arrangements should be, but will focus instead on ensuring that trustees have fully considered these, and the needs of their scheme's membership.

23. Other respondents also asked about the interaction between the new default arrangement requirements and the guidance on offering a default option published by DWP in 2011[9]. We continue to think the guidance is relevant to anyone offering a scheme that will be used for automatic enrolment. We will however consider whether any further guidance is needed to help trustees fulfil their new responsibilities, and how this could be best delivered.

24. **We therefore intend to regulate so that trustees must ensure that default arrangements are designed in members' interests. The trustees must prepare a statement including a description of the default arrangement or arrangements offered by the scheme, with a clear statement of aims, objectives and policies in relation to investments and an explanation of how these are in the best interests of the scheme's membership. This statement must be included in the Chair's Statement.**

[8] https://www.gov.uk/government/publications/budget-2014-documents
[9] Guidance for offering a default option for defined contribution automatic enrolment pension schemes – DWP May 2011.

25. We do not intend to set out in regulations the factors that trustees should take into consideration when designing their default arrangement strategy, but would expect these to include the level of costs and the risk profile that are appropriate for the scheme's membership. These should be considered in light of the overall objective of the default arrangement strategy, which may vary depending on the needs and demographics of the scheme's membership.

26. There is already practical guidance for trustees about designing and reviewing their default strategy and other investment options in TPR guidance on governance and administration[10]. We will work with TPR to consider whether this, or DWP's guidance on offering a default option, need updating in light of the new regulatory requirements, but would suggest trustees look at the content of the code for more guidance on their role in selecting investment options.

Reviewing the default strategy and performance of investment funds

27. As well as clearly setting out the aims, objective and structure of the default arrangement strategy, we proposed that trustees should regularly review the strategy and the performance of the underlying investment funds. We proposed two aspects to this review:

- Reviewing the strategy itself to see whether it remains appropriate for the scheme's membership; and
- Reviewing the performance of the underlying investment funds to see whether they are meeting the aims of the strategy.

28. Of those respondents who commented on reviewing the default strategy, most agreed about the importance of review.

> "It is [also] critical that default strategies are kept under review over time; performance is monitored and the position reviewed to account for the changing needs of members over time, changing investment opportunities, and in light of future legislative regulatory and environmental developments."
>
> **Institute and Faculty of Actuaries**

29. While we received some questions about what a default review should entail and how often it should take place – and how much of this detail should be put in regulations – few respondents challenged the importance of reviewing the default. **We intend to regulate so that trustees must review their default strategy, and the net performance of the underlying investment funds. The annual Chair's Statement must include a report on any review undertaken during the year and any changes resulting from that review or, if there was no review during the year, it must indicate when the last review took place.**

30. In practice, we recognise that many schemes will already receive regular advice on the performance of their funds on an ongoing basis. However, we want to require a minimum standard for the frequency of review in regulations, to ensure that all schemes – and particularly those that may not regularly review their default arrangement strategy and fund performance at the moment – ensure that the design and performance of the default arrangement remain appropriate for their membership.

[10] http://www.thepensionsregulator.gov.uk/codes/code-governance-administration-occupational-dc-trust-based-schemes.aspx

31. In order to review whether the default strategy remains suitable for the scheme's membership, trustees will need an understanding of the demographics of the scheme's membership. We also then expect trustees will take into account similar features to those when first designing the strategy – for example, the demographics and needs of the scheme's membership and the costs and affordability of the strategy.

32. Trustees should also consider any wider changes in the pension landscape and whether these affect the appropriateness of the default strategy. For example, many trustees will be considering their default strategy design in light of the pensions flexibility changes announced in the Budget 2014. Innovations in the pensions market that affect the value for money of their default strategy may also be relevant – what looked like good value when the strategy was first selected may not do over time.

33. In reviewing the characteristics and net performance of the funds underlying the default strategy we expect trustees to focus on whether the returns delivered by the funds have delivered the aims and objectives of the strategy. The relevant benchmarks or measures will vary depending on the aims and objectives of the default strategy, but would typically include consideration of the level of investment returns and the volatility of returns. Trustees should also consider relevant changes in the wider investment landscape and how these may have impacted on their investment returns.

34. As with the design of the default strategy, our regulations will not specify the features that trustees should take into account when reviewing their default strategy or funds. We do however think it important that trustees consider the performance of the funds used in their default arrangement net of charges, and intend to specify this in regulations.

35. **We therefore intend to say in regulations that trustees must carry out both the review of their default arrangement strategy, and of the performance of the underlying funds:**

    - **at least every three years;**
    - **without delay after any significant change in investment policy;**
    - **without delay after any significant change in the demographics of scheme membership.**

    Trustees will, in particular, be required to review the extent to which the net return on investments relating to the default arrangements is consistent with the aims and objectives the trustees have in respect of the default arrangement.

36. The first two criteria align with the frequency with which trustees are required to review their Statement of Investment Principles. While these two exercises are separate, we recognise their commonalities. By adopting the same frequency of review we hope this will allow trustees to choose to carry out the exercises at the same time, where this might be more efficient.

Core scheme financial transactions

37. In the March Command Paper we proposed that trustees should ensure that core scheme financial transactions are processed promptly and accurately. We also reflected that responses to our earlier call for evidence on minimum quality standards had warned against putting specific administrative stages and timings into legislation.

38. Consultation responses agreed that ensuring accurate administration and prompt processing of transactions is a central part of running a scheme, and that trustees have an important role in ensuring financial transactions are processed promptly and accurately.

"[We] recognise the importance of accurate administration in ensuring that an individual receives the pension pot due to them. We believe strengthening trustees' legislative responsibilities for ensuring and reporting on how core scheme financial transactions are processed promptly and accurately should ensure accurate administration"

Association of British Insurers

39. However, some respondents queried how the new requirement might work in practice. In particular, some respondents stated that trustees are already responsible for scheme administration and questioned how the new proposed requirement would add to this. Others highlighted the role that external parties play in administering a pension scheme, and questioned the division of responsibility between trustees and their administrators.

"Ultimately trustees are reliant on those charged with the administration of the schemes, and have to rely on a combination of self reporting by the administrators, third party audits and their own inspections/questioning to gain comfort that the scheme is being administered correctly."

Independent Trustee Services Ltd

40. We recognise that trustees rely on other parties to administer their pension scheme and do not intend to place new responsibilities on trustees that require them to undertake transactions themselves. However, we do not think this detracts from trustees' responsibility to ensure that administration is undertaken promptly and accurately. While trustees may be reliant on information from third parties about how transactions have been processed, managing third party contracts and ensuring that they deliver services in members' interests is an important part of the trustee's role.

41. With regard to existing responsibilities, as part of their role in governing a scheme on behalf of members, trustees should already satisfy themselves that all aspects of the scheme's administration are undertaken promptly and accurately. There are also specific requirements in regulations about trustees' responsibilities with regards to record keeping[11], and TPR guidance to support trustees in ensuring good standards of record keeping within their scheme[12].

42. There are not currently any specific requirements about trustees' responsibilities regarding transactions undertaken once a member's funds are within the scheme. These are essential features of running a money purchase scheme and the speed and accuracy with which these transactions are carried out will have a direct impact on member outcomes. Examples of these types of transactions include:

- the investment of a member's contributions into their selected or default arrangements;
- switches from one fund to another within the same scheme – including, for example the implementation of life-styling options;
- redirections of future contributions; and
- the movement of all or part of the assets comprising an individual's pension savings into and out of the scheme – for example, when a member moves employment and transfers their pot with them.

[11] Occupational Pension Schemes (Scheme Administration) Regulations 1996 (SI 1996/1715);
• The Occupational Pension Schemes (Disclosure of Information) Regulations 1996 (SI 1996/1655);
• The Personal Pension Schemes (Disclosure of Information) Regulations 1987 (SI 1987/1110);
• The Occupational Pension Schemes (Internal Controls) Regulations 2005 (SI 2005/3379).

[12] http://www.thepensionsregulator.gov.uk/guidance/guidance-record-keeping.aspx

43. **We therefore intend to regulate so that trustees must ensure that core scheme financial transactions (including the types of transactions listed above) are processed promptly and accurately**. We do not intend for regulations to contain an exhaustive list of relevant transactions, or to specify how quickly each transaction should be executed. We instead want to leave flexibility for trustees to satisfy themselves that they have sufficient intelligence about how the scheme is being administered to know whether core transactions are being executed promptly and accurately, and that they are taking action where this is not the case.

44. **The Chair's Statement must explain how trustees have assured themselves that core scheme financial transactions are processed promptly and accurately**. We recognise that these transactions will be undertaken by the scheme's administrator rather than by the trustees themselves. Trustees will therefore need to consider what information they need from their administrators about the standards of administration being delivered to satisfy themselves that their scheme meets this requirement.

Assessing charges and transaction costs

45. The level of charges that a member of a money purchase scheme pays will have a significant impact on their pension savings. Knowing the charges their members pay and whether these represent value for money is therefore central to trustees' ability to act in members' interests.

46. In the March Command Paper we proposed that trustees should have to assess the levels of charges and costs borne by scheme members. By "costs" we mean transaction costs incurred through investment of pension assets.

47. Responses to the consultation agreed the importance of trustees regularly reviewing charges and costs. They also stressed the importance of considering the value delivered by charges and costs, rather than considering these in isolation.

"Trustees should assess costs and charges to satisfy themselves that they represent value for money for members, and ensure they are properly disclosed".
Institute and Faculty of Actuaries

48. We agree that trustees should consider the value delivered by charges and costs. **We therefore intend to regulate so that trustees must calculate the charges and transaction costs borne by members and assess the extent to which they provide good value for members. This must also be reported in the annual Chair's Statement, which should contain:**

- **the charge levels and the trustee's assessment of the value delivered by these (by charges, we mean all member-borne deductions excluding transaction costs);**
- **the levels of transaction costs – where trustees have been able to access this information – and their assessment of the value delivered by these; and**
- **details of any information about transaction costs which trustees have been unable to obtain and an explanation of the steps being taken to obtain that information in future.**

49. **The Chair's Statement must report the level of charges and transaction costs in the default arrangement and the range of charges and costs in other funds.**

50. Chapter 3 gives more information on the Government's plans for improving transparency and disclosure. The rest of this section sets out how we expect trustees to meet the requirements.

Assessing charges

51. The charge measures detailed in Chapter 4 mean that trustees will have to understand the types and levels of member borne deductions (MBD) that members of their default arrangement bear, and be able to report on these. Further information about how trustees should calculate their MBD is contained in Chapter 4. How the charges figure is worked out will depend on the structure of the scheme, and the types of charges. For example, an 'unbundled' scheme that buys services from a number of different providers (potentially also including in-house investment or administration services) might need to aggregate the various charges and then break them down to a single member level charge.

52. It is likely that there will also be different levels of charges for different funds within the same scheme. Trustees will be expected to scrutinise the charges experienced by members of all funds, not just those who are protected by the default arrangement charge cap.

53. **The Chair's Statement must report the types and level of charges being paid by members of their default arrangement – or arrangements where there are multiple defaults – and the range of the levels of charges in other funds.**

54. We will expect trustees to report on:

    - Member-borne deductions as a percentage of funds under management (FUM);
    - A percentage contribution charge on regular premiums paid into the scheme, where such a charge is present; and
    - Any flat fee – often termed a policy fee – (£ per annum, per member), where such a charge is present.

55. **As well as the level of these charges, trustees will need to report their assessment of the extent to which the charges represent good value**. We do not intend to be prescriptive in regulations about how trustees should carry out this assessment. We do however expect this to go beyond simply considering whether the default arrangement's charges are within the charge cap, and expect trustees to compare the level of their scheme's charges with the benefits delivered to members.

56. These benefits will include financial features such as investment returns, and other benefits such as the quality of customer services and communications. Trustees will ascribe different levels of importance to these benefits depending on the needs of their membership. TPR's regulatory guidance for DC schemes[13] already includes guidance on assessing value for money which might be built on for this purpose.

57. Trustees may also like to compare their charges and service levels against those obtained by trustees in other schemes. NEST already represents one benchmark in the market, and IGCs' reports on workplace personal pension schemes will provide others. There is also published research that trustees may like to look at such as the pensions Landscape and Charges Survey published by DWP[14]. The next phase of the government's work on transparency (see Chapter 3) will also mean that schemes across the market will publish their charging levels for the first time, enabling greater comparability.

[13] http://www.thepensionsregulator.gov.uk/professionals/value-for-money-in-your-clients-dc-schemes.aspx
[14] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/281128/rr859-defined-contribution-pension-schemes.pdf

Assessing transaction costs

58. There is increasing recognition of the importance of the transaction costs incurred in buying selling, lending and borrowing of investments, and the impact these can have on an individual's savings. As well as knowing the level of the charges paid by members and assessing the value of these, **we therefore want trustees to know the types and levels of transaction costs that are incurred by the different investments their schemes uses, and assess the value these deliver to members**.

59. We do not intend to set out a list of transaction costs in regulations that trustees must assess, but examples of the costs we expect trustees to consider include:

    - brokerage commission and fees
    - bid-offer spreads
    - transaction taxes (including stamp duty)
    - soft commission services included in brokerage fees, e.g. research costs
    - foreign exchange commissions and
    - fees relating to stock lending or stock borrowing.

60. As with information on charges, the ease with which schemes will be able to obtain information about their transaction costs will vary depending on the nature of their investment arrangements. We recognise that information on transaction costs is not routinely requested by all schemes at the moment and that trustees may not be able to access all of this information in the first period of reporting.

61. **Therefore, rather than be prescriptive in legislation about which costs must be considered and reported at this stage, we intend for regulations to require trustees to report on those transaction costs about which they are able to get information. Where trustees, despite their best efforts, have not been able to obtain this information, they will be required to explain this in the Chair's statement along with an explanation about how they will obtain fuller information in the future.**

62. **As well as the level of transaction costs, trustees will need to report their assessment of the value which these costs represent**. We do not intend to be prescriptive in regulations about how trustees should carry out this assessment.

63. We would generally expect trustees to consider the level and nature of the costs incurred and whether these seem appropriate for the particular investment funds. This assessment will vary depending on factors such as the purpose of the funds under question and the wider trading environment. For example, high levels of research costs might be appropriate for a high-return seeking developing markets fund, but inappropriate in a passive tracker fund; or a shock in the foreign exchange market might mean that higher than usual levels of trading in a foreign exchange fund are appropriate for the period following this shock.

64. Trustees may also wish to compare their transaction costs against those in other schemes. We recognise that the ability to do this may be limited in the first phase of reporting, but think that the introduction of the new reporting requirements and the next phase of work on transparency as described in Chapter 3 will make this a more common approach in the future.

Chair of trustees

65. We proposed in the March Command Paper that trustees should be required to have a chair of trustees, who would have particular responsibility for the annual statement about how the scheme has met the minimum governance standards. This was with the intention that having a named individual with responsibility for reporting on how the standards have been met would help ensure compliance.

66. Of those who responded to this question, most felt that the majority of schemes will already have a chair. Some of these respondents thought it might be overly prescriptive to include this requirement in regulations, while others were supportive on the grounds that a chair is necessary for the effective running of a scheme.

"The vast majority of such schemes already have a person fulfilling this role, but we would have no issue with formalising this as a requirement"
Association of Consulting Actuaries

67. A small number of respondents also stressed the importance of trustees' joint and several responsibilities to govern the scheme and meet the minimum governance standards, and expressed concern that the role of the chair should not interfere with this.

"It is suggested that the Chair must produce an annual report. We suggest that the trustees should collectively have this responsibility."
Financial Reporting Council

68. Having considered these responses, **we intend to legislate so that schemes must have a Chair of trustees**. We recognise that trustees have joint and several responsibilities to meet the legal requirements of running a scheme and do not want to interfere with this approach. **So we intend that the only regulatory responsibility the Chair will be required to have, above and beyond the scheme's other trustees – is in signing off the Chair's Statement.**

69. Where schemes do not already have a Chair, we recognise that they may not be able to appoint a new Chair from the day the regulations come into effect. **We therefore intend to include a three month transitional period for existing schemes to appoint a Chair. We will also provide for a similar three months' period of grace if a Chair resigns, dies or is removed**. We do not intend to set out detailed legislative requirements in regulations for how the Chair should be appointed, in particular because we would not want to override existing scheme rules. We will however require trustees to register the name of the chair with TPR.

70. **We also propose to add the name of the chair to the list of registrable information that must be provided to The Pensions Regulator (TPR)** for those schemes that are required to register with them. We also propose that schemes should to be required to update this information both when the chair is first appointed and where the chair changes.

Trustee competence

71. As well as being aligned with members' interests it is important that trustees have the skills and experience to act in members' interests. In the March Command Paper we proposed that there should be a requirement to the effect that trustees should have, or have access to, all of the knowledge and competencies necessary to properly run the scheme.

72. Many respondents questioned how much this adds to existing requirements, in particular those contained in the Pensions Act 2004[15] and TPR's code of practice covering Trustee Knowledge and Understanding.

73. We continue to think it essential that trustees have the skills and experience to act in members' interests but accept that there are already existing requirements to this effect. **We therefore do not intend to introduce the requirement proposed in the March Command Paper, but do intend to require the Chair's Statement to include an assessment of how the combined knowledge and understanding of the trustees, together with the advice which is available to them, enables them to properly exercise their functions as trustees**. This should include setting out how the trustees meet their knowledge and understanding requirements (already set out in legislation and TPRs' Code of Practice 7) as well as a broader assessment of the knowledge and competencies across the board as a whole, including access to professional advice.

Trustees' freedom to choose investments and providers

74. We proposed in the March Command Paper that trust deeds and rules should not be allowed to tie trustees to certain service providers or investments. This was intended to ensure that trustees have the freedom to change service providers or investments where they deem this to be in members' interests.

75. Respondents who commented on this proposal were generally in favour of this approach, and stressed the importance of trustees not being constrained in fulfilling their fiduciary duties to members.

"We agree that the trust deeds of all schemes should enable the trustees to exercise unfettered powers to appoint and dismiss advisers and service providers."

Friends Life

76. However, having looked into this further we are concerned about potential unintended consequences of preventing trust deeds and rules from specifying parameters about the investments trustees can make. In particular, we do not want to prevent employers from setting parameters about the sorts of investments they think appropriate for their organisation on ethical grounds. For example, this could be particularly relevant for some health organisations or charities.

77. While we think it can be appropriate for trust deeds and rules to set requirements about the types of investments trustees may make, we do not think there are situations where it is appropriate for trustees to be required to use particular service providers.

78. **We therefore intend to require in legislation that a scheme must not restrict the choice of who provides administrative, fund management, advisory or other services to the scheme. Where schemes have provision in their trust deeds or rules that require them to use a particular individual or company to provide services to the scheme, that provision will be overridden by our regulations.**

[15] s247 and s248 of the Pensions Act 2004 – TPR Code of Practice No 7.

Reporting on the governance standards

79. In the March Command Paper we asked whether the proposed reporting requirements – centring on the Chair's statement – would help drive compliance with the new minimum standards.

80. Many respondents thought that the new reporting requirements would help ensure compliance, in particular because they would help to focus minds and ensure delivery.

"[We] believe that it is inevitable that having to make a written statement about how the quality standards are met will compel trustees and providers of bundled defined contribution schemes to review and document their existing administration services and to improve or document governance processes."

Anonymous

81. But respondents also stressed that any approach to compliance should be proportionate, and should focus on changing behaviours rather than reporting for its own sake.

"While accountability mechanisms are essential, good governance is ultimately about behaviour. Great care needs to be taken in getting the balance right between influencing behaviour and creating a complicated and onerous culture where there is an undue focus on compliance, rather than energy focused on delivering what is judged best for scheme members."

Investment Management Association

82. We agree with these responses. We think the requirement to annually produce a Chair's Statement on how the minimum governance standards have been met will help ensure that trustees are considering the most important aspects of running their scheme. We will not however be overly prescriptive in regulations about how trustees complete the Chair's Statement. The onus will instead be on trustees to consider and report on how best to assess their scheme, taking into account the particular needs of their members. This flexibility will help ensure that reporting helps to drive effective behaviours.

83. We consider that the best, and least burdensome, way of introducing these new reporting requirements, is to build on the existing requirements for schemes to produce an annual report as set out in the existing Disclosure Regulations[16]. **We therefore intend to regulate for the Chair's Statement to be produced annually and included in the scheme's annual report**.

84. **As part of the annual report, we propose that the Chair's Statement will be made available on request to members, prospective members, and beneficiaries**. But we also expect (as is the case now for annual reports) that many schemes will want to disseminate their Chair's statement more widely – for example via websites.

85. The March Command Paper also suggested that there could be a requirement for the Chair's Statement to be subject to a light touch audit approach, and could be attached to the scheme's audited accounts. Respondents questioned this approach, and it did not receive widespread support.

"[The command paper] refers to trustees providing "a clear independent audited annual statement that they have met the governance standards". We do not believe that the governance standards will be audited and this sort of terminology should be avoided..."

Institute of Chartered Accountants of England and Wales

[16] The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2103 SI 2013/2734.

86. Having considered these responses we agree that the potential burden on schemes of requiring the Chair's statement to be audited would not necessarily lead to better outcomes for members. **We therefore intend that the Chair's Statement should be subject to the same level of scrutiny as the rest of the annual report**. This provides a safeguard in coming within the general duty placed on auditors to notify TPR if they believe that a legislative or regulatory requirement has not been complied with, but should not lead to significant additional audit costs on schemes.

87. Chapter 5 contains more information about how compliance with the new regulations will be monitored. TPR will be given powers to regulate occupational schemes. The regulation of providers of workplace personal pension schemes is the responsibility of the FCA who have recently consulted on a set of draft rules for IGCs.

Independence standards for master trusts

88. Unlike single-employer occupational schemes, master trusts do not have the built in relationship with a single employer which can act as a safeguard for protecting members' interests. Where master trusts use a vertically integrated provider there may also be greater potential for conflicts of interest. So as well as the minimum governance standards discussed above, the March Command Paper contained proposals to strengthen the independent governance of master trusts, as follows:
    - master trust boards must have a minimum of seven trustees, the majority of whom, including the chair should be independent of providers of advisory, administration or investment services to the master trust;
    - limited terms for independent trustees;
    - open and transparent recruitment process of independent trustees; and
    - arrangements to ensure that members' views are directly represented.

89. In the March Command Paper we also asked:
    - whether master trusts should have to meet the same independence requirements as providers of workplace personal pension schemes;
    - for views on the proposed definition of "independent"; and
    - whether the independence requirements should be applied in different ways to different models of master trusts.

90. We appreciate that the term "master trust" is used to refer to a variety of different types of multi-employer occupational schemes. In this context, by "master trust" we mean any multi-employer scheme where the employers are non-associated[17]. This will include schemes which have been set up as master trusts for non-associated employers, but which only currently have, for whatever reason, one participating employer or group of connected employers.

91. Respondents to the consultation were in general agreement that providers of workplace personal pension schemes and master trusts should meet broadly equivalent – if not always identical – standards.

    "It is important to ensure as level a playing field as possible for the various pension provider frameworks. Since both master trusts and commercial providers share many of the same challenges in terms of having diverse employers and workforces within the same "product" and the use of the provider's services in operating the product (administration and investment management), similar governance frameworks should also apply."

    Mercer

[17] As set out in the Chapter 1, the governance requirements, including those for master trusts, apply to workplace schemes which provide money purchase benefits (except where the only money purchase benefits are in respect of AVCs).

92. We agree with this assessment and have been working with the FCA to ensure that the proposed rules on IGCs and our intended regulations set out broadly equivalent requirements for providers of work based personal pensions and master trusts.

Definition of independence

93. In Annex B of the March Command Paper we set out a detailed set of requirements that master trust trustees would have to meet in order to be classified as 'independent' of the scheme and its providers. These were:

- That an independent trustee cannot have been an employee of the scheme or any of its providers, or the same company or group, within the last five years; and
- That an independent trustee must not have, or have had within the last three years, a material business relationship with the scheme or any of its providers either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the scheme or its providers.

94. Whilst respondents broadly agreed that there should be independence requirements for master trusts, many were concerned that the criteria set out in the March Command Paper were too prescriptive, and should not be set out in legislation. In particular they thought that too stringent requirements might diminish an already limited talent pool and that overly rigid requirements might lead to good people being excluded from master trust boards.

"We believe that it is essential that the definition does not operate to unduly restrict the pool of talent with the necessary skill set or to undermine the competence of the governing body. .... we have concerns that there is a limited amount of resource and capability to undertake these roles and restricting the definition too much could add to that."

Capita

95. We have taken these comments on board and agree that there are risks with being too prescriptive about circumstances in which trustees cannot be considered to be independent. While it is important that the majority of master trust trustees are independent of the scheme and its providers, we want trustee boards to have sufficient flexibility in appointing the trustees they think best able to fulfil these roles for their schemes.

96. **We therefore intend to use regulations to set out the factors to be taken into account in assessing whether a trustee would be considered to be independent**. This will set clear expectations about those circumstances that would generally be expected to prevent a trustee from being considered independent, while still allowing sufficient flexibility for trustees to decide what is best for their scheme. This also aligns with the approach that the FCA has proposed in its draft rules for IGCs.

97. Some respondents also asked whether it would be possible for someone to be both an independent member of a firm's IGC and an independent trustee of a master trust provided by that firm. We do not think that sitting as an independent member of a firm's IGC should in itself prevent someone from also being an independent trustee on a master trust. **We will therefore ensure that regulations do not prevent an independent trustee for a master trust sponsored by an insurance company from also being an independent member of that provider's IGC.**

Professional trustee firms

98. We asked in the March Command Paper whether the independence requirements should be applied to different models of master trusts. We particularly asked how the requirements should be applied to master trusts that use a professional trustee firm to act as their corporate trustee.

99. Of those who responded on this point, some respondents thought that the current arrangements whereby many master trusts use a single trustee firm to govern their master trust can concentrate too much influence in a single entity. Some also suggested that the commercial relationship between the trustee firm and the scheme provider can limit the independence of the firm.

    "There is a need for diversity on a trust board and no matter how "arms-length" an independent trustee may claim to be, the act of appointing one in a corporate capacity (without the diversification of other viewpoints) is disquieting."

    Pensions Playpen

100. Some other responses, including from trustee firms and providers who use them, stressed the experience and professionalism that using a trustee firm can bring. Some suggested that, because the firm can draw on the skills of more than one individual, it would be appropriate to appoint a firm in place of a larger number of individual trustees.

    "We think that there may be an argument for some difference in requirements in the case of master trusts that are run by a single, corporate independent trustee; i.e. there is no need for individuals to be appointed alongside such a trustee provided that the trustee is suitably qualified and there is a mechanism for their performance to be assessed."

    JLT Benefit Solutions Ltd.

101. We agree that professional trustee firms can bring strengths to a trustee board. However, we want to ensure that all master trusts have sufficient breadth of views and experience, and agree with those respondents who suggested that using a single trustee firm to govern a scheme may not provide this.

102. **We do not therefore intend to make any special provision to treat a company that provides professional trustee services otherwise than as a single trustee for the purposes of these legislative requirements**. Normally it is the company, rather than individual members of staff, which is appointed as the trustee.

Incorporated trustee boards

103. Some respondents also commented on arrangements where a single corporate trustee is created to govern a particular scheme, and how they would need to meet the independence requirements. There was general support for the directors of these corporate trustees to have to meet the governance requirements in the same way as other trustee boards.

104. We agree that the independence requirements should apply to an incorporated trustee in the same way as to an unincorporated trustee board. **We therefore intend that, where a scheme has set up a company to act as a trustee with individuals or trustee firms acting as directors within that company, the directors should have to meet the minimum number and independence requirements in the same way as individual trustees.**

Different models of master trust

105. Some respondents described different models of master trusts, in particular those that are only open to employees within a particular industry, and asked whether they were intended to be in scope of these regulations.

106. We recognise that master trusts come in a number of different models with different strengths and risks, and have considered whether some models of master trust should be excluded from the scope of the new independence requirements.

107. However, we think that the new requirements offer protections that are relevant for members of all types of master trust. For example, even if a scheme is only open to employees of a particular industry, there would still be risks of insufficient breadth of oversight if the scheme was overseen by a single trustee, so we think the minimum number of trustees should apply.

108. **We therefore intend the regulations to apply to occupational schemes that are open to multiple non-associated employers, regardless of whether those employers operate within the same sector, or whether or not the scheme is operated on a commercial basis**[18, 19].

109. But we have also set out two exceptions to this. Firstly, we do not want to include those schemes which have distinct sections relating to employers which are not connected and each of those sections is governed by different trustees. We do not define these schemes as master trusts for this purpose and they are therefore not covered by these regulations. Secondly, we do not intend to cover the National Employment Savings Trust (NEST) because there are existing statutory requirements concerning how it is governed.

Minimum number of trustees

110. In the March Command paper we proposed that master trusts should be required to have a minimum number of seven trustees, and that the majority of trustees including the chair must be independent of the scheme's providers[20]. Respondents to the consultation questioned this minimum number, and in particular whether the costs of providing seven trustees would necessarily be in members' interests. While some respondents agreed there was value in ensuring a diversity of views and approaches in people governing a master trust, others suggested that increasing the number of people would not necessarily lead to better decision making. There were also concerns that there may be a limited pool of people with the appropriate skills and experience to be an effective master trust trustee.

"Whilst we can see some attractions in setting a minimum number of trustees to ensure a scheme is not dominated by a single trustee a lower figure such as three or five would allow greater flexibility. The higher the minimum number, the greater the risk that master trusts feel obliged to appoint trustees just to fill numbers rather than because of the skills and knowledge of each appointee."

NAPF

[18] For clarity, we do not intend the new regulations to cover those schemes which are only open to employers within the same corporate structure ("connected employers").

[19] This will include those schemes which have been set up as master trusts for non-associated employers, but which only currently have, for whatever reason, only one participating employer or group of connected employers.

[20] Unlike the other provisions in this paper we are referring to trustees only and not scheme managers.

"The number of members should be based on the knowledge and competencies required as well as how these skills are represented by the current membership and/or outsourced providers. We are supportive of an odd number of members so that there is a natural majority on each vote, leading to decisions being taken. However, the larger the group, the more difficult effective decision making is likely (but not necessarily guaranteed) to be. Larger groups are also more costly, eroding the value of savers' ultimate pensions."

Charlton Frank

111. We have taken these views on board and reconsidered our initial proposal. While we still think it important to have a minimum number of trustees, we agree that seven may not be the right minimum number for all schemes. Such a requirement would lead to additional costs for those schemes which currently have a smaller trustee board, which may not always be in members' interests.

112. We think that most significant master trust schemes should have a minimum of five trustees. However, in some cases – for example smaller schemes which also have fewer investment options – we recognise that a smaller number of trustees may be sufficient to effectively govern the scheme.

113. The FCA has recently consulted on rules requiring workplace personal pension providers to establish and run IGCs with at least five members. The rules also provide for smaller and less complex schemes to use a "Governance Advisory Arrangement" in place of an IGC. This recognises that in some cases it may be appropriate for providers to appoint a third party to take on the responsibilities of an IGC. Therefore, while the majority of providers will be required to have an IGC with at least five members, this requirement would not apply across the whole market.

114. We have considered whether it would also be appropriate to legislate for a minimum number of five master trust trustees, with provision for an alternative arrangement for small and simple schemes. However, we think the different characteristics of workplace personal pensions and master trusts and their providers mean that it is appropriate to take slightly different approaches to minimum numbers of trustees. In particular, we do not think it would be appropriate for any master trust, regardless of its size or complexity, to have fewer than three trustees.

115. **We therefore intend to regulate for master trusts to have a minimum of three trustees, with the majority, including the chair, being independent of the providers used by the scheme. This is however a minimum number and we will expect schemes to have the appropriate number and mix of trustees to oversee their particular scheme**, bearing in mind factors such as its size and complexity. We intend to use guidance to set out our expectation that most master trusts are likely to need at least five trustees to provide the appropriate breadth and depth of oversight. Trustees will be required to report on how the independence requirements have been met.

Duration of Appointment

116. In the March Command Paper we proposed that independent master trust trustees should be appointed for limited terms of a maximum of three years and only be eligible for re-appointment a maximum of twice. This was primarily proposed as a means of ensuring that independent trustees remain truly independent of the scheme.

117. While respondents were not necessarily opposed to limited terms in principle, a number reported concerns with the particular limits proposed in the March paper. In particular some felt that three years was too short a term, and would bring risks of losing valuable, experienced trustees as well as increasing cost and complexity.

"If trustees are genuinely independent then we think that three years may be too short for a maximum term of office, and would prefer five years as a maximum term of appointment with a ten year limit on total service. We want schemes to be run for the long term and think that trustee appointments should be allowed to reflect this."

TUC

118. We continue to think that independent trustees should be appointed to serve a limited term, and should be subject to a maximum length of service. This is both to ensure that independent trustees remain sufficiently independent of the scheme and its providers and also to ensure that there is sufficient turnover of representation within a trustee board.

119. We accept however that the durations originally proposed may be insufficiently flexible. **We therefore intend to regulate so that independent trustees can only be counted as independent for a period of up to five years at a time. Where an independent trustee serves for a cumulative ten year period they will not be eligible for reappointment until five years have elapsed**. Some respondents also asked how the limited terms would be applied where trustee firms are used instead of individual trustees, particularly given trustee firms' ability to rotate the individuals representing them on a master trust's board.

120. We think that limited term appointments of a maximum of five years should be used in all cases, regardless of whether the independent trustee is an individual or a firm. **However, where the trustee is an independent trustee firm we propose that there should not be an overall limit of cumulative term. Instead, trustee firms will have to be represented on the board by a named individual. This individual (rather than the trustee firm) would be subject to an overall term of ten years following which they would need to be replaced by an alternative representative of the firm**.

121. We recognise that there will be trustees already in place on the day that the regulations come into force, who may not currently be subject to limited term appointments. We do not want to exempt these trustees from these duration requirements as this could lead to some trustee boards retaining the same personnel for very long periods. Nor do we want to apply these requirements to any period before implementation as that could mean some trustee boards having to turn over their entire personnel immediately. So instead **we intend that the duration and cumulative terms should begin from the date that the regulations come into force**.

122. We also appreciate that it would be unrealistic to expect master trusts to appoint the required number of independent trustees from the day that the regulations come into effect and **so intend to give existing schemes up to three months after the regulations come into force to comply with the requirements**. Where a scheme is established after the regulations come into force we propose giving a three month period after establishment in which the required number of independent trustees must be appointed.

123. **We also intend to give a period of grace of three months between appointments if an independent trustee leaves at short notice** and in doing so leaves the trustee board short of the required number of independent trustees.

Transparent appointment of trustees

124. In the March Command Paper we proposed that schemes must use either an external search consultancy or open advertising to appoint independent trustees, including the chair. We also said that where an external search consultancy has been used it must be identified by the scheme and a statement made as to whether it has any other connection with the scheme or its providers and proposed that the scheme must involve the chair in the appointment of other trustees.

125. Some respondents questioned whether the requirement to openly advertise trustee vacancies or use a recruitment agency was too prescriptive and would lead to unnecessary costs. There was also a concern that open advertising might not attract suitable candidates. However, others welcomed this move to greater transparency in the appointments process.

"We do not agree that trustees/IGC members should be appointed only by use of a search firm or by open advertising. What is important is the objectivity, independence and openness of the appointment process. This is otherwise a further cost without justifiable benefit".

Legal and General

126. We continue to think that transparent recruitment of independent trustees is important and that open advertising or using a recruitment agency would be two good ways of achieving this. We have however listened to the concerns raised about being unnecessarily prescriptive about the methods of recruitment that schemes must use. **We therefore intend that rather than imposing specific requirements, the regulations will stipulate that the appointment process for recruiting independent trustees must be open and transparent and will include examples of ways to achieve this**.

127. **We intend that trustees should set out in the Chair's Statement details of how the recruitment process has been open and transparent**. The suggestion that the trustee chair must be involved in the appointment of other trustees received little comment from respondents. **We intend to legislate so that trustee chairs must be consulted on the appointment of other trustees** but will not be prescriptive about how this should be achieved. We will also consider whether to use guidance to set out further how firms can meet this requirement.

Hearing directly from members

128. In the March Command Paper we proposed that master trusts should have arrangements in place to ensure that members' views are directly represented. Some master trusts already have such arrangements in place and we think that they perform important roles both in informing members about their scheme and generating input from members. Examples of these arrangements include annual general meetings for members, member surveys and member representation on trustee boards.

129. Whilst these proposals were generally welcomed by respondents, there were some concerns expressed. Some respondents thought that there would be practical issues in having direct representation drawn from large diversified membership of a master trust. Another thought that whilst member and employer forums were to be encouraged, they should be an addition to board representation and not an alternative to it. Other respondents thought that there should be arrangements in place to ensure that members' views are directly represented without prescribing how this should be done.

"For confidence in a pension scheme to be retained it is important that members and employers can see that they have adequate representation in the running of the pension scheme.

It is clearly a matter for debate as to how such representation could be achieved, although it is worth noting that organised groups of employee and employer representatives exist; and their knowledge and experience of representation could and should be put to use. The inclusion of a requirement for employee and employer representatives would easily complement the aim to have some independent expertise on governing bodies".

GMB

130. A common theme in responses was that – because of the different ways that member representation could be achieved, and the different strengths and weaknesses these options might have for different schemes – it might not be appropriate to put detailed requirements about member representation into legislation.

"There are a number of practical difficulties in ensuring that members' views are genuinely heard and considered – for example AGMs on their own might not be sufficient – and these will need to be taken into account, potentially in legislation, but perhaps more appropriately in any guidance issued by the government."

Society of Pension Consultants

131. We have considered these responses. **We do not intend to specify what these arrangements should be in legislation but say that master trust trustees must encourage members, or their representatives, to make their views known on matters relating to the scheme. The Chair's Statement must include a description of how this has been achieved**. We aim to set out further details on how this might be achieved in guidance.

NEST

132. The National Employment Savings Trust (NEST) is a money purchase trust based pension scheme that was set up to facilitate automatic enrolment. Although it is a master trust, NEST differs to other occupational schemes in that there are existing statutory requirements concerning how it is governed. These are set out in the Pensions Act 2008 and in NEST's order and rules, and include requirements about the appointment and tenure of the Chair and trustee members; a requirement for between 9 and 15 members including the chair; and a requirement to set up panels to represent both members and employers. NEST does not have control over the appointment of trustee members as these are public appointments made by the Secretary of State for the Department for Work and Pensions.

133. **As there are already (usually higher) governance requirements set out in existing legislation and setting out new requirements would contradict these provisions, we intend to exempt NEST from the additional requirements for master trusts. The other governance standards and charge controls set out in this paper would apply to NEST.**

Accreditation of administrators

134. As well as the legislative minimum standards outlined above, we are also interested in exploring non-legislative ways of raising standards in occupational schemes. In the March Command Paper we focussed on administration and helping schemes get assurance about their administration standards, in particular through accreditation and quality marks. We mentioned the Pensions Administration Standards Association (PASA)'s accreditation programme for pensions administrators and encouraged schemes to take advantage of this.

135. In the March Command Paper we asked:

- for views on the potential benefits of accreditation of administrators, and what role government and regulators could play in supporting this; and
- for suggestions of other approaches to helping trustees and IGCs ensure that their scheme is being administered to a good standards.

136. Respondents recognised the importance of good administration and many thought that a system of voluntary accreditation such as that operated by PASA would play an important role in this. There was considerably less support for any move to make accreditation compulsory, because of fears that this could lead to extra burden and costs.

"We support independent accreditation of administrators. However, this should initially be on a voluntary basis but trustees should be encouraged to seek out firms that have that accreditation."

Legal & General

137. We agree that legislative action is not required at this stage. **We will continue to consider ways in which we can raise awareness of the benefits of using a voluntary accreditation regime such as that run by the Pension Administration Standards Association, and encourage good practice in this area.**

What the draft regulations say

138. This section provides a narrative on Part 3 of the draft regulations attached at Annex C, aimed at improving the governance of occupational pension schemes. Whilst specific consultation questions are set out here, views are welcomed on this Part of the draft regulations as a whole.

139. This part of the regulations will amend the Occupational Pensions Schemes (Scheme Administration) Regulations 1996 ("the Administration Regs") in order to insert most of the new governance requirements into those Regulations. It also makes amendments to:

- The Occupational Pension Schemes (Investment) Regulations 2005 ("the Investment Regulations").
- The Occupational Pension Schemes (Disclosure of Information) Regulations 2013 ("the Disclosure Regulations").
- The Register of Occupational and Personal Pension Schemes Regulations 2005 ("the Registration Regulations").

Definition of relevant scheme

140. Regulation 1 of the Administration Regulations, as amended by regulation 13 of the Charges and Governance Regulations will define a "relevant scheme" to which the governance standards apply, in line with the scope and coverage described in Chapter 1.

Appointment of service providers

141. New regulation 6A of the Administration Regulations will ensure that trustees are not constrained in relation to their choice of service providers. The regulations requires that a relevant scheme must not restrict the choice of who provides administrative, fund management, advisory or other services to the scheme. Where schemes have provision in their trust deeds or rules that require them to use a particular individual or company to provide services to the scheme, that provision will be overridden by this regulation.

> **Consultation Question 3**
>
> Do the regulations achieve the policy intention of protecting against trustees being restricted to particular service providers, while allowing employers to set appropriate parameters around investments?

Chair of trustees

142. New regulation 22 of the Administration Regulations requires trustees of a relevant scheme to appoint a chair of trustees. The chair must either be:

- an individual who is a trustee of the scheme;
- a professional trustee body which is a trustee of the scheme);
- where the trustee is a company but is not a professional trustee body, an individual who is a director of that company.

143. A professional trustee body will be defined in regulation 1 of the Administration Regulations, as a body which:

- was not established by an employer in relation to the scheme;
- is remunerated for its services as a trustee of the scheme; and
- has arranged a policy of insurance in relation to the exercise of its functions as a trustee of the scheme.

> **Consultation Question 4**
>
> Do the regulations adequately describe professional trustees?

144. Where an occupational scheme is run by managers rather than trustees, the managers must also appoint a Chair. In this case the chair must be one of the managers. New regulation 22(6) provides a period of grace of three months from the date the regulations come into force to appoint a Chair.

145. Where the chair ceases to be a chair for any reason (e.g. because they resign, die, are removed by the trustees or managers), the regulations allow schemes up to three months to appoint a replacement chair.

146. The amendment to the Registration Regulations made by regulation 15(2) adds the name of the chair to the list of registrable information that must be provided to TPR. This applies to relevant schemes that are required to register with TPR.

Annual statement

147. Under new regulation 23 of the Administration Regulations, trustees or managers will be required to prepare an annual statement within seven months of the end of each scheme year including:

- in relation to the default arrangement
  - the statement of investment principles governing decisions about investments in the default arrangement
  - any review of the default strategy or performance of funds underlying the default strategy undertaken during the year and changes resulting from such a review
  - where no review was undertaken during the year in question, gives the date of the last review
- how the requirement to process core financial transactions promptly and accurately has been met;
- in relation to charges and transaction costs:
  - the level of charges and transaction costs applicable to the default arrangement during the year or where the scheme has more than one default arrangement, the range of levels of charges and costs;
  - the range of the levels of charges and transaction costs for funds which are not part of the default arrangements; and
  - information on transaction costs which the trustees or managers have not been able to obtain and an explanation of what steps are being taken to get that information in future;
  - the extent to which the charges and transaction costs represent good value for members.
- how the trustees requirements for knowledge and understanding under Sections 247 and 248 of the Pensions Act 2004 have been met throughout the year and an explanation of how the trustees or managers have, or have access to, all the competencies necessary to properly run the scheme;
- the statement must be signed on behalf of the trustees or managers by the chair.

148. New regulation 23(2) provides that where the first scheme year ending after 6th April 2015 is sooner than the 5th April 2016, the Chair's statement should relate to the period from 6th April 2015 to the end of that first scheme year.

149. The insertion of new paragraph 34 in Schedule 3 to the Disclosure Regulations requires the Chair's Statement to be included in the annual report.

Requirement for processing financial transactions

150. New regulation 24 of the Administration Regulations requires trustees or managers to ensure that core financial transactions are processed promptly and accurately. New regulation 24(2) describes a non-exhaustive list of core financial transactions as:

- investment of contributions to the scheme;
- transfers of assets relating to members into and out of the scheme;

- transfers of assets relating to members between different investments within the scheme; and
- payments from the scheme to, or in respect of, members.

Assessment of charges and transaction costs

151. New regulation 25 of the Administration Regulations requires that the trustees or managers must, at intervals of no more than one year calculate the charges, and as far as they are able, the transaction costs borne by members of the scheme. It requires that the trustees or managers must assess the extent to which the charges and transaction costs represent good value for members.

Design and review of the default strategy and review of the underlying funds

152. New regulation 2A(1) of the Investment Regulations requires that the trustees or managers prepare and maintain a statement of the investment principles governing the default arrangement and that this statement must include

- The aims and objectives of the trustees or manages in respect of such investments for the purposes of the default arrangement
- Their policies in relation to the matters mentioned in Regulation 2(3)(b) of the Investment Regulations (policies on investments) in respect of the default arrangement
- An explanation of how the default strategy is intended to ensure that assets are invested in the best interest of members and beneficiaries

153. New regulation 2(A)(2) requires that the trustees or managers must review both the default strategy and the performance of the funds used to deliver the default strategy at least every three years and without delay after any significant change in investment policy or the demographic profile of relevant members.
154. In particular, trustees and managers must review the extent to which the return on investments relating to the default arrangement (after deduction of charges) is consistent with their aims and objectives in respect of the default arrangement.
155. Regulation 4(2) of the Investment Regulations already requires that assets must be invested in the best interests of members and beneficiaries and in the case of a potential conflict of interest in the sole interest of members and beneficiaries. However this requirement does not apply in some circumstances, for example where the scheme has fewer than 100 members. For schemes to which this provision does not apply, new regulation 4A of the Investment Regulations will extend the same requirements to these scheme's default arrangements.

New requirements for master trusts

Definition

156. The term "master trust" does not have an agreed single definition and is used to refer to different types of multi-employer pension schemes. Rather than refer to a master trust these regulations use the term "relevant multi-employer scheme" (hereafter referred to as a master trust). This will be defined in regulation 1(2) of the Administration Regulations as one in which some, or all of the participating employers are not connected employers, or which is promoted as a scheme where

participating employers need not be connected employers. New regulation 1(2ZA) will define both "connected employers" and "participating employer". A participating employer is any employer currently or previously participating in the scheme in accordance with the scheme rules. In defining "connected employers" the regulations refer to provision in s.1159(1) of the Companies Act 2006 and to partnerships where each partnership has the same person as at least half of its partners.

157. The definition of "relevant multi-employer scheme" incorporates two exceptions. The first relates to schemes which have distinct sections relating to employers which are not connected and where each of those sections is governed by different trustees. The second exception is NEST.

Consultation Question 5

Does the definition at regulation 1(2) capture those schemes described as master trusts in chapter 2?

Annual Chair's Statement for master trusts

158. New regulation 26 of the Administration Regulations requires that, for master trusts covered by these arrangements, the Chair's statement should include the following additional information if relevant to the scheme:

- how the requirement for there to be a majority of independent trustees and an independent chair have been met;
- where an independent trustee was appointed during the year, how the requirement for an open and transparent recruitment process was met; and
- Details of the arrangements in place to ensure that members views are represented.

Appointment of trustees

159. Under new regulation 27(1) of the Administration Regulations a master trust must have at least three trustees. This provision also requires that a majority of the trustees, including the chair, must be independent – the regulations do not use the term "independent" but instead refer to "non-affiliated" trustees in order to avoid confusion with trustees who are independent for the purposes of section 23 of the Pensions Act 1995. New regulation 27(8) defines non-affiliated as being independent of any company which provides advisory, administration, investment or other services in respect of the master trust. The factors that must be taken into account in determining whether a person is independent of a service providers is set out in new regulation 28.

160. New regulation 27(3) requires that the chair of trustees must be consulted on any appointment, this applies to both non-affiliated and other trustees.

161. Where there is a corporate trustee which is not a professional trustee body, new regulation 27(4) provides for the individual trustee directors to be treated as if they were individual trustees for the purposes of these requirements.

162. New regulation 27(7) provides for a period of grace of three months from the date the scheme is established, or becomes a master trust, for these requirements to be met. New regulation 27(6) provides for a similar period of grace where a trustee ceases to be a trustee, or ceases to be non-affiliated.

Appointment of trustees who are non-affiliated

163. New regulation 28 of the Administration Regulations requires that the appointment process for a trustee who is non-affiliated must be open and transparent and we have set out some examples of what we mean by an open and transparent appointment processes. These are:

- a process which includes advertisement of the vacancy in at least one appropriate national publication;
- a process which includes engagement of a recruitment agency to assist in the selection of candidates; and
- a process which meets the requirement for appointing member nominated trustees and trustee directors as set out in of sections 241(2) and 242(2) of the 2004 Pensions Act – this would help to encourage member nominated trustees to be counted as independent.

164. New regulation 28 also sets out the circumstances that must be taken into account when determining whether or not a trustee is non-affiliated. These are

(a) Whether the person;

  (i) is a director, partner or employee of a company which provides advisory, administration, investment or other services in respect of the scheme (a "service provider") or a company which is connected to a service provider; or

  (ii) has been such a director, partner or employee during the period of five years ending with the date of the person's appointment as a trustee;

(b) whether the person receives any payment or other benefit from a service provider – other than in respect of a role in the governance of a personal pension scheme; and

(c) whether or not, in the person's relationship with a service provider, the person's obligations to the service provider conflict with their obligations as a trustee of the relevant multi-employer scheme and whether their obligations as a trustee will take priority in the case of a conflict. This provision, along with the exception to paragraph (3)(b) is intended to ensure that a trustee can also be an independent member of an IGC.

165. New regulation 28(4) includes provision to ensure that non-affiliated trustees who are individuals (and directors of corporate trustees who are themselves treated as trustees for this purpose) can only be classified as non-affiliated for a single term of no more than 5 years, with a cumulative limit of 10 years. But no period of appointment of an individual trustee is taken into account if more than 5 years have elapsed since that trustee last held office in the scheme.

166. Where the non-affiliated trustee is a professional trustee body new regulation 28(7) requires that the trustee is subject to the 5 year terms but there is no overall cumulative term. Instead, a nominated individual must act as a representative of the professional trustee body and may not act for more than ten years in total.

167. For the purposes of the definition of "affiliated trustee" regulation 28(8) uses the same definition of whether two companies are connected as in the definition of relevant multi-employer scheme as in regulation 1(2ZA).

Representation of members

168. New regulation 29 of the Administration Regulations require that the trustees or managers of a master trust must encourage members of the scheme, or their representatives to make their views on matters relating to the scheme known to the trustees or managers.

Consultation Question 6

Do the draft regulations meet our policy intention of ensuring that occupational schemes are well-governed?

Transparency in workplace pension schemes

3

Summary

- Improving the transparency of costs and charges is essential to address the current weaknesses in the workplace pensions market and to enable an effective review of the default arrangement charge cap in 2017.
- From April 2015, subject to Parliamentary approval, as part of the new governance standards described in Chapter 2, trustees and Independent Governance Committees will be required to report on costs and charges. TPR and FCA are working with the pensions and asset management industries on how existing disclosure practices will be improved to support these new governance requirements.
- The Government will go further in 2015 and will consult on regulations under duties in the Pensions Act 2014 requiring information about transaction costs to be disclosed to members and others and the publication of costs and charges information.

Introduction

1. The March Command Paper set out the Governments proposals for achieving full transparency of costs and charges in workplace schemes. Specifically, the March Command Paper proposed placing new duties on trustees and IGCs to report on costs and charges and proposed new requirements for the standardisation and disclosure of administration charges and transaction costs. The March Command Paper also included consultation questions on how transparency should be applied in unbundled occupational money purchase schemes and in Defined Benefit (DB) schemes.

2. This chapter:

- describes the first phase of transparency measures and the reporting requirements that will facilitate this – primarily the new reporting requirements incumbent on trustees and IGCs;
- sets out the Government's position regarding transparency in unbundled occupational money purchase schemes and the extension of transparency requirements to DB schemes, in response to those specific questions raised in the March Command Paper; and
- provides an update on the Government's plans for improving transparency in a second phase of measures; we intend to consult on these in 2015.

The first phase of enhanced transparency

3. The Government's proposals for improving transparency of costs and charges were generally welcomed by many of those who responded to the March Command Paper.

"We believe it is essential that customers in both trust-based and contract-based schemes benefit from consistently high levels of transparency, disclosure and regulatory protection."
Lloyds

"We welcome the government's intervention on charge disclosure. Whilst we also recognise the value in the various industry initiatives we believe that the only way to meet the aims of greater transparency of charges is through the implementation of a single disclosure regime across all workplace pensions."
Fidelity

4. As part of the new minimum governance standards described in the previous chapter, trustees and IGCs will be required to consider their scheme's costs and charges, making an assessment of the value for money the scheme is providing for its members, and reporting on this annually. In occupational schemes this will be in the form of an annual statement signed by the Chair of trustees ('Chair's Statement') attached to the Annual Report. Regulation 16(1) of the attached draft regulations amends Part 5 of Schedule 3 to the Occupational and Personal Pensions (Disclosure of Information) Regulations 2013[21] to include a Chair's Statement, where one is required under regulation 23 of the Scheme Administration Regulations, in the list of information which must be included in the scheme's annual report.

5. For workplace personal pension schemes, the FCA's recent consultation on 'Proposed Rules for Independent Governance Committees' sets out their plans for making rules to similarly require public disclosure of IGCs' assessments of value for money in an annual IGC Chair's report. This first phase will be an important building block in empowering trustees and IGCs to more fully scrutinise costs and charges across the workplace pensions market.

[21] S.I. 2013/2734.

The Chair's Statement

6. As described in Chapter 2, for occupational schemes the Chair's Statement will bring together all the information about how the scheme is meeting its governance standards (regulation 16 of the attached draft regulations refers). These standards include the requirement to report on the scheme's administration charges and the variable trading costs a scheme incurs as a result of buying, selling, lending and borrowing underlying investments (commonly referred to as "transaction costs") and describe how the trustees have assessed the value for money they offer. There was general agreement during the consultation that there would be value in requiring schemes to report against these standards, so long as the reporting requirements were proportionate. A detailed explanation of what will be expected of trustees in terms of assessing costs and charges and the value of these is set out in Chapter 2.

7. This new requirement to report on costs and charges in the Chair's Statement will demonstrate how trustees are meeting the minimum governance standards of assessing charges and costs, and will also lay the foundations for the next phase of improved transparency. As mentioned in Chapter 2, we recognise that information on transaction costs is not routinely requested by or made available to many schemes at the moment and that trustees may not be able to access all of this information in the first year of reporting. We expect that trustees will obtain, describe and report on these costs as far as possible – explaining in their reporting why they have not been able to obtain information on particular types of costs and what steps they are taking to obtain this information in the future.

8. The FCA has recently consulted on comparable requirements for IGCs and has proposed that the terms of reference for an IGC must require its Chair to produce an annual report on the IGC's work. This will include a report on the value for money delivered by schemes, and in particular an assessment of how the provider has performed against aspects of scheme quality set out in the governance standards. As DWP intends to prescribe for occupational schemes, our expectation is that FCA rules will set out how IGCs will report on the level of direct and indirect costs incurred for transactions and other activities in managing and investing the pension assets of workplace personal pension scheme members.

Support from the asset management industry on disclosure of transaction costs

9. Requiring trustees and IGCs to report on transaction costs will contribute towards greater awareness and transparency of such costs being incurred by schemes and members. Asset managers also have a critical part to play in disclosing these costs back to trustees, IGCs and investors. The DWP, FCA and TPR have been working with the Investment Management Association (IMA), and the Association of British Insurers (ABI) with a view to improving the disclosure of transaction costs in time for the new governance standards coming into force from April 2015. The FCA plan to consult in 2015 on rules outlining how cost information is to be disclosed by firms to both trustees and IGCs, taking into account the efforts made by industry to improve the transparency of transaction costs.

The Government's response to its consultation questions on transparency in unbundled occupational money purchase schemes and extending requirements to Defined Benefit schemes

10. In the March Command Paper consultation we asked for views on:

- how the proposed transparency requirements could be made to work effectively in unbundled trust-based arrangements (including master trusts); and
- whether the transparency requirements we propose for DC schemes should, in the future, be extended to DB schemes, to enable sponsoring employers to further scrutinise the costs of such schemes.

We set out below our proposals in these two areas, following consideration of the responses we received.

Making transparency work for unbundled occupational schemes

11. Of those who responded to this question, many pointed out that the new arrangements should work equally well for these types of schemes, and envisaged no additional issues:

"We do not see any reason why unbundled trust-based arrangements should have any difficulty in complying with the transparency requirements set for other types of arrangements. In fact, trustees of unbundled arrangements are more likely to have natural sight of the various costs as they are procuring these services separately than those trustees / IGCs that are contracting for services on a bundled basis".

Charlton Frank

"We welcome the DWP's intention to ensure that "minimum governance standards will apply across all DC workplace pensions" (page 11, para 2). We therefore hold the view that the transparency requirements should also apply to unbundled trust arrangements."

Aviva

12. However, some respondents pointed out that there were challenges for unbundled schemes.

"Given the considerable range of costs and the differences between the manner in which they are calculated, this requirement will present a particular challenge to trustees of unbundled schemes".

Buck Consultants

"By increasing the transparency obligations that are placed on unbundled trust-based arrangements, the compliance costs associated with that transparency would increase. This would be a result of the additional level of data collation which the administrator would need to perform in order to report on the transaction costs per individual member"

BlackRock

13. We recognise that different schemes may face different challenges in obtaining and collating all the necessary information about charges and transaction costs, depending on how much of this information they currently consider and the structure of their scheme. However we agree with respondents that the governance and transparency requirements should apply equally to bundled and unbundled arrangements. We will therefore require the Chair's Statement, to report on costs and charges, regardless of whether the scheme is a bundled or unbundled scheme.

Defined Benefit scheme transparency

14. In the March Command Paper we also asked for views on whether we should extend the requirements we propose for DC schemes to DB schemes. Some respondents were in favour of this approach, and others pointed out that extending the governance and transparency requirements to DB schemes may not be appropriate given the different nature of these types of schemes.

"At a high level, the benefits payable to members of DB schemes do not depend directly on the charges incurred in running a DB scheme. ...The advice regime available to trustees and sponsoring employers is better developed, and generally at a higher level of expertise, than necessary in the context of minimum standards required for members of DC schemes. It should also be noted that the level of scheme governance is more robust in the more mature DB schemes market than for DC schemes. Thus, the requirement for minimum standards is less of a material issue for DB schemes...We welcome transparency of costs for DC and DB schemes, but we suggest that the current mechanisms are satisfactory for DB schemes."

Institute and Faculty of Actuaries

15. We are aware, both from responses to the March Command Paper consultation and from research undertaken by TPR that there are some shared challenges between trustees of DB and DC schemes in terms of fully understanding and effectively scrutinising costs. A number of consultation respondents favoured greater transparency in DB schemes at the asset management level – particularly around transaction costs – to enable trustees of DB schemes to be fully aware of the costs involved in providing a scheme and ensure they are getting value for money. Several respondents also commented that it would be beneficial for employers providing DB schemes to be provided with costs and charges information, again to enable them to assess if they are getting value for money, since the risk lies with employers in terms of making up any shortfall.

"The aim of the new requirements is to address issues specific to DC schemes and these features are generally not present in DB schemes. Having said this, because the employer generally makes up any shortfall through a recovery plan, they already take a much keener interest in the costs of running DB schemes though we do not see the need to require this information to be provided to employers.

Employers and trustees should though be able to request information about transaction costs from their investment managers, and many managers already choose to disclose them in any event, but that the measures for DB schemes should not be the same as for DC schemes. We see little benefit though of members (or others outside the arrangement) being given the right to request this information."

Association of Consulting Actuaries

16. As the statutory employer bears the funding risk, it would be expected that they would wish to keep costs under review. Employers are also free to engage their own actuary to advise them. Some respondents did feel that employers were already engaged in asking for this information – by virtue of being the bearers of risk in DB schemes – and that any requirement should be for investment managers to provide this information to employers on request.

17. The Government's work to improve transparency in workplace money purchase schemes will ultimately benefit those running DB schemes. Trustees across all types of scheme will be able to engage more effectively with investment managers in ascertaining the full nature of transaction costs as both the buyer and supply side will have greater clarity regarding definitions and information expectations.

18. As we consider how regulations will support this work during 2015, we will look specifically at whether regulation for additional transparency in DB schemes is required.

The Government's plans for further improving transparency of costs and charges in 2015

19. In 2015 the Government will build on the new reporting requirements relating to costs and charges and consult on draft regulations to drive further transparency. Section 44 of the Pensions Act 2014[22] amends section 113 of the Pension Schemes Act 1993 and inserts a new section (section 137FA) into the Financial Services and Markets Act 2000 to place duties on the Secretary of State and FCA respectively, to make regulations and rules relating to the disclosure of costs and charges.

20. The amendments to section 113 of the Pension Schemes Act require the Secretary of State to make regulations requiring information about transaction costs to be given to members and other prescribed persons and also to require the publication of information about transaction costs and administration charges to facilitate public comparability of costs and charges. In 2015 the FCA intends to consult on the rules it will make to enable standardised, comparable disclosure of costs and charges information. The DWP and FCA will work together in 2015 to ensure that respective consultations, regulations and rules are coherent and complementary.

21. Taken together, these measures will represent a step change in the way that the pensions market operates and will enable those responsible for choosing schemes (such as employers and trustees) to make that choice with a fuller understanding of the costs and charges that will be incurred. Ultimately the Government's intention is that members will be able to compare the costs and charges they are paying with those of other schemes and see if they are getting value for money relative to that offered by alternative providers. We believe that this comparability of costs and charges will drive competition in the workplace pensions market and address some of the weaknesses identified by the Office of Fair Trading.

22. We recognise that the investment management and insurance industries are essential stakeholders to facilitate the transparency of transaction costs. The need for close working was also recognised by the IMA in their response to the consultation.

"We agree that investment and pensions industry needs to work towards greater transparency and consistency in its disclosure of charge and cost information, and are working to facilitate that objective."

Investment Managers Association

23. We are grateful for the close co-operation of the IMA in this work and have considered the comparative table of costs and charges that the IMA has recently consulted on with regard to authorised collective investment schemes[23]. We understand that a number of respondents to the IMA consultation gave examples of transaction costs which they said would not be disclosed through the IMA mechanism and we are aware that the table in its current form does not reflect all the costs identified in the March Command Paper. This may be a starting point to develop a template for investment managers to disclose transaction costs across a wide range of funds to trustees and IGCs in an easily understandable way. We will consider this as part of the work we have already commenced with the IMA, ABI, FCA and TPR to develop a model for detailed disclosure of transaction costs.

[22] http://www.legislation.gov.uk/ukpga/2014/19/section/44/enacted

[23] The comparative table is set out in the IMA's Statement of Recommended Practice which was re-issued on 14 May 2014 and can be found at: http://www.investmentfunds.org.uk/policy-and-publications/sorp-0314/

24. In planning our work programme, we are also mindful of proposals for enhanced transparency at a European level through IORP II[24], MiFID[25] and PRIIPs[26] and we are working on a cross-government basis to consider the interaction with our own transparency proposals.

25. We will work in partnership with the FCA to bring forward further regulations and rules that will introduce the requirements for the full disclosure and publication of costs and charges in workplace pension schemes. We intend to consult on our proposals during 2015, with a view to bringing regulations into force in 2016 to support the enhanced requirements and new reporting mechanisms. As detailed previously, the FCA intends to consult on amending their own rules to introduce equivalent enhanced transparency provisions for workplace personal pension schemes during 2015. In 2015, we will also examine whether regulation for further transparency in DB schemes is required.

[24] Directive on Institutions for Occupational Retirement Provision Mk II.
[25] Markets in Financial Instruments Directive.
[26] Packaged Retail and Insurance-Based Investment Products Directive.

Further information on the charges measures announced in the March 2014 Command Paper

4

Summary

1. The March Command Paper announced a series of measures to control charges in workplace pensions, to be introduced in two phases from April 2015 and April 2016. The primary legislation needed to enact these measures is contained in the Pensions Act 2014.

2. In relevant[27] occupational schemes used as qualifying schemes[28], trustees and managers[29] will be required to ensure that their schemes are compliant with the measures, with compliance regulated by The Pensions Regulator (TPR). We intend to lay the attached regulations for Parliamentary approval early next year, subject to any changes required as a result of this consultation. This legislation will form the regulatory framework which will also give enforcement powers to TPR.

3. Providers of workplace personal pension schemes[30] used as qualifying schemes will be required to follow rules which the Financial Conduct Authority (FCA) propose to make using their powers under the Financial Services and Markets Act 2000. The FCA will consult soon on rules equivalent to DWP's draft regulations, based on the principles described in this chapter.

[27] As explained in the Scope chapter, we propose the charges measures should not apply to qualifying schemes which provide no money purchase benefits. They also would not apply to executive pension schemes or relevant small schemes, where, amongst other conditions, all the members of the scheme are trustees, or directors of a company which is the sole trustee (see regulation 2). In addition we propose that the default arrangement charge cap should not apply to schemes where there is a third party promise in relation to the money purchase benefits (see regulation 4(3)). As most members of qualifying schemes will be subject to all the charges measures, for simplicity we refer to qualifying schemes throughout the rest of this chapter.

[28] By a 'qualifying scheme' we mean a scheme which is used by an employer to fulfil their automatic enrolment duties in relation to one or more jobholders under the Pensions Act 2008.

[29] Trustees will be used for simplicity through this chapter, but this should be understood to also include managers in the case of the small number of occupational schemes which are not trust-based.

[30] These are also referred to as contract-based schemes.

4. This chapter describes how the DWP has moved from the core charges measures announced in March to the detailed policy reflected in the attached draft regulations. This publication launches a consultation, including a number of specific questions, on that policy (as reflected in the draft regulations), which will last for four weeks and close on 14 November. We would welcome views on the policy intent itself and whether the draft regulations meet that intent.

Introduction

5. The March Command Paper signalled the Government's intention to:

- introduce a charge cap on the default funds of qualifying schemes, set at 0.75 per cent of funds under management. This cap will apply from April 2015 to all member-borne charges and deductions, excluding transaction costs. The Command Paper also explained how the cap will apply to schemes with combination charge structures;
- extend the existing ban on consultancy charges in automatic enrolment schemes to all qualifying schemes from April 2015;
- ban member-borne commission in qualifying schemes from April 2016. Where commission remains between April 2015 and April 2016, member-borne charges must fall within the cap;
- ban Active Member Discount (AMD) structures in qualifying schemes from April 2016. Where AMD structures remain in place between April 2015 and April 2016, deferred member-borne charges must fall within the cap; and
- in 2017, review the level of the default fund charge cap, to see if it should be lowered, and also whether it should include some or all of the transaction costs that are ultimately borne by members.

6. The March Command Paper formed the Government's response to the charges consultation conducted in the autumn of 2013.[31] It signalled our intention to work further with stakeholders and regulators on how the measures should be implemented. Therefore, since publication DWP has met with a wide range of stakeholders to discuss minimum standards, including charges, in workplace pensions. Alongside our own evidence and analysis these discussions have informed the policy draft regulations on which we are now consulting.

7. The areas covered in this chapter are as follows.

- Responsibility for complying with the charges measures.
- The default arrangement charge cap – defining member borne deductions that fall within the cap; defining the default arrangement; transitional questions on the default arrangement.
- When the cap applies, to whom and on what funds – permissible charge structures; entry and exit charges; assessment of charges; and opt-in services.
- Transitional questions on workplace personal pensions and the charge cap.
- Active Member Discounts.
- Commission and consultancy charges.

[31] Better workplace pensions: a consultation on charging CM8737. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/254332/cm8737-pension-charges.pdf

8. In designing the policy on which we are now consulting, we have been guided by the need to:
   - protect members who have not made an active choice about where their contributions are directed;
   - support the roll-out of automatic enrolment by minimising disruption for schemes and providers;
   - establish a proportionate and appropriate regulatory framework.

Responsibility for complying with the charges measures

9. Since the publication of the March Command Paper we have considered whether the duty for compliance should sit with employers and/or with trustees and providers. Working closely with the FCA and TPR, we have judged these two alternatives in the light of the need for the compliance regime to:
   - be effective in achieving high levels of compliance;
   - be proportionate in terms of the burden placed on employers (especially smaller employers), trustees and providers;
   - support the roll-out of automatic enrolment by minimising disruption for schemes and providers.

10. With these considerations in mind, the DWP proposes that the legal duty to comply with the charges measures should rest with trustees and managers in occupational schemes (as set out in regulation 4(1)), and with pension providers in workplace personal pension schemes. They are responsible for providing or buying in services on behalf of members and will be best placed to obtain the information on costs and charges. They will also be best placed to make changes to meet the new charges requirements, if these are required. Trustees will need to report via the annual Chair's Statement (described in Chapter 2 of this paper – see regulation 16) that they have complied with all the charges measures, and to The Pensions Regulator via the scheme return (see Chapter 5 and regulation 31).

11. Notwithstanding the charge cap measure, employers are still required to meet their employer duties, including providing a pension scheme for certain workers to be automatically enrolled into or be given the opportunity to opt in to or to use an existing scheme as long as it is a qualifying scheme. Successful compliance with the charges measures will, therefore, require trustees and providers to be aware when they are operating a qualifying scheme and under current requirements that should already be the case:
   - regulation 7 of the Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010 (SI 2010/772) states that employers must give trustees or providers all automatically enrolled jobholders' information, including each person's enrolment date, automatic enrolment date or re-enrolment date, as applicable;
   - regulation 7 of The Employers' Duties (Registration and Compliance) Regulations 2010 (SI 2010/5) ('the Registration and Compliance Regulations') imposes duties on providers and trustees relating to record keeping and opt-out notices for all automatically enrolled jobholders, once this information is provided to them by the employer;
   - in relation to workplace personal pension schemes, section 26 of the Pensions Act 2008 requires that there must be two specific agreements in place for the scheme to be a qualifying scheme:

- an agreement between the scheme and the employer;
- an agreement between the scheme and the jobholder, which must state that the latter will make up any shortfall between the employer's contribution and the automatic enrolment minimum of 8 per cent of qualifying earnings[32].

12. We will work with industry bodies, the FCA and TPR to maximise compliance with these existing requirements and where it is required, remind employers, trustees, managers and providers of their responsibilities.

13. We expect that as part of their record keeping duties under regulation 7 of the Registration and Compliance Regulations, trustees will maintain the necessary records to demonstrate compliance with the charges measures.

Consultation question – responsibility for complying with the charges measures

Q7: Do you have any comments regarding the policy on who should have the duty of compliance with the charges measures?

Do you have any comments about how the draft regulation (regulation 4) meets the policy intention?

The default arrangement charge cap

14. The March Command Paper announced that the default fund charge cap would be introduced from April 2015 for qualifying schemes. It also announced that the cap would cover all member-borne charges and deductions excluding transaction costs and will be set at 0.75 per cent of funds under management per annum, or at an equivalent rate in a combination charge structure.

15. This section consults on further detail on the definition of member-borne deductions which are subject to the cap, and the definition of the default arrangement. The regulations and this consultation refer to the 'default arrangement' rather than the 'default fund' to reflect the fact that common practice in designing a default strategy is to invest in more than one underlying fund during the accumulation phase, switching to less volatile investments in the run-up to decumulation.

16. Where the default is actually a group or a blend of funds, the cap will apply to the arrangement overall, rather than to each of the individual funds within the arrangement. An arrangement is defined in regulation 3(6) as an allocation of contributions to an investment, or to more than one investment according to a strategy. More information on defining the default arrangement is given from paragraph 30 of this chapter.

Defining member-borne deductions that fall within the cap

17. The Government announced in the March Command Paper that the default arrangement charge cap would apply to all member-borne deductions paid to the pension provider or another third party, excluding transaction costs. The deductions which are subject to the cap therefore relate to both general scheme administration and investment administration –approximate to current Total Expense Ratio (TER) measures used across financial services.

[32] There may not always be a second agreement if the employer pays 8% or more, and the employee is not required to pay any contributions at all – in this case there would be no 'shortfall'. See section 26(6) of the Pensions Act 2008.

18. In the regulations (see regulation 2(1)) we have referred to the deductions subject to the cap as "charges", which has the meaning given to "administration charges" in paragraph 1 of Schedule 18 to the Pensions Act 2014[33], excluding transaction costs, and certain other costs, as explained below.

Transaction costs

19. In the March Command Paper, we referred to transaction costs – to be excluded from the cap pending a review in 2017 – as the variable costs which a scheme incurs when buying, holding and selling underlying investments. To illustrate these concepts, the March Command Paper provided some examples of existing costs and whether they would be classed as member-borne deductions to be capped, or transaction costs.

20. With regard to the definitions of member-borne deductions and transaction costs, stakeholders have asked for clarification in two areas. First, they have pointed out that some fees which we have classified as fees to be capped, such as depositary fees and fees to the custody bank, may be interpreted as fees for holding investments. Second, costs relating to stocklending, which we have classified as lying outside the cap, may not be interpreted as related to the selling of investments.

21. Therefore, we have clarified the definition of transaction costs in regulation 2 as "the costs incurred as a result of the buying, selling, lending and borrowing of investments." We are not proposing to make any change in respect of the treatment of individual costs and charges as outlined in the examples provided in the March Command Paper. The policy intention remains that depositary fees and fees to the custody bank will be subject to the cap, whilst costs relating to stocklending will remain transaction costs outside the cap.

22. Trustees and providers will need to familiarise themselves with the types of deductions which are covered by the charge cap and ensure that they calculate such charges accordingly. These are set out in Annex B. This includes unbundled trust-based schemes, where trustees secure services from a range of service providers and a single figure for member borne charges may not have been previously apparent.

23. Charges relating to general scheme administration and investment administration which are borne by employers are not member-borne deductions, and are therefore not subject to the cap. The Government will examine the level of the cap in 2017, to ensure that qualifying schemes continue to present value for money for savers. It will also consider whether some or all of the transaction costs borne by members should be included within the cap.

Other costs excluded from the cap

24. Further to our March publication, we have identified two further types of cost which we propose should not be subject to the cap. These are reflected in the proposed definition of "charges" in regulation 2(1).

25. First, the costs and charges incurred by trustees in respect of pension sharing and complying with court orders are attributable to specific individuals, and recoverable from the parties to pension sharing and to the court order. They are quite different in nature from the charges associated with general scheme and investment administration.

[33] Pensions Act 2014 (c.19) – http://www.legislation.gov.uk/ukpga/2014/19/pdfs/ukpga_20140019_en.pdf

26. If the costs of pension sharing or complying with court orders were to be subject to the cap the extent of charges would be very difficult for trustees to predict and to control, and would place them at risk of breaching the cap through no fault of their own. We therefore propose that these costs are excluded from the cap.

27. Secondly, we propose that costs incurred by trustees as a result of scheme wind-up should also not be subject to the cap. Where trustees have concluded that they wish to close the default arrangement to future contributions, it will often be desirable for members and trustees alike for members' assets to be transferred to another lower charging scheme.

28. Whilst it would be preferable for all members to make an active decision to transfer their funds, in practice it could be difficult to contact and gain agreement from all members, and trustees will need to work with employers to proceed to wind up the scheme.

29. However, it would be perverse for trustees to be both unable to proceed (because the wind-up costs would result in a breach of the cap), and less and less able to comply with the cap (particularly if there is a flow of member-initiated transfers out of the scheme). As this would clearly not be in members' best interests, we are proposing that wind up costs should not be subject to the cap.

Consultation question – member-borne deductions that fall within the cap

Q8. Do you have any comments on the policy regarding the member borne deductions that fall within the cap, and how the draft regulations reflect the policy intention? These exclusions are:

(a) the non-recurring variable transaction costs which are incurred by a scheme when buying, selling, lending and borrowing underlying investments ("transaction costs" definition in regulation 2)

(b) pension sharing and compliance with court orders ("charges" definition in regulation 2)

(c) winding up costs ("winding up costs" definition in regulation 2)

Defining the default arrangement

30. The March Command Paper outlined an important principle – that charges should be limited where the member has made no active choice. It is not intended to prevent the member from actively choosing a more expensive arrangement. Since 2012 and the advent of the employer duties relating to automatic enrolment, trustees and providers of pension schemes used for automatic enrolment have had to offer a default arrangement, into which jobholders are enrolled if they make no active fund choice (an exception to this is catered for below in paragraphs 35-37). It is therefore clear that the default arrangement charge cap will apply to these arrangements.

31. In the March Command Paper, we recognised that some qualifying schemes, set up before the introduction of automatic enrolment, may not have a fund which can be easily identified as the 'default arrangement', as jobholders could have been required to make an active fund choice on joining. In occupational schemes, available data suggests this may be relatively rare – TPR's Scheme Governance Survey 2013/14[34] found that 23 per cent of occupational DC schemes only offer one fund and, of those that offer a choice of fund, 75 per cent reported having a default arrangement. The lack of an obvious default arrangement may be more common in pre-

[34] Occupational pension scheme governance: a report on the 2013 (seventh) scheme governance survey – http://www.thepensionsregulator.gov.uk/docs/governance-survey-report-2013.pdf

automatic enrolment workplace personal pensions, although providers who participated in the Landscape and Charges Survey 2013[35] reported that 80-95 per cent of members were invested in a default fund.

32. In designing the proposed regulations relating to the default arrangement, we have been guided by the twin principles of capturing as many workers as possible who did not make an active or fully informed decision about their investment strategy, whilst minimising the risk of capping funds where members did make an active choice. Alongside this, we have also sought to reduce the impact on the ongoing roll-out of automatic enrolment, by minimising the disruption for trustees and existing schemes.

33. As explained in Chapter 1, the charges measures will apply to default arrangements of qualifying schemes which provide money purchase benefits[36]. In the context of the charge cap this means any scheme which is a qualifying scheme in relation to one or more jobholders of an employer, at any date on or after 6 April 2015 (or the employer's staging date, if later). This means that the scheme does not need to be a qualifying scheme in relation to each individual member.

34. The policy is that a default arrangement should be in relation to an employer (covered in regulation 3(1)). So an arrangement which is a default arrangement for one employer will not necessarily be a default for another. Where a scheme is used by multiple employers, this assessment will need to be undertaken for each employer who is using the scheme as a qualifying scheme for their jobholders.

35. Where an existing scheme is going to be used as a qualifying scheme after the application of the charge cap, trustees and providers will need to identify the arrangement or arrangements in their scheme that the charge cap will apply to. As well as the 'true' default arrangement (funds into which workers' contributions are directed without the worker making any active choice), it is proposed that the cap will apply to other investment options, with the aim of capturing arrangements that have been used in a similar way to default arrangements in the past, and to capture arrangements used by employers who contract-join their workers before the automatic enrolment duty applies.

36. It is therefore proposed that the default arrangement covers:

    A. Any arrangement into which workers' contributions are directed without them having made an active choice as to where their contributions are directed is a default arrangement (see regulation 3(2)(a)).

    B. An arrangement into which 80% of the employer's workers are actively contributing on the relevant date (the date the charge cap comes into force, or the employer's staging date, if later). This is designed to be a one-off assessment at the relevant date, with no on-going requirement to monitor the proportion of active members in a given arrangement, which is likely to change over time – for instance, as people defer or transfer (see regulation 3(2)(b)); and

[35] Landscape and charges survey 2013: charges and quality in defined contribution pension schemes (RR859) – https://www.gov.uk/government/publications/defined-contribution-pension-schemes-landscape-and-charges-survey-2013.

[36] There is also an additional exclusion for the charge cap, in that it does not apply to schemes offering a third party promise in relation to money purchase benefits where there is a third party promise.

C. An arrangement into which 80% of the employer's workers who first made contributions after the relevant date are contributing. This will require trustees to monitor on an ongoing basis the proportions of members invested into the various funds used by the employer to see whether any one arrangement meets the default fund definition at any point (see regulation 3(2)(c)).

37. These policy is designed to capture existing members of qualifying schemes who were already members at the employer's staging date, where the vast majority of members are in the same investment arrangement (and therefore can be reasonably viewed not to have made an informed choice), and to capture situations where employers continue to enrol new workers into qualifying schemes which do not have a true default arrangement, and require the scheme member to make an active choice as to where their contributions are invested. This might occur where an employer contract-joins new employees before they become jobholders eligible to be automatically enrolled, and requires that they choose a fund. If an employer subsequently sets up a new arrangement for contract-joiners, this will be captured as a default arrangement at the point where 80% of more of the members who are workers of that employer are actively contributing to the arrangement.

38. We propose that where an arrangement is a default for a particular employer then all members of that arrangement who are or have been employees of the employer will continue to be covered by the charge cap as long as they remain invested in the default arrangement (except those who cease contributing before April 2015, or the employer's staging date, if later and do not resume contributing), regardless of whether they were jobholders or workers without qualifying earnings. This is covered in regulation 3(5) and regulation 4(2).

39. This meets a fundamental test of fairness, that members of the same scheme in the same organisation enrolled in the same arrangement should pay the same charges, whilst also simplifying administration of the cap for trustees and managers.

Example: Clare joined her employer's pension scheme in 2010, before automatic enrolment began; she was presented with a list of three options from which she had to choose. She selected the first on the list - Fund X - and signed and returned the membership form.

Sam was automatically enrolled two years later, in 2012, and her contributions were directed into Fund Y without her making any active choice.

When the default arrangement charge cap is introduced in April 2015, we propose that Fund Y is identified as one of the employer's default arrangements, as Sam's funds are directed into it without her exercising any choice. Clare's fund X will also be identified as a default for that employer, because at least 80% of those active members who joined before their employer's staging date and were required to choose a fund ticked this option.

If Clare were to subsequently actively choose to join Fund Y, the charge cap will apply to her as well. This meets the principle outlined above, of minimising differences in treatment between colleagues.

40. There will be some schemes in which arrangements for a particular employer are so diverse that no fund can be designated as a default in relation to that employer.

41. This may occur, for instance, where an employer has an existing scheme at their staging date, but decides to open a new scheme for the purposes of automatic enrolment. As new members were being automatically enrolled into the new scheme, it would have a default arrangement. However if the old scheme continued to be used as a qualifying scheme in respect of existing members, but there was no arrangement taking contributions from 80% or more of active members in April 2015 (or the staging date if later), the old scheme would have no default arrangement to be capped.

42. However, as set out in Chapter 2, trustee boards and Independent Governance Committees (IGCs), as part of their reporting requirements, will consider the level of costs and charges, and value for money experienced by all scheme members, regardless of the funds in which they are invested. This would include the charges in the old scheme, as well as those in the new scheme, in the example above.

Consultation question – Defining the default arrangement

Q9. Do you agree with the policy on which the draft regulations are based (see regulation 3) – to capture as many workers as possible who made no active or informed choice about their investment strategy, whilst also minimising the risk of capping funds where members made an active choice?

Transitional questions on the default arrangement

43. Stakeholders have raised with us the possibility of a situation where trustees or providers create a new charge cap compliant arrangement in advance of the application of the cap to their scheme. They have also queried whether, in such a situation, some members may opt to remain invested in their current arrangement despite the fact that it is not cap compliant. This may be because the arrangement contains benefits which members may value, such as waiver of premium or a loyalty bonus, or because they wish to remain in a particular investment strategy.

44. As explained above, where members' contributions have been redirected to a new fund or arrangement without making an active choice, then it is reasonable that this new fund should be considered a default. If, however, they have made a recent active choice to remain invested in a particular fund, despite a charge cap compliant option being on offer, we propose that the option which they have expressly chosen to remain invested in should not be classified as a default arrangement.

45. We therefore propose that, if at any time in the three month period ending with the date the charge cap applies to members of the scheme ('the relevant date') a new charge compliant default is offered to all the members who are actively contributing to such an arrangement, but some workers agree in writing to remain in their existing arrangement then the current arrangement would not be subject to the cap (see regulation 3(2)(b) and 3(3)).

46. Where this is the case, trustees and providers will need to be able to demonstrate that workers made an active choice and acknowledged that they would not be protected by the default arrangement charge cap (see regulation 3(4)).

47. Government and regulators will continue to closely monitor the communications issued to members by trustees and providers making use of this regulation, and revisit this policy, if necessary, to ensure that members are protected as intended.

48. We have re-used the example of Sam and Clare to demonstrate how this may work in practice.

Example: in January 2015, Clare is in Fund X and Sam in Fund Y. The member-borne deductions in both funds exceed the level of the default arrangement charge cap. As outlined above, if the trustees/provider and employer take no action, both will be designated default arrangement subject to the charge cap from April 2015.

The trustees/provider and employer decide to allow people the option to remain invested in Funds X and Y and open Fund Z as a new default, which will be subject to the charge cap.

They write to all active members of Funds X and Y who are workers of the employer to tell them that their contributions will be redirected to Fund Z in March 2015 if they take no further action. The letter also explains that they may actively choose to stay in Funds X and Y (and outlines the process to do so) but indicates that these funds will not be subject to the default arrangement charge cap.

Sam takes no action and her future contributions are invested in Fund Z, while Clare actively chooses to stay in Fund X. From April 2015, the default arrangement charge cap applies to Fund Z because workers' contributions are being directed into this fund by default.

If many of Clare's colleagues make the same decision as Clare and actively chose to stay in Fund X, then Fund X may still meet the 80 per cent threshold (outlined in paragraph 36) at April 2015. However, provided the trustees or provider can demonstrate that a notification was issued to all active members (who are workers of the relevant employer) of Fund X within the 3 months prior to April 2015 indicating that future contributions would be redirected to a new arrangement, unless they made an active choice to remain invested in their current arrangement, then Fund X will not be considered a default arrangement. It will not therefore be subject to the cap.

Consultation question – transitional questions on the default arrangement

Q10. Do you agree that the draft regulations (regulation 3(3)) should allow members who have made a recent active choice to remain in an arrangement which is not subject to the charge cap?

Is the 3 month time period allowed reasonable?

When the cap applies, to whom and on what funds

49. This section provides more detail on the application of the charge cap. The March Command Paper announced that the charge cap will come into force for default funds of qualifying schemes from April 2015.

50. We have continued to work with regulators and stakeholders on the detailed application of the charge cap in a number of areas, including deferred members, workers without qualifying earnings, schemes and funds which are closed to future contributions, and funds invested in the default arrangement prior to April 2015. Our proposals in relation to these aspects of implementation are covered in the following sections.

When the cap applies

51. As stated in the Command Paper, the default arrangement charge cap will apply to a qualifying scheme from the later of:

- April 2015; and
- the date from which the scheme begins to be used as a qualifying scheme.

52. The charge cap will continue to apply for as long as the member's funds remain invested in the default arrangement, including if they become a deferred member of the scheme (see regulation 3(5)).

53. Following the introduction of the new flexibilities announced in Budget 2014 , the pensions industry is developing solutions to allow individuals to access their savings in a way that suits them. Where members are able to take up the new flexibilities while remaining invested in the default arrangement of a qualifying scheme, the charge cap will continue to apply to funds in the default arrangement. However, the charge cap is designed to protect those who have been defaulted into saving without making an active choice, and schemes will be able to levy additional charges for services which members agree to in writing (see regulation 8, and the section on opt-in services below).

54. The Government and regulators will closely monitor any additional charges levied and consider policy changes if necessary to ensure that members are protected as intended.

To whom the cap applies

55. In determining those scheme members to whom the cap should apply, we have again applied the principles of protecting members who have not made an active choice, whilst supporting the roll-out of automatic enrolment through minimising the disruption to schemes and providers. We have also considered the information which will be available to trustees and providers about the members of the scheme, and the need for them to be able to make changes to, or close, in an orderly way, any schemes and arrangements which cannot be made charge compliant in advance of the measures coming into force.

56. We propose that the default arrangement charge cap will therefore apply to all members (including workers, as well as jobholders) of a given employer's scheme who actively contribute to the default arrangement at any point on or after the relevant date (the later of 6 April 2015 and the date at which that scheme is used as a qualifying scheme in relation to that employer - see regulation 4(2)). The cap will apply from the point that the first contributions after this date are received by the trustees or managers. The cap will continue to apply to these members for as long as they have funds invested in the default arrangement, including where they leave their employer or cease contributions and become a deferred member of the scheme. The cap will not apply to those members who have already ceased contributing when the charge cap is first applied to their scheme, unless they make at least one contributions after the relevant date.

> Example: in September 2014, James and Rahul are both contributing to fund J of their employer's scheme, into which they were automatically enrolled. The following month, James moves to a new job and stops contributing to his previous employer's scheme.
>
> From April 2015, the charge cap apples to active members of Fund J; as Rahul is currently paying into the default arrangement, he must not experience member-borne deductions in excess of 0.75 per cent. As James stopped contributing before the default arrangement charge cap was introduced, the cap does not apply.

57. This means that the charge cap, and other charges measures, will not apply to schemes which close to future contributions prior to April 2015, as these schemes would not be used as qualifying schemes from April 2015 (see regulation 3(1)(a)).

58. Similarly, where a default arrangement is closed to all future contributions prior to April 2015 (or ceases use as a default but remains available as a fund for members to actively select), and future contributions by members who have not made an active choice are instead directed to a new charge compliant arrangement within the same scheme, the charge cap will not apply to the old arrangement.

59. In all three cases (deferred members, closed schemes and closed arrangements), we would expect trustees and providers to give scheme members the option to transfer their funds from any old scheme or arrangement into a new charge-compliant scheme or arrangement and to make reasonable efforts to notify them of this option.

60. The Government and regulators will closely monitor the efforts made by trustees and providers to contact scheme members and offer them the options to transfer, and consider policy changes if necessary to ensure that members are protected as intended.

> **Consultation question – to whom the cap applies**
>
> Q11. Do you have any comments on the policy about protecting the members to whom the cap applies?
>
> Do you have any comments about how the draft regulations meet the policy intention?

On what funds the cap applies

61. In the case of members to whom the cap applies, we have considered whether to only apply the cap to funds accumulated from contributions made to the default arrangement after the implementation of the cap. However, if we did this it would result in members' funds being segmented into lower charging pots, from funds accumulated after the cap applies, and higher charging pots, from funds accumulated before the cap applies. Segmenting pots in this way could place a significant burden on trustees, providers and regulators to confirm compliance. Moreover, it would also provide less protection to members because a smaller pot would be covered by the cap.

62. We therefore propose that the charge cap will apply (as set out in regulation 6) to all of the member's funds in any arrangements identified as a default, irrespective of whether these contributions were made prior to or after the introduction of the cap to their scheme (subject to the requirements set out in paragraph 56 above).

Permissible charge structures

63. The Office of Fair Trading, in their 2013 DC market study, expressed concern about the lack of comparability in the workplace pensions market as a result of the variety of types of charges:

    "When stakeholder pensions were introduced in April 2001, the pensions industry moved towards levying a single charge, known as an AMC, although this has not precluded the industry from using other charges as well… despite this simplification, we remain concerned that there is insufficient visibility and comparability of charges to ensure that competition on charges is fully effective."

64. The Government shares the OFT concerns and stated in the March Command Paper that it wishes to see transparent and comparable charges across the workplace pensions market. This will allow employers and savers to make comparisons and providers to compete on cost.

65. Some workplace schemes, especially older arrangements, have charging structures with multiple elements (for instance, a monthly flat fee, plus a percentage of funds under management charge, plus also a contribution charge). Our understanding is that schemes with multiple charges are now rarely used as qualifying schemes.

66. As was noted in the March Command Paper, however, some schemes use dual combination charge structures – such as a combination of a flat fee plus a percentage of funds under management, or a charge based on a percentage of contributions plus a percentage of funds under management. These structures can help support market dynamics by allowing new schemes or providers to raise capital sooner. The March Command Paper therefore described in what circumstances dual combination charge structures could be judged as being compliant with the default arrangement charge cap, using equivalency tables.

67. Some providers have asked DWP to consider providing a methodology by which schemes with more complex charges can demonstrate compliance with the default arrangement charge cap. However the government's intention remains to permit only single or dual charging structures. Allowing a wider range of charging structures to meet the charge cap, whether temporarily or permanently, would undermine the existing trend towards simpler charges and make market-wide comparisons more difficult.

68. Consequently, the default arrangements of schemes used as qualifying schemes will need to meet the default arrangement charge cap through either a single annual charge of 0.75 per cent of members' funds under management (described in the regulations as the value of the member's rights) or lower, or by using a dual charge that is equivalent to 0.75 per cent of funds under management or lower in the DWP equivalency tables, which are set out in regulations 6(3) and 6(4).

69. Other charging structures in default arrangements of qualifying schemes are prohibited by regulation 5. Trustees of qualifying schemes currently using more complex charging structures will need to make changes to ensure that they are using a permitted charging structure in all default arrangements.

70. In response to concerns raised in our 2013 consultation on charges about 'flipping' charges structures between single and combination charge structures for financial benefit, we are also proposing to introduce a measure (regulation 5(4)) which restricts trustees to changing their charging structure at the end of each charges year (see Assessment of charges below). This limits

the opportunities for trustees to make alterations to charging structures, without indefinitely locking them into a particular structure.

Entry and exit charges

71. In the March Command Paper we stated that administrative charges associated with transfers into or out of a workplace scheme would be subject to the charge cap. We remain committed to this principle – individuals should not be subject to unfair charges as they consolidate their pension saving. We propose that any scheme that continues to use such charges should only use the permitted charge structures above (for each member within a given charges year) to ensure that no member transferring funds to, from or between default fund arrangements, is charged above the cap. In schemes using entry and exit fees, we will expect trustees and IGCs to keep charges under review and report on them as part of the new governance requirements, considering whether they represent value for money for scheme members, including charges within both default arrangements and non-default investments.

Consultation Question – Permissible charge structures

Q12. Do you have any comments on the policy intention of:

(a) imposing the cap on the total fund of the member and no just on contributions made after the relevant date?

(b) prohibiting charge structures other than those set out in paragraph 68 (and reflected in regulation 5?

(c) limiting the opportunities for altering charging structures as described above, whilst avoiding locking schemes into particular charging structures indefinitely? (regulation 5(4))

Assessment of charges

72. As with the charge cap on Stakeholder Pensions, the charge cap will apply at member level, so that no member in the employer's default arrangement may experience charges above 0.75 per cent of funds under management annually, when charged solely on the basis of a percentage of funds under management. This is made clear in regulation 4(1)(a) and regulation 6(2).

73. Where the default is actually a group or a blend of funds, charges for individual funds within the arrangement may exceed the cap as long as the overall charges for each individual member invested in the default arrangement do not exceed the charge cap.

74. For schemes using a combination charge structure, regulations 4(1)(a) and 6(1) require that the charges borne by each individual member must correspond to a permissible combination in the equivalency tables set out in regulations 6(3) and 6(4). These tables are a simpler form of the tables contained in Annex C of the March Command Paper.

75. Where a member is invested for only part of a year, the charge on funds under management and any flat fee must not exceed the cap when measured over that period of time (see regulations 2(2) and 2(3)).

76. Pension schemes use many different ways of measuring and deducting member-borne charges over different frequencies. For instance, some fund managers and life funds cancel units on a monthly or quarterly basis, whilst others make daily deductions from the unit price (the number of 'units' a person holds represents the value of their assets in a fund). Some schemes (and particularly unbundled trusts) pay for services at different intervals.

77. The default arrangement charge cap needs to be sufficiently flexible to encompass a range of existing charging practices, such as daily, monthly, and quarterly charges, whilst maintaining the principle of protecting members who have not made an active choice.

78. We therefore propose that schemes should be permitted to deduct charges at different intervals. However, the charges deducted annually must not total more than 0.75 per cent of funds under management. It is proposed that the fund value on which this calculation is based will be an average of its value, measured at a number of reference points, set at equal intervals through the year. These intervals must be no longer than three months – this is covered in regulations 7(1), (3) and (4).

79. Trustees should validate charges over the charges year. This is defined as the scheme year set out in the scheme rules, or a year starting from 6 April if none is specified (see regulation 2).

80. Provision is also made within the regulations for cases where trustees opt to change the frequency with which they calculate the fund value (regulation 7(5)), and where members are only invested in the default at one reference point during the scheme year (regulation 7(6)(a)) or at no reference points (regulation 7(6)(b)).

Consultation Question – Assessment of charges

Q13. Do you have any comments on the policy described above in relation to the valuation of the member's fund and the period over which the charge cap applies?

And do you have any comments on how the draft regulations reflect that policy (regulation 7)?

Opt-in services

81. The March Command Paper announced that we would bring forward measures to ensure that members were only defaulted into paying for services without which the scheme cannot function. Trustees and IGCs will monitor the services into which members are defaulted to ensure that they represent value for money (see paragraphs 45 to 64 of Chapter 2).

82. The March Command Paper announced that the charge cap will apply to default arrangements of qualifying schemes but members will still be able to choose alternative investment options and services that are not subject to the cap. In keeping with this principle, opt in services which members have entered into an agreement for will not be subject to the default arrangement charge cap. To provide adequate safeguards, we also propose that such agreements:

- are not a condition of becoming or remaining a member of the scheme or arrangement (regulation 8(2)(b)(i));
- must include a statement that the charges may be higher than those permitted under the charge cap (regulation 8(2)(b)(ii));
- cannot be used for services which the provider is already legally required to provide (regulation 8(3)(a)); and

- may not cover the core services provided by a scheme (regulations 8(3)(b) and 8(4)) – by which we mean, designing and implementing an investment strategy; investing members' contributions; and holding members' investments.

Consultation question – member agreement for services

Q14. Do you have any comments on the policy regarding opt-in services described above?

Do you have any comments on the draft regulation (regulation 8) which reflects that policy?

Transitional questions on workplace personal pensions and the charge cap

83. Since the publication of the Command Paper in March 2014, many providers of workplace personal pensions have begun to make adjustments to existing schemes to make them compliant ahead of April 2015. Other providers have asked us about how their existing schemes can be made compliant with the charges measures, given the presence of individual contracts with each scheme member. They have expressed concern that individual member consent might be required before charging and investment arrangements are altered to ensure compliance.

84. Our understanding is that most personal pension contracts allow significant flexibilities to alter terms and conditions, particularly in response to Government legislation or regulatory change, which should allow providers to lower charges in existing funds without explicit member consent. If, alternatively, a new charge-compliant arrangement were established to receive future contributions then again the Department is not aware of any contracts which would prevent these new contributions being redirected.

85. Contractual provisions will, however, vary between contracts and providers may interpret these differently. Providers will need to continue to examine the contract terms for each relevant scheme and ascertain what changes are needed to make a scheme compliant, including whether accumulated assets may be moved into a different fund (for example by negative affirmation, where the provider notifies the member that their assets will be moved unless they choose to opt out) following their own due diligence process.

86. We recognise that, in some cases, this may mean that previous contributions are left invested in a former default arrangement, whilst future contributions are redirected to a new charge compliant default, unless scheme members make an active decision to transfer funds over. We would expect providers to make best efforts to contact scheme members in order to facilitate such a transfer and we will continue to discuss with providers and regulators the steps that providers may take to achieve this.

Active Member Discounts

87. The Government announced in the March Command Paper that Active Member Discounts (AMDs) would be banned in qualifying schemes from April 2016 (or the employer's staging date, if later).

88. In determining the detail of the AMD ban, we have applied the principles of protecting members who have not made an active choice, whilst supporting the roll-out of automatic enrolment through minimising the disruption to existing schemes. We have considered the wide range of tiered charging structures in place in some schemes, where charges reduce once members have been invested for a given period, or the size of their pot reaches a certain threshold. We have also considered the possibility that in some circumstances charges may rise for active members and whether in these circumstances it would be fair to maintain charges at the same rate for non-contributing members. Finally we considered stakeholders' expectation about the extent of the AMD ban as set out in the March Command Paper.

89. The Government's intention is that any member who makes a contribution to a qualifying scheme[37] after April 2016 whilst a worker of the employer (regulation 10(3) and (4)) must not be charged more when they cease contributing than they would if they were still making contributions to the scheme. This is designed to ensure that members who cease contributing, whether as a result of leaving pensionable service, or whilst still in pensionable service, do not experience poor value for money.

90. From April 2015 until April 2016, any AMD structures remaining in qualifying schemes must not push charges for members who cease contributing during that period over the default arrangement charge cap of 0.75 per cent (regulation 6).

91. The ban will apply to all arrangements whereby a member's charge or an equivalent combination charge would increase on ceasing active contributions to the scheme, regardless of whether it is identified as an 'active member discount'. In the case of a scheme with a single charge as a percentage of funds under management, this means that the percentage charge levied on a non-contributing member must be no higher than if they were still a contributing member. In the case of a combination charging scheme, this means that neither the percentage charge on funds under management, nor, where relevant, the flat fee may be higher (regulation 10(1)).

92. We propose that the non-contributing member should not pay more than they would if they were a contributing member with the same number of years' contributions, the same value of funds under management, making the same level of contributions as their last contribution (regulation 10(2)).

93. Some stakeholders have asked us whether the AMD ban will prevent employers paying, or subsidising the member-borne deductions of active members. This has a similar effect to AMD structures, as the charge experienced by the member will increase if they leave that employer and stop benefiting from their subsidy.

94. The intention is that the practice of employers paying charges on behalf of their current employees will not be banned, as long as the total charge level imposed is the same for contributing and non-contributing members. If employers wish to pay some of the charges for particular members then they can continue to do so.

95. This is designed to ensure that employers are able to continue to offer this benefit to employees, while reducing the risk of members who cease contributing, whether as a result of leaving pensionable service or whilst still in pensionable services, experiencing poor value for money.

[37] In the context of the AMD ban, a qualifying scheme means any scheme which is a qualifying scheme in relation to one or more jobholders of an employer, at any date on or after 6 April 2016 (regulation 10(5)).

Consultation question – Active Member Discounts

Q15. Do you have any comments on the policy in relation to Active Member Discounts?

Do you have any comments on the draft regulation (regulation 10) which reflects this policy?

Commission and consultancy charges

96. Following a consultation on charges in October 2013, we announced in the March Command Paper:

- a ban on consultancy charge structures in all qualifying schemes (member-borne payments for advice agreed between an employer and an adviser) from April 2015;
- a ban on member-borne commission payments to an adviser in qualifying schemes from April 2016;
- between April 2015 and April 2016, any commission payments within qualifying schemes will be subject to the default arrangement charge cap.

97. New commission arrangements were banned in workplace personal pension schemes from 1 January 2013 through the Retail Distribution Review, conducted by the Financial Services Authority (now the FCA). Following this ban, consultancy charges were introduced by the FCA as an alternative means of adviser remuneration in Group Personal Pensions and Group Stakeholder Pensions.

98. DWP regulations on consultancy charges came into effect on 14 September 2013, effectively banning consultancy charges in automatic enrolment schemes (both occupational and workplace personal pension schemes), aside from where there was a legally enforceable agreement in place between an employer and third party before 10 May 2013 (when the ban was announced[38]).

99. Separately, the Office of Fair Trading's (OFT) Defined Contribution Workplace Pensions Market Study, published in September 2013, concluded that adviser commission was incompatible with the principles of automatic enrolment. The OFT drew particular attention to the fact that members could pay commission without realising, and that commission presented a significant barrier to switching. Importantly, the report highlighted the conflict of interest that commission arrangements could cause, as advisers would know in advance the income that each different recommendation could bring. The OFT pointed to similar potential conflicts of interest with regard to consultancy charges.

100. The DWP came to similar conclusions following its consultation in autumn 2013, with the March Command Paper stating that member borne charges should not be used to fund the cost of advice to employers or providers. That Command Paper announced bans on consultancy charges and commission payments in schemes that are used as qualifying schemes in April 2015 and April 2016 respectively, as described above.

101. The FCA will consult shortly on draft rules to introduce these bans in workplace personal pension schemes used as qualifying schemes from April 2015 and April 2016 respectively, as announced in the March Command Paper.

[38] The Occupational and Personal Pension Schemes (Automatic Enrolment) (Amendment) Regulations 2013 (SI 2013/2328).

102. The DWP remains committed to banning consultancy charges and commission payments in qualifying schemes. However, the structure of occupational schemes – where trustees may be one step removed from negotiations and agreements in relation to commission payments between providers or fund managers and advisers – makes designing these bans in the occupational sector more complex. The DWP, therefore, wishes to consult on the best way of designing regulations to achieve the bans. The timetable for this work is described below.

103. In workplace personal pensions the intention is that providers will be responsible for compliance with the new charges measures and the Government's understanding is that they have direct control over the commission payments to be banned. The FCA will consult shortly on relevant rules here. However, although the Department's intention is that trustees of occupational schemes will be responsible for compliance with the commission ban, they do not have similar direct control over commission payments to advisers and may not know of the existence of commission payments.

104. In designing the ban, therefore, we must be confident that trustees have sufficient information about commission payments between providers and advisers. The DWP, in conjunction with TPR and FCA, is considering what legislative mechanisms may be available to support trustees in securing this information. The Department will consult in 2015 on draft regulations to ban commission payments in occupational schemes used as qualifying schemes. The Department's intention remains that the commission ban will commence in April 2016, as announced in the March Command Paper.

105. Consultancy charges were originally created by FCA rules for workplace personal pensions, as an alternative remuneration mechanism for advisers. Government and regulators are not aware of any consultancy charges in occupational schemes and, in any case, many occupational scheme trust deeds and rules would not allow such charges. Therefore, the Department has decided not to include separate measures banning consultancy charges in occupational schemes used as qualifying schemes in this set of regulations. However, the Department intends to design the regulations to come into force in April 2016 in such a way as to ban both commission and consultancy charge payments in occupational schemes. The Department will also consider the options in relation to the existing DWP regulations effectively banning consultancy charges in automatic enrolment schemes (see paragraph 98 above).

Conclusion

106. The measures outlined in this chapter explain in detail how the DWP has moved from the core measures announced in the March command paper to the detailed, draft legislation published alongside this paper. This publication launches a consultation, including a number of specific questions, on the draft regulations which will last four weeks and close on 14 November.

Consultation question

Q16. In addition to the questions already asked, is there anything else in the policies as set out in this paper on which you have any comments?

Do you have any comments on how the draft regulations reflect the policies explained in this paper?

The regulatory approach and compliance for occupational schemes

5

- The draft regulations attached to this paper relate to governance and charges in occupational schemes and give enforcement powers to The Pensions Regulator (TPR). This chapter describes these powers and the circumstances under which TPR may use them.
- Providers of workplace personal pensions are regulated by the Financial Conduct Authority (FCA), and will be subject to equivalent rules relating to governance and charges and the FCA's enforcement regime.
- In designing the proposed compliance measures the DWP has sought to minimise the burden on trustees and schemes and to use existing processes wherever possible.
- We propose that the TPR annual scheme return notice will incorporate three additional questions. These will be used to identify the Chair of trustees, gather information on the completion of the Chair's Statement on governance standards and confirm compliance with the charges measures. In the case of non-compliance with the Chair's Statement requirement we specifically propose that TPR will issue a fine against the board of trustees, including officers of corporate trustees.
- Default funds in qualifying occupational schemes should be compliant with the charge cap from April 2015. If, from that date, trustees identify that they are unlikely to be able to ensure compliance over the charges year, then we propose providing an 'adjustment measure' to rectify that likely non-compliance. Under this measure, available only between April 2015 and October 2015, trustees must direct future contributions to a compliant fund within their scheme, or inform employers that they must find an alternative qualifying scheme. The charge cap will continue to protect members from April 2015 in such schemes.
- This chapter also introduces a proposal to cover unexpected and exceptional events where trustees[39] of occupational pension schemes may find themselves in breach of the charge cap despite their best endeavours. As per the adjustment measure, scheme members must remain protected by the charge cap during any such periods and this proposal gives trustees a route to ensure sustainable compliance with the charges measures.

[39] Where in this chapter we speak about trustees, we are also referring to managers of the scheme unless otherwise stated.

Introduction

1. The regulatory regime for workplace pensions is overseen by TPR and the FCA, with, broadly speaking, the former regulating occupational schemes and automatic enrolment compliance and the latter regulating the firms which provide workplace personal pensions. As described in the March 2014 document 'Guide to the regulation of workplace defined contribution pensions'[40], both regulators work closely with DWP on maintaining a coherent regulatory environment that maximises consistency and minimises duplication.
2. These key principles will continue to be adhered to as TPR and FCA regulate compliance with the measures contained in the Government's Better Workplace Pensions programme. These measures aim to ensure that all relevant workplace schemes offering money purchase benefits meet the minimum governance standards and that members are protected from high and unfair charges.
3. The compliance measures and regulations contained in this document relate to the charges and governance measures for occupational schemes only. The charges and governance measures for workplace personal pensions will be introduced via FCA rules.

Reporting compliance to TPR

4. We have worked with TPR to consider the best way to gather information from schemes to find out whether they are compliant with the governance and charges measures. We have sought to build on existing measures where possible and we think that the most simple and cost effective way of doing this is for schemes to report their compliance to the Regulator via the existing scheme return.
5. Trustees of pension schemes have a legal obligation to complete a scheme return on a regular basis (generally annually, though for schemes with fewer than 12 members this may be less frequent) to supply information about their scheme to TPR. Failure to complete the scheme return is a breach of the Pensions Act 2004 and could lead to trustees being fined.
6. We propose to add three further items to the list of registrable information that relevant schemes are required to send to TPR as part of their scheme return under Regulation 3 of the Register of Occupational and Pensions Schemes Regulations 2005. The first of these is the name of the scheme's Chair of trustees, as set out in Chapter 2 and regulation 15(2). The other two items are covered in regulation 23, and require relevant schemes to report:
   - Whether trustees have produced the Chair's Statement required by the governance regulations; and
   - Whether their scheme complies with the default arrangement charge cap of 0.75% of funds under management, or an equivalent amount using a combination charge structure (from April 2015), and whether it complies with the measure banning Active Member Discounts (from April 2016). When member-borne consultancy charges and commission payments are banned from April 2016 schemes will also need to report compliance with these measures.
7. Chapter 2 explains the important role the annual Chair's Statement will play in helping to drive compliance with the minimum governance standards. The Chair's Statement requires trustees to consider and report against the governance standards about default arrangement design and review, core scheme financial transactions, charges and transaction costs, as well as describing how trustee requirements for knowledge and understanding have been met.

[40] http://www.thepensionsregulator.gov.uk/docs/guide-to-the-regulation-of-workplace-defined-contribution-pensions.pdf

8. Rather than require schemes to report to the Regulator whether they have met each of these individual standards, we think that a more proportionate approach would be for schemes to report, via the scheme return to TPR, on whether or not they have produced a Chair's Statement that covers the standards covered within Chapter 2 of this Command Paper.

9. The only exceptions to this approach are the charges measures. The importance of the charge cap, including the numbers of savers within each scheme that they will impact on, means that we think trustees should separately confirm to TPR whether or not whether or not they have complied with the charges measures. We would again expect them to do this via the scheme return to the TPR.

10. Given the importance of minimum governance standards and protecting member interests, we specifically propose including in regulations the requirement, in the case of non-compliance with the Chair's Statement requirement, to issue a fine against the board of trustees of between £500 and £2,000. More details can be found in draft regulation 26(3).

Question 17

Is the scheme return the most proportionate way to obtain information on compliance with the governance standards and charges measures? Draft regulation 23 sets this out in more detail.

Question 18

Is the proposed compliance approach to the Chair's Statement, as described in draft regulations 24 and 26 appropriate and proportionate?

The charge cap

11. The March Command Paper announced a default arrangement charge cap of 0.75%, or equivalent amount using a combination charge structure, and further controls on inappropriate types of charge, to protect savers from high and unfair charges. In working with TPR and FCA on the approach to compliance with the charges measures across the workplace pensions market we have been mindful of the differences between occupational schemes and workplace personal pension schemes.

12. We have focused in particular on the differences in scheme funding between the types of scheme. Insurers, who are usually the providers of workplace personal pensions, will have financial reserves which are commonly not available to occupational schemes. Moreover, many occupational schemes have a 'closed loop' of members' funds with which to operate. Unlike defined benefit schemes, employers may not be required to put money into money purchase schemes beyond minimum required contributions, unless the scheme rules require otherwise.

13. Given this closed loop of funding, we therefore recognise that for a minority of occupational schemes that are already being used (or about to be used) by employers as qualifying schemes, compliance with the charges measures could be more difficult than for other schemes. We have therefore made provisions in the draft regulations (see regulation 9) to address this issue.

14. Where it is evident to trustees prior to April 2015 that a given arrangement will not meet the charges regulations then the arrangement should not be used as the default arrangement of a qualifying scheme. Trustees should instead close the arrangement to future contributions (as set out in paragraphs 55 to 60 of Chapter 4) and direct those future contributions to arrangements compliant with the charge cap. The only exception would relate to any members who make an active choice to continue to contribute, as explained in paragraphs 43 to 48 if Chapter 4.

15. If trustees believe that they are likely to be able to at least initially comply with the charge cap, then they may continue to accept contributions to the default arrangement after 6 April 2015. Some trustees may subsequently identify within a short period of time after April 2015, that they are unlikely to be able to meet the charge cap for members of a particular default arrangement, despite their best endeavours for the appropriate charges year. This may be, for instance, where a scheme is tied in to a contract with an external provider or supplier from which they are unable to exit quickly and without significant extra cost.

16. In this circumstance, we are proposing that trustees and managers have the option to rectify this situation and invoke an 'adjustment measure' within six months of 6 April 2015. Under this measure, trustees would still have to ensure compliance with the cap from that date, but they would initiate a process which would end with an alternative default arrangement that would be compliant with the charge cap in the long-term. The previous default arrangements would not be subject to the cap from the date at which contributions are directed into those alternative arrangements. This measure will only be available to occupational schemes between April and October 2015.

17. We propose that, in invoking the adjustment measure, trustees must follow this process:
    - If they identify that there is a risk that they may be unable to comply with the cap over the charges year, they should first use their best endeavours to become compliant.
    - If, despite those best endeavours, trustees determine that they are unlikely to be able to comply over the charges year, they must give the employer, members and the Regulator at least one month's notice of the 'adjustment date'.
    - From the 'adjustment date' trustees have two options. Either they can divert members' contributions into a compliant fund(s) within the same scheme, or they can inform the employer that they must re-enrol their jobholders into an alternative qualifying scheme that is compliant with the charges measures.
    - From the adjustment date the default arrangement closes to all future contributions and is not subject to the charge cap. If trustees decide to offer workers the option to continue contributing to that fund, then any worker agreements must be provided in writing and must come with acknowledgement that they may be subject to charges higher than those allowed under the charge cap.

18. As with arrangements which close to future contributions prior to April 2015 (or the date from which the scheme is used as a qualifying scheme, if later), we will expect trustees, wherever appropriate, to contact scheme members to facilitate a transfer from their former default arrangement to their member's new charge compliant default arrangement.

19. This is strictly a time limited measure – schemes used as qualifying schemes from October 2015 will have had sufficient time to identify the long term prospects for charge compliance and make best endeavours to renegotiate contracts, or, with the employer, make alternative arrangements for the employer's jobholders.

Question 19

Do the adjustment regulations (regulation 9(2)(a)) reflect our policy intent of providing an adjustment mechanism for occupational schemes which cannot stay compliant with the charge cap, to take action to resolve the situation promptly?

Complying with the charge cap in the light of unexpected events

20. The draft regulations also include provisions to cater for unexpected events that may push costs for occupational schemes to significantly higher levels and make charge cap compliance difficult, despite trustees' best endeavours. Such events could include a sudden fall in the value of the arrangements' assets or costly legal action against the trustees of the scheme. As above, this measure is only available to occupational schemes, due to the closed loop of their funding, and the particular vulnerabilities which this creates.

21. As with the adjustment measure described above, the trustees are able to implement an adjustment measure, which would bring the default arrangement outside the charge cap from the adjustment date. Due to the nature of the event against which the measure is intended to offer protection, there is no time limit on trustees being able to access the adjustment measure. However, once trustees have concluded that they are unlikely to be able to continue to comply with the cap, they will have a six month period to implement the adjustment measure described above in paragraph 17.

22. Again, trustees must comply with the charge cap for any period before the adjustment date, and the trustees must provide the Regulator, employers and members with one month notice of their intentions. Our intention in providing this option is that trustees should only use it in the most exceptional circumstances, and we will monitor the use of the measure, to ensure that trustees are not using it inappropriately.

23. Many trustees will not have a unilateral power under the scheme rules to close a scheme to future contributions in respect of some or all members. Because of the limited time available to take advantage of the adjustment measure option, we are providing for a statutory modification power to allow trustees to amend the scheme to implement the adjustment measure. This is an amendment to the Occupational Pension Schemes (Scheme Modification) Regulations 2006.

Question 20

Do the adjustment regulations (regulation 9(2)(b)) meet the policy intention of providing an adjustment mechanism for occupational schemes when, as a result of an unexpected event; they are unlikely to be able to comply with the cap?

Exclusion of the employer consultation duties

24. In addition, closure of the scheme to future contributions in respect of members of the default arrangement is likely in many circumstances to trigger the employer consultation duties under the Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006. Again, because of the limited time available to take advantage of the adjustment measure, we have amended these regulations to make clear that any scheme change made for the purposes of implementing an adjustment measure, is outside the scope of the employer consultation duty.

Compliance notices, penalties and reviews

25. The regulations require TPR to investigate instances of non-compliance where breaches of legislation are identified and to issue compliance notices to the board of trustees or where appropriate, a third party (such as a fund manager or provider). Regulations 24 and 25 of the compliance section of the Regulations set this process out in more detail. If TPR is of the opinion that steps in the compliance notice are not followed as designated, it must issue a penalty notice as appropriate to either the board of the trustees or a third party. We propose that the amount of the fine for any initial failure each scheme year to produce a Chair's statement is in a lower range from the range of the fine for a breach of any other charges or governance provision of the regulations or for failure to comply with a compliance notice, third party compliance notice. Regulation 26(3) refers.

26. We have also considered the scenario where TPR may be required to recover a penalty from the officers of a company where a trustee or manager is part of a corporate body. We therefore propose to give TPR a power through regulation 28 to seek payment from any director, manager, secretary or other similar officer of the body, or a person purporting to act in any such capacity.

27. Where TPR have issued a compliance notice, a penalty notice or both, we propose that the trustee or the third party has the right if in their opinion they feel the notice has been issued in error to ask for a review. Regulation 29 sets out the process for applying to TPR for a review. TPR may also initiate a review where they consider it appropriate to do so. Where a penalty notice has been issued and remains unpaid, in line with Section 42 of the Pensions Act 2008 we are introducing procedures where TPR may refer the case to the County Court for recovery. The Court would then consider ordering the enforcement of the payment into the consolidated fund of Her Majesty's Treasury. Draft regulation 27 gives further information.

Implementation timetable 6

Summary

- The Better Workplace Pensions measures are designed to protect members of workplace schemes that provide money purchase benefits[41] by tackling high and unfair charges and raising standards in scheme governance. The regulatory landscape will be updated to support these new standards.
- In addition to this DWP consultation on draft regulations, the Financial Conduct Authority (FCA) will also be consulting on draft rules to implement the charges measures shortly, ahead of them coming into force from April 2015 (and 2016 for the commission and Active Member Discounts (AMD) bans). For workplace personal pension schemes, firms will be required to set up and maintain Independent Governance Committees (IGCs) to provide oversight on behalf of scheme members. The FCA has recently completed their consultation on new rules to introduce IGCs to take effect from April 2015.
- Following these consultations, DWP will make secondary legislation, subject to Parliamentary approval, to introduce the charges and governance measures in occupational pension schemes, which will be regulated by The Pensions Regulator (TPR), while the FCA will make rules with regard to the governance and charges measures for the firms they regulate.
- DWP, TPR and FCA will continue to work closely together to ensure that compliance with these measures is maximised and that the implementation of the measures meets the policy objectives.

[41] The scope of these measures is outlined in the Chapter 1, from paragraph 11.

Introduction

1. This chapter summarises the measures contained within the Better Workplace Pensions Command Papers, confirms the implementation timetable across the range of measures and provides more detail about the approach to regulation. The section below sets out the range of Better Workplace Pensions measures and when they are due to come into force. The DWP intends to introduce those measures relating to occupational pension schemes and the FCA intend to make equivalent rules for the providers of workplace personal pensions. The timings below are subject to Parliamentary approval and FCA consultation requirements.

Governance

From April 2015:

- New minimum governance standards will be introduced across workplace money purchase pension schemes and the money purchase sections of other schemes (except where the only money purchase benefits are those provided by Additional Voluntary Contributions).
- Providers of workplace personal pensions will have new duties to establish IGCs to oversee the value delivered by the schemes they supervise, including the design and performance of the default arrangement; standards of administration; and the value of costs and charges.
- Trustees and managers of occupational schemes will have new duties to ensure that default arrangements are designed in members' interests and kept under regular review, that core financial transactions are processed promptly and accurately and that they assess the value of transaction costs and charges borne by scheme members.
- There will also be new independence requirements for master trusts who must have a minimum of three trustees, the majority of whom – including the chair – must be independent and these independent trustees will be subject to limited terms.
- Trustees must also appoint a chair who will be responsible for signing off an annual Chair's Statement on how the minimum governance standards have been met. This statement will also describe how trustees have the relevant knowledge and understanding to run the scheme effectively.

Transparency

From April 2015:

- Trustees and IGCs, as part of their duties under the minimum governance standards, must assess and report on costs and charges, including transaction costs incurred by funds.
- Through the remainder of this year and 2015, DWP will work with the FCA on appropriate regulations and rules to meet their duties under section 44 of the Pensions Act 2014 with regard to the disclosure and publication of costs and charges, including transaction costs.

Charges

2. The charge measures will apply to workplace money purchase schemes and the money purchase benefits accrued in non-money workplace purchase schemes, except for the exclusions described in paragraph 25 of Chapter 1.

From April 2015:

- A charge cap will be introduced in the default arrangements of qualifying schemes, set at 0.75 per cent of funds under management, or equivalent to 0.75 per cent for schemes with combination charge structures. This will cover all Member-Borne Deductions (MBDs), excluding transaction costs, and costs resulting from pension sharing, complying with court orders and scheme wind-up.
- Any AMD structures in qualifying schemes must not result in the level of charges faced by members who cease contributing going over the default arrangement charge cap.
- Between April 2015 and April 2016, any commission payments must be counted as Member Borne Deductions for the purposes of the charge cap.
- Member-borne payments for advice to employers – consultancy charges – in all qualifying workplace personal pension schemes will be banned from April 2015.

  The DWP intends to consult in 2015 on regulations to ban commission charges in occupational schemes used as qualifying schemes from April 2016.

From April 2016

- Member-borne adviser commission and consultancy charges will be banned from qualifying schemes.
- AMDs will be banned from qualifying schemes.

In 2017:

- The level of the default arrangement charge cap will be reviewed, to see whether a) the level should be lowered and b) whether it should include some or all transaction costs.

The path to April 2015

3. The provisional timetable for the next steps is as follows:

   - **October-November 2014** – DWP consultation (covered in this document) on draft secondary legislation relating to the charges and governance measures as they apply to occupational schemes but not including draft commission ban regulations, which we will consult on in early 2015.
   - **Late autumn** – FCA consultation on rules to introduce and enforce the charges measures for workplace personal pensions, as described in the March Command Paper.
   - **Early 2015** – Regulations laid in Parliament for the charges and governance measures as they apply to occupational schemes.
   - **Early in the New Year** – FCA publish a policy statement on IGCs.
   - **Early in the New Year** – FCA publish a policy statement on the charges measures.

- **April 2015** – DWP secondary legislation and FCA rules come into force, subject to Parliamentary approval and FCA consultations (with the ban on commission and Active Member Discounts which come into force from April 2016).

4. This timetable will help stakeholders understand how the legislative approach will work. It should also help trustees, providers and employers understand more about how the Government intends to design these measures, taking into account the responses we receive from our consultations, the regulations and FCA rules that come into force from April 2015 and 2016. Several providers have already described their plans to offer schemes compliant with the charges measures in time for April 2015 and are already speaking with employers about what adjustments may be needed to comply with the measures. Given the lead-in times for adjustments to pension schemes, those running schemes, including trustees, managers and providers, should be considering now how they might comply once the regulations and rules are finalised. The Government will continue discussions with industry and regulatory bodies to see what information those running pension schemes need during 2014 and into 2015.

Annex A
Consultation on draft governance and charges regulations and how to respond

Introduction

This consultation seeks views on draft regulations that will support the implementation of a range of measures aimed at protecting members of workplace schemes offering money purchase benefits, critical in an environment where 8 to 9 million people will have been defaulted into workplace saving by 2018. The draft regulations – The Occupational Pension Schemes (Charges and Governance) Regulations 2015 – are attached at Annex C.

This Command Paper sets out in chapters 1 to 5 the Government's policies and objectives and how these are reflected in the regulations. There are specific questions included in the chapters that primarily ask respondents for their view on how well the draft regulations meet the Government's policy intentions.

About this consultation

Who is this consultation aimed at
We welcome comments from those involved in designing and running pension schemes, pension industry professionals and advisers, pension scheme members, consumer groups and member representative organisations, and anyone with an interest in pensions.

Scope of consultation
This consultation applies to England, Wales and Scotland.

Duration of consultation
The consultation period begins on 17 October 2014 and runs until 14 November 2014. Please ensure your response reaches us by that date as any replies received after this may not be taken into account.

How to respond to this consultation or raise queries about its content
Please send your consultation responses to:

Private Pensions Policy and Analysis
Department for Work and Pensions
1st Floor, Caxton House
6-12 Tothill Street
London
SW1H 9NA

Email: reinvigorating.pensions@dwp.gsi.gov.uk

Please ensure you response reaches us by **14 November 2014**.

When responding, please state whether you are doing so as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make it clear who the organisation is, and where applicable, how the views of members were assembled. We will acknowledge your response.

How we consult

Freedom of information
The information you send us may need to be passed to colleagues within the Department for Work and Pensions, published in a summary of responses received and referred to in the published consultation report.

All information contained in your response, including personal information, may be subject to publication or disclosure if requested under the Freedom of Information Act 2000. By providing personal information for the purposes of the public consultation exercise, it is understood that you consent to its disclosure and publication. If this is not the case, you should limit any personal information provided, or remove it completely. If you want the information in your response to the consultation to be kept confidential, you should explain why as part of your response, although we cannot guarantee to do this.

To find out more about the general principles of Freedom of Information and how it is applied within DWP, please contact:

[Central Freedom of Information Team Caxton House 6-12 Tothill Street London SW1H 9NA
Email: Freedom-of-information-request@dwp.gsi.gov.uk]

The Central Freedom of Information team cannot advise on specific consultation exercises, only on Freedom of Information issues. More information about the Freedom of Information Act can be found at https://www.gov.uk/make-a-freedom-of-information-request

Consultation principles

This consultation is being conducted in line with the Government's Consultation Principles, which were introduced on 17 July 2012, and have been recently updated. The revised Principles are at:

[https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/255180/Consultation-Principles-Oct-2013.pdf]

The key principles are:

- departments will follow a range of timescales rather than defaulting to a 12-week period, particularly where extensive engagement has occurred before
- departments will need to give more thought to how they engage with and use real discussion with affected parties and experts as well as the expertise of civil service learning to make well informed decisions
- departments should explain what responses they have received and how these have been used in formulating policy
- consultation should be 'digital by default', but other forms should be used where these are needed to reach the groups affected by a policy
- the principles of the Compact between government and the voluntary and community sector will continue to be respected.

Feedback on the consultation process

We value your feedback on how well we consult. If you have any comments on the process of this consultation (as opposed to the issues raised) please contact our Consultation Coordinator:

[Elias Koufou DWP Consultation Coordinator 2nd Floor Caxton House Tothill Street London SW1H 9NA Phone: 020 7449 7439 Email: elias.koufou@dwp.gsi.gov.uk]

In particular, please tell us if you feel that the consultation does not satisfy the consultation criteria. Please also make any suggestions as to how the process of consultation could be improved further.

If you have any requirements that we need to meet to enable you to comment, please let us know.

List of Consultation questions

Q1. a) Does the definition of "relevant scheme" (regulation 2) meet the policy intention of protecting members of schemes used for automatic enrolment from high and unfair charges?

b) Does the definition of "relevant scheme" at (regulation 13) meet the policy intention of ensuring that workplace schemes are well governed in members' interests?

Q2. Do the draft regulations (regulations 4(3) and 4(4)) meet the policy intention of excluding from the charge cap members of qualifying schemes who have the advantage of a third party promise?

Q3. Do the regulations achieve the policy intention of protecting against trustees being restricted to particular service providers, while allowing employers to set appropriate parameters around investments?

Q4. Do the regulations adequately describe professional trustees?

Q5. Does the definition at regulation 1(2) capture those schemes described as master trusts in chapter 2?

Q6. Do the draft regulations meet our policy intention of ensuring that occupational schemes are well-governed?

Q7: Do you have any comments regarding the policy on who should have the duty of compliance with the charges measures?

Do you have any comments about how the draft regulation (regulation 4) meets the policy intention?)

Q8. Do you have any comments on the policy regarding the member borne deductions that fall within the cap, and how the draft regulations reflect the policy intention? These exclusions are:

(a) the non-recurring variable transaction costs which are incurred by a scheme when buying, selling, lending and borrowing underlying investments (“transaction costs” definition in regulation 2)

(b) pension sharing and compliance with court orders (“charges” definition in regulation 2)

(c) winding up costs (“winding up costs” definition in regulation 2)

Q9. Do you agree with the policy on which the draft regulations are based (see regulation 3) – to capture as many workers as possible who made no active or informed choice about their investment strategy, whilst also minimising the risk of capping funds where members made an active choice?

Q10. Do you agree that the draft regulations (regulation 3(3)) should allow members who have made a recent active choice to remain in an arrangement which is not subject to the charge cap?

Is the 3 month time period allowed reasonable?

Q11. Do you have any comments on the policy about protecting the members to whom the cap applies?

Do you have any comments about how the draft regulations meet the policy intention?

Q12. Do you have any comments on the policy intention of:

(a) imposing the cap on the total fund of the member and no just on contributions made after the relevant date?

(b) prohibiting charge structures other than those set out in paragraph 68 (and reflected in regulation 5?

(c) limiting the opportunities for altering charging structures as described above, whilst avoiding locking schemes into particular charging structures indefinitely? (regulation 5(4))

Q13. Do you have any comments on the policy described above in relation to the valuation of the member’s fund and the period over which the charge cap applies?

And do you have any comments on how the draft regulations reflect that policy (regulation 7)?

Q14. Do you have any comments on the policy regarding opt-in services described above?

Do you have any comments on the draft regulation (regulation 8) which reflects that policy?

Q15. Do you have any comments on the policy in relation to Active Member Discounts?

Do you have any comments on the draft regulation (regulation 10) which reflects this policy?

Q16. In addition to the questions already asked, is there anything else in the policies as set out in this paper on which you have any comments?

Do you have any comments on how the draft regulations reflect the policies explained in this paper?

Q17. Is the scheme return the most proportionate way to obtain information on compliance with the governance standards and charges measures? Draft regulation 23 sets this out in more detail.

Q18. Is the proposed compliance approach to the Chair's Statement, as described in draft regulations 24 and 26 appropriate and proportionate?

Q19. Do the adjustment regulations (regulation 9(2)(a)) reflect our policy intent of providing an adjustment mechanism for occupational schemes which cannot stay compliant with the charge cap, to take action to resolve the situation promptly?

Q20. Do the adjustment regulations (regulation 9(2)(b)) meet the policy intention of providing an adjustment mechanism for occupational schemes when, as a result of an unexpected event; they are unlikely to be able to comply with the cap?

Annex B
Non-exhaustive list of examples of costs and charges which we would expect to be included and excluded

In scope of the default fund charge cap on MBD: **all member-borne deductions relating to scheme and investment administration paid to the pension provider or another third party**
Set-up fees
Scheme-level entry fees; both on entry into, or on transferring a pre-existing pot into, the scheme
Scheme-level exit charges
Fees for non member-initiated switching of funds
Fees paid to governance bodies, e.g. trustees, IGCs and others
Governance charges and expenses, e.g. trustee insurance
Fund or investment management fee, payments to investment consultants and administrators, including underlying and separate in-house fund managers, performance fees etc
Ongoing charges for underlying funds in investment portfolio, e.g. fee for holding units in a UCITS fund
Ongoing costs for running of scheme, e.g. IT, office and staffing costs, data management and record keeping
Registration and regulatory costs and fees
Payments to providers of professional services and other third parties or fees for related services, e.g. administrators, advisers, actuaries, lawyers, auditors, audit and legal fees for investment, accounting fees, valuation services
Depositary fees and fees to the custody bank
Banking fees

Costs of member communication services, e.g. statement costs, website, printing/ posting accounts
Costs of capital requirements
Unrecoverable VAT
Payments to shareholder service providers
Platform fees
Commission (pending ban from April 2016)

Excluded from the default fund charge cap on MBD: **transaction costs – the variable costs associated with buying, selling, lending and borrowing the underlying investment instrument**
Brokerage commission and fees
Soft commission services included in brokerage fees, e.g. research costs
Transaction taxes, e.g. stamp duty and non-reclaimable withholding taxes on dividends
Spreads, e.g. bid-offer on bonds, FX (and associated costs such as commission)
Other charges embedded in the transaction price, e.g. payments incurred through financial derivative instruments
Deductions of expenses or fees from profits such that they are not shared equally with members, e.g. in relation to activities such as stocklending, interest income, foreign currency exchange

Annex C
Draft Occupational Pension Schemes (Charges and Governance) Regulations 2015

Draft Regulations laid before Parliament under section 54(2)(e) and (f) of the Pensions Act 2014, for approval by resolution of each House of Parliament.

D R A F T   S T A T U T O R Y   I N S T R U M E N T S

2015 No.

PENSIONS

The Occupational Pension Schemes (Charges and Governance) Regulations 2015

Made - - - - ***

Coming into force in accordance with regulation 1

The Secretary of State for Work and Pensions, in exercise of the powers conferred by sections 113(1), 181(1) and 182(2) and (3) of the Pension Schemes Act 1993([42]), sections 36(1) and (1A), 47(6)(a), 68(2)(e), 124(1) and 174(2) and (3) of the Pensions Act 1995([43]), sections 1(5), 8(1) and 83(4)(a) of the Welfare Reform and Pensions Act 1999([44]), sections 60(2)(h), 259(1), 315 and 318(1) of the Pensions Act 2004([45]) and sections 43 and 54(5) and (6) of, and paragraphs 1(1), (2)(a), (3) and (5), 2(1) to (3) and (5), 6 and 7 of

(42) 1993 c. 48. Section 113(1) was amended by the Child Support, Pensions and Social Security Act 2000 (c. 19), section 52(1). Section 181(1) is cited for the meaning it gives to "regulations".

(43) 1995 c. 26 ("the 1995 Act"). Subsections (1) and (1A) of section 36 were substituted by the Pensions Act 2004 (c. 35) ("the 2004 Act"), section 245(2). Section 124(1) is cited for the meaning it gives to "regulations".

(44) 1999 c. 30. Section 1(5) was amended by the 2004 Act, section 285(3). Section 8(1) is cited for the meaning it gives to "prescribed".

(45) 2004 c. 35. Section 318(1) is cited for the meaning it gives to "prescribed".

Schedule 18 to, the Pensions Act 2014([46]), makes the following Regulations.

In accordance with section 185(1) of the Pension Schemes Act 1993[47], section 120(1) of the Pensions Act 1995, section 317(1) of the Pensions Act 2004 and paragraph 8 of Schedule 18 to the Pensions Act 2014, the Secretary of State has consulted such persons as the Secretary of State considers appropriate.

A draft of these Regulations has been laid before and approved by a resolution of each House of Parliament in accordance with section 54(2)(e) and (f) of the Pensions Act 2014.

PART 1

INTRODUCTION

Citation and commencement

1.—(1) These Regulations may be cited as the Occupational Pension Schemes (Charges and Governance) Regulations 2015.

(2) Subject to paragraph (3), these Regulations come into force on 6th April 2015.

(3) Regulation 10 and the words "with the exception of regulation 10" in regulation 4(2) come into force on 6th April 2016.

Interpretation

2.—(1) In these Regulations—

"the 1995 Act" means the Pensions Act 1995;

"the 2008 Act" means the Pensions Act 2008([48]);

"the Administration Regulations" means the Occupational Pension Schemes (Scheme Administration) Regulations 1996([49]);

"the Investment Regulations" means the Occupational Pension Schemes (Investment) Regulations 2005([50]);

"annually" means per charges year;

"charges" means administration charges([51]) other than—

(a) transaction costs;

(b) where an order of the court provides for the recovery by the trustees or managers of costs incurred in complying with the order, the amount of those costs;

(c) charges permitted by regulations made under section 24 or 41 (charges in respect of pension sharing costs) of the Welfare Reform and Pensions Act 1999([52]);

(46) 2014 c. 19.
(47) Section 185(1) was amended by the 1995 Act, sections 122, 151 and 177 and Schedule 3, paragraph 46, Schedule 5, paragraph 80(a), (d) and (f) and Schedule 7, Part 1.
(48) 2008 c. 30.
(49) S.I. 1996/1715.
(50) S.I. 2005/3378.
(51) "Administration charge" is defined in paragraph 1(5) of Schedule 18 to the Pensions Act 2014 (c. 19).
(52) Section 24 was amended by the Family Law Act 1996 (c. 27), section 66 and Schedule 8, paragraph 43A (subject to savings as to which see section 66(2) and Schedule 9, paragraph 5 of that Act) and the Civil Partnership Act 2004 (c. 33), section 261(1) and (4), Schedule 27, paragraph 158(1) to (2) and Schedule 30.

(d) winding up costs;

"charges year" means a year specified for the purposes of the scheme in any scheme document or, if no such year is specified, a period of 12 months commencing on 6th April;

"contributing member" is a member of a pension scheme in relation to whom a contribution is being made to that scheme;

"contribution" in relation to a member, means a contribution paid by, or on behalf of or in respect of that member;

"contribution percentage charge" has the meaning given in regulation 5(3);

"default arrangement" has the meaning given in regulation 3;

"employer" has the meaning given in section 99 of the 2008 Act([53]);

"executive pension scheme" means a scheme—

(a) in relation to which a company is the only employer and the sole trustee; and

(b) the members of which are either current or former directors of the company and include at least one third of the current directors;

"existing rights charge" has the meaning given in regulation 5(2);

"flat fee charge" has the meaning given in regulation 5(3);

"jobholder" has the meaning given in section 99 of the 2008 Act;

"qualifying scheme" has the meaning given in section 99 of the 2008 Act;

"relevant scheme", for the purposes of paragraph 1(5) of Schedule 18 to the Pensions Act 2014, means, unless the context provides otherwise, an occupational pension scheme—

(c) under which all the benefits which may be provided are money purchase benefits; or

(d) which provides money purchase benefits, in relation to those benefits,

other than an executive pension scheme or a relevant small scheme;

"relevant small scheme" means a scheme with fewer than 12 members, where—

(e) all the members are trustees of the scheme and either—

(i) the provisions of the scheme provide that any decision made by the trustees is made by the unanimous agreement of the trustees who are members of the scheme; or

(ii) the scheme has a trustee who is independent in relation to the scheme for the purposes of section 23 of the 1995 Act([54]) (power to appoint independent trustees), and is registered in the register maintained by the Authority (as defined in that Act)([55]) in accordance with regulations made under subsection (4) of that section; or

(f) all the members are directors of a company which is the sole trustee of the scheme and either—

([53]) There are amendments to section 99 which are not relevant to these Regulations.
([54]) Section 23 was substituted by the 2004 Act, section 36(3).
([55]) See section 124(1) of the 1995 Act, substituted by the 2004 Act, section 7(2)(b).

(i) the provisions of the scheme provide that any decision made by the company in its capacity as a trustee is made by the unanimous agreement of the directors who are members of the scheme; or

(ii) one of the directors of the company is independent in relation to the scheme for the purposes of section 23 of the 1995 Act and is registered in the register maintained by the Authority (as defined in that Act) in accordance with regulations made under subsection (4) of that section;

"transaction costs" means the costs incurred as a result of the buying, selling, lending and borrowing of investments;

"winding up costs" means the costs of winding up the pension scheme including (but not limited to) the cost of —

(g) legal advice;

(h) tracing, consulting and communicating with members;

(i) advice on exiting investments; and

(j) selection of an alternative scheme or investments;

"worker" has the meaning given in section 99 of the 2008 Act;

"writing"' includes by electronic communication and 'electronic communication' has the meaning given in section 15(1) of the Electronic Communications Act 2000([56]).

(2) Where, in these Regulations, the circumstances require one or more of the calculations listed in paragraph (3) to be made in relation to a period of less than a charges year, that calculation shall be done on a pro rata basis.

(3) The calculations referred to in paragraph (2) are—

(a) a charge under a single charge structure, as defined in regulation 5(2);

(b) a flat fee charge, as defined in regulation 5(3);

(c) an existing rights charge, as defined in regulation 5(3).

Default arrangement

3.—(1) A "default arrangement", in relation to an employer, means an arrangement which,—

(a) on or after the relevant date is used by a qualifying scheme in relation to one or more relevant jobholders; and

(b) satisfies one or more of the descriptions in paragraph (2).

(2) The descriptions referred to in paragraph (1) are—

(a) an arrangement under which the contributions of one or more workers are allocated to a fund or funds where those workers have not expressed a choice as to where those contributions are allocated;

[56] 2000 (c. 7). Section 15(1) was amended by the Communications Act 2003 (c. 21), section 406(1) and Schedule 17, paragraph 158.

(b) subject to paragraph (3), an arrangement which, on the relevant date, was an arrangement under which the contributions of 80% or more of the workers who were contributing members of the scheme on that date were allocated where those workers were required to make a choice as to where their contributions were allocated;

(c) an arrangement under which the contributions of 80% or more of workers who are contributing members of the scheme and who first made contributions after the relevant date are allocated, where those workers were required to make a choice as to where their contributions are allocated.

(3) An arrangement does not satisfy the description in paragraph (2)(b) if, at any time in the 3 months before the relevant date,—

(a) each worker whose contributions were allocated under that arrangement ('the original arrangement') at that time was informed that contributions payable after the relevant date would be allocated under a default arrangement satisfying the description in paragraph (2)(a) ('the new arrangement') unless the worker agreed that allocation of that worker's contributions under the original arrangement should continue; and

(b) in the event that a worker did not agree that allocation of that worker's contributions to the original arrangement should continue, that worker's contributions payable after the relevant date were allocated to the new arrangement.

(4) A worker's agreement, referred to in paragraph (3)(a), must—

(a) be in writing; and

(b) include a statement that the worker acknowledges that charges under the original agreement may be higher than the charges permitted under these Regulations.

(5) Where an arrangement is a default arrangement in relation to an employer by virtue of paragraphs (1) and (2), it continues to be such an arrangement regardless of whether it continues to satisfy those paragraphs.

(6) In this regulation—

"arrangement" means an allocation of contributions to —

(a) an investment; or

(b) more than one investment according to a strategy;

"relevant date" means the date referred to in regulation 1(2) or, if later, the employer's staging date;

"relevant jobholder" means a jobholder of the employer referred to in paragraph (1);

"staging date" means the date on which sections 2 to 9 of the 2008 Act([57]) first apply to the employer; and

"worker" means a worker of the employer referred to in paragraph (1).

[57] Section 2 was amended by the Pensions Act 2011 (c. 19) ("the 2011 Act"), section 4. Section 3 was amended by the 2011 Act, sections 5 and 6, and S.I. 2012/1506, S.I. 2013/667 and S.I. 2014/623. Section 4 was substituted by the 2011 Act, section 6(2). Section 5 was amended by the 2011 Act, sections 4, 5 and 6, the Pensions Act 2014, sections 37 and 38 and S.I. 2012/1506, S.I. 2013/667 and S.I. 2014/623. Section 6 was amended by the 2011 Act, sections 4,6 and 7. Section 7 was amended by the 2011 Act, section 6.

PART 2
RESTRICTIONS ON CHARGES

Restrictions on charges

4.—(1) Subject to regulations 8 and 9, the trustees or managers of a relevant scheme must not impose or permit to be imposed on a member of that scheme to whom this Part applies charges which —

(a) exceed the limits specified in this Part; or

(b) are of a description prohibited by this Part.

(2) With the exception of regulation 10, this Part applies—

(a) to a member of a relevant scheme to the extent of the value of his or her rights under a default arrangement in relation to his or her employer;

and

(b) beginning with the date the first contribution to the default arrangement referred to in sub-paragraph (a) is received by the trustees or managers after the date this regulation comes into force.

(3) A relevant scheme, for the purposes of paragraph (1)(a), does not include a scheme which provides for there to be a third party promise about the rate or amount of any benefit at a time before the benefit comes into payment.

(4) For the purposes of paragraph (3), a scheme provides for there to be a third party promise if it-

(a) requires a promise to be obtained from a third party; or

(b) provides for the member to be given the option of requiring a promise to be obtained from a third party (whether or not the option is subject to conditions).

Prohibited charge structures

5.—(1) It is prohibited for the purposes of regulation 4(1)(b) to impose or permit to be imposed on a member of a relevant scheme to whom this Part applies charges under a charge structure other than—

(a) a single charge structure; or

(b) a combination charge structure.

(2) In these Regulations, a single charge structure is one under which the charges imposed on the member are calculated solely by reference to the value of the member's rights under the scheme.

(3) In these Regulations, a combination charge structure is one under which charges are calculated by reference to the value of the member's rights under the scheme ('an existing rights charge') and either-

(a) calculated as a percentage of the value of contributions ('a contribution percentage charge'); or

(b) charges for a period of time which are not calculated by reference to contributions or by reference to the value of a member's rights under the scheme ('a flat fee charge').

(4) It is prohibited for the purposes of regulation 4(1)(b) to change, during a charges year,—

(a) the charge structure; or

(b) the type of combination charge structure,

that applies to a member.

Limits on charges

6.—(1) The limits on charges for the purposes of regulation 4(1)(a) are the limits specified in this regulation and are calculated in accordance with regulation 7.

(2) The limit in relation to a single charge structure is 0.75% annually of the value of the member's rights under the default arrangement.

(3) The limit in the case of a combination charge structure whose charges fall within regulation 5(3)(a) is —

(a) in relation to the contribution percentage charge, 2.5% of the contributions allocated under the default arrangement —

(i) annually or,

(ii) where the member is a member for less than a charges year, in that period; and

(b) in relation to the existing rights charge, the percentage annually of the value of the member's rights under the default arrangement which is the figure in Column 2 of the following table which corresponds to the contribution percentage charge rate in Column 1 of that table which is imposed on the member.

Column 1 **Contribution percentage charge rate (%)**	**Column 2** **Existing rights charge rate (%)**
1 or lower	0.6
Higher than 1 but no higher than 2	0.5
Higher than 2 but no higher than 2.5	0.4

(4) The limit in the case of a combination charge structure whose charges fall within regulation 5(3)(b) is—

(a) in relation to the flat fee charge, £25 annually; and

(b) in relation to the existing rights charge, the percentage annually of the value of the member's rights under the default arrangement which is the figure in Column 2 of the following table which corresponds to the annual flat fee charge in Column 1 of that table which is imposed on that member.

Column 1 **Flat fee charge (£)**	**Column 2** **Existing rights charge rate (%)**
10 or less	0.6
More than 10 but no more than 20	0.5
More than 20 but no more than 25	0.4

Assessment of charges

7.—(1) Subject to paragraph (6), the limit of permitted charges under—

(a) a single charge structure; or

(b) an existing rights charge in a combination charge structure,

is exceeded if the charges imposed on the member annually exceed the average of the reference point values multiplied by the applicable percentage.

(2) The applicable percentage is—

(a) in the case of a single charge structure, 0.75%; and

(b) in the case of an existing rights charge in a combination charge structure, the percentage in Column 2 of the table in regulation 6(3) or (4), as the case may be.

(3) A reference point value is the value of the member's rights under the default arrangement calculated at each reference point.

(4) Reference points must be at equal intervals throughout the charges year, subject to paragraphs (5) and (6), and those intervals must be—

(a) of no more than 3 months; and

(b) chosen by the trustees or managers of the relevant scheme.

(5) Where the trustees or managers wish to change the interval chosen for the purposes of paragraph (4) the new valuation period must commence on the day following the final day of the last valuation period.

(6) Where a member joins or leaves the scheme at a point at which—

(a) only one reference point has occurred in a charges year, the charges are calculated by multiplying the reference point value by the applicable percentage;

(b) no reference point has occurred in a charges year, the charges are calculated by multiplying the value of the member's rights in the default fund on the member's final day as a member of the scheme or, where the member is a member on the final day of the charges year, on that day, by the applicable percentage.

(7) In this regulation monthly intervals are to be treated as equal intervals.

(8) In this regulation "valuation period" means the period since the last reference point.

Member agreement for services

8.—(1) Subject to paragraph (3), the restrictions in regulation 4 do not apply in relation to a service for which the member has entered into an agreement with a person for the provision of that service, provided the conditions in paragraph (2) are satisfied.

(2) The conditions referred to in paragraph (1) are that the agreement must—

(a) be in writing; and

(b) include a statement that entering into the agreement—

(i) is not a condition of—

(aa) becoming or remaining a member of a relevant scheme;

(bb) the member's contributions being allocated under a default arrangement; and

(ii) will incur charges at the agreed rate and that such charges may be higher than the charges permitted under these Regulations.

(3) This regulation does not apply to ah service which —

(a) the provider of that service is under a statutory obligation to provide; or

(b) is a core service.

(4) In this regulation "core service" includes (but is not limited to)—

(a) designing and implementing an investment strategy;

(b) investment of contributions to the scheme;

(c) holding investments relating to scheme members;

(d) a transfer out of a default arrangement into a different arrangement, fund or scheme; or

(e) a transfer into a default arrangement.

Charge limits adjustment

9.—(1) The charge limits do not apply, on or after the adjustment date, to a member of a relevant scheme whose contributions are allocated to a default arrangement, in the circumstances set out in paragraph (2), if the conditions in paragraph (3) are met.

(2) The circumstances for the purposes of paragraph (1) are –

(a) the trustees or managers have used their best endeavours to comply with the charge limits for the current or the following charges year in relation to one or more members of the default arrangement referred to in paragraph (1) but have determined that they are unlikely to be able to comply with those limits; or

(b) an event happens which is outside the control of the trustees or managers, and the trustees or managers have used their best endeavours to mitigate the effect of the event on the scheme but they have determined that, because of that event, they are unlikely to be able to comply with the charges limits for the current or the following charges year in relation to one or more members of the default arrangement.

(3) The conditions referred to in paragraph (1) are that –

(a) the trustees or managers have elected to implement an adjustment measure in relation to the default arrangement beginning with the adjustment date;

(b) the trustees or managers have informed the persons listed in paragraph (4), at least one month before the adjustment date–

(i) that the trustees or managers have determined that they are unlikely to be able to comply with the charge limits, in relation to one or more members of the default arrangement, for the current or following charges year, as applicable;

(ii) of the adjustment measure that will be implemented on the adjustment date, and

(iii) that the charge limits will no longer apply to members of the default arrangement on or after the adjustment date; and

(c) where the adjustment measure chosen by the trustees or managers includes the option for members to expressly agree that the allocation of their contributions under the default arrangement should continue after the adjustment date, the trustees or managers have –

(i) informed the members described in paragraph (4)(b) of that option; and

(ii) explained the process for giving of that agreement, which must –

(aa) be in writing; and

(bb) include a statement that the member acknowledges that charges under the default arrangement may be higher than the charges permitted under these Regulations.

(4) The persons referred to in paragraph (3)(b) are –

(a) the employer whose workers are members of the default arrangement;

(b) members of the default arrangement whose contributions have been allocated to the default arrangement in the 12 month period ending with the date of the determination in paragraph (3)(b), as applicable; and

(c) the Regulator.

(5) The "adjustment date" means the date chosen by the trustees or managers on which the adjustment measure is to begin, and –

(a) if the circumstances in paragraph (2)(a) apply, must be a date falling within a period of 6 months beginning with the date this regulation comes into force; or

(b) if the circumstances in paragraph (2)(b) apply, must be a date falling within a period of 6 months beginning with the date that the trustees or managers make the determination described in that paragraph.

(6) The "adjustment measure" means a measure where –

(a) the scheme will no longer allocate contributions in respect of members of the default arrangement to that default arrangement, and will not accept any new members, into the default arrangement; or

(b) the scheme will no longer allocate contributions in respect of members of the default arrangement to that default arrangement, unless a member has agreed that the allocation of his or her contributions under the default arrangement should continue after the adjustment date, and will not accept any new members, into the default arrangement.

(7) In this regulation, “charges limits” means the provisions of regulation 4(1)(a) and regulation 6.

Non-contributing members

10.—(1) It is prohibited for the purposes of regulation 4(1)(b) to impose or permit to be imposed on a non-contributing member to whom this regulation applies a higher—

(a) rate of charges under a single charge structure, contribution percentage charge or existing rights charge; or

(b) amount of charges in the case of a flat fee charge,

than that to which he or she would have been subject if he or she were a contributing member.

(2) In paragraph (1), the comparison is to be made on the basis of—

(a) the period for which the member had contributed to the scheme on the date of his or her last contribution;

(b) the value of the member’s rights under the scheme on the date the charges are imposed; and

(c) the value of the last contribution made by the member.

(3) This regulation applies to a member of a relevant scheme provided that—

(a) a contribution in relation to that member has been made to that scheme on or after the date this regulation comes into force; and

(b) at least one contribution referred to in (a) was made when the member was a worker of the employer in relation to whose jobholders the scheme is a qualifying scheme.

(4) This regulation applies to a member beginning with the date the first contribution satisfying paragraph (3)(a) and (b) is received by the trustees or managers.

(5) In this regulation-

“non-contributing member” means a member who is not a contributing member; and

“relevant scheme” is a scheme satisfying the definition in regulation 2(1) which is a qualifying scheme for at least one jobholder of the member’s employer.

Amendment of the Stakeholder Pension Schemes Regulations 2000

11.—(1) The Stakeholder Pension Schemes Regulations 2000([58]) are amended as follows.

(2) In regulation 1(3)([59]), insert in the appropriate place alphabetically-

“”default arrangement” has the meaning given by the FCA Handbook;”;

“”workplace pension contributions” has the meaning given by the FCA Handbook.”.

(58) S.I. 2000/1403.

(59) The definition of “the FCA Handbook” was substituted for the definition of “the FSA Handbook” by S.I. 2013/472. The definition of “the FSA Handbook” was inserted by S.I. 2005/577.

(3) In regulation 13([60]), after paragraph (4) insert-

"(5) This regulation and regulations 14 to 14C([61]) do not apply in the circumstances set out in regulation 14D.".

(4) After regulation 14C insert-

"Disapplication of regulations 13 to 14C in certain circumstances

14D. (1) The circumstances referred to in regulation 13(5) are as follows.

(2) In relation to a member of a stakeholder pension scheme that is a personal pension scheme the circumstances are that-

(a) the scheme is a qualifying scheme in relation to an employer; and

(b) the member's workplace pension contributions are allocated under a default arrangement.

(3) In relation to a member of a stakeholder pension scheme that is an occupational pension scheme, the circumstances are that Part 2 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015 applies.".

Amendments of other regulations

12.—(1) In regulation 10(1) of the Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendments) Regulations 2006([62]), after sub-paragraph (a) insert—

"(aa) is made for the purposes of implementing an adjustment measure within regulation 9 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015.".

(2) After regulation 7A of the Occupational Pension Schemes (Scheme Modification) Regulations 2006([63]) insert—

"7B. The trustees of a trust scheme may by resolution amend the scheme for the purposes of implementing an adjustment measure within regulation 9 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015.".

PART 3

CHAPTER 1

GOVERNANCE OF RELEVANT SCHEMES

Definition of "relevant scheme"

13. The Administration Regulations are amended as follows—

(a) in regulation 1(2) (interpretation) insert in the appropriate place alphabetically—

(60) Regulation 13 was amended by S.I. 2001/934, S.I. 2005/577 and S.I. 2011/246.
(61) Regulations 14, 14A, 14B and 14C were substituted by S.I. 2005/577. Regulation 14, as substituted, was amended by S.I. 2007/814 and S.I. 2013/459.
(62) S.I. 2006/349.
(63) S.I. 2006/759.

““relevant scheme” means an occupational pension scheme which provides money purchase benefits([64]) other than—

(a) an executive pension scheme;

(b) a relevant small scheme;

(c) a scheme that does not fall within paragraph 1 of Schedule 1 (description of schemes) to the Occupational Pension Schemes (Disclosure of Information) Regulations 2013([65]);

(d) a public service pension scheme([66]) which—

(i) falls within regulation 4(2) of those Regulations (limitations on application to certain public service pension schemes); or

(ii) does not fall within regulation 4(2) of those Regulations but is a public service pension scheme within the meaning of the 2004 Act([67]); or

(e) a scheme which provides no money purchase benefits other than benefits which are attributable to additional voluntary contributions;”;

(b) after regulation 1(2ZA)([68]) insert—

“(2ZB) For the purposes of the definition of “relevant scheme”—

“executive pension scheme” means a scheme—

(a) in relation to which a company is the only employer and the sole trustee; and

(b) the members of which are either current or former directors of the company and include at least one-third of the current directors;

“relevant small scheme” means a scheme with fewer than 12 members, where—

(a) all the members are trustees of the scheme and either—

(i) the provisions of the scheme provide that any decision made by the trustees is made by the unanimous agreement of the trustees who are members of the scheme; or

(ii) the scheme has a trustee who is independent in relation to the scheme for the purposes of section 23 of the 1995 Act (power to appoint independent trustees), and is registered in the register maintained by the Authority (as defined in that Act) in accordance with regulations made under subsection (4) of that section; or

(b) all the members are directors of a company which is the sole trustee of the scheme and either—

(i) the provisions of the scheme provide that any decision made by the company in its capacity as a trustee is made by the unanimous agreement of the directors who are members of the scheme; or

[64] See S.I. 1996/1715, regulation 1(2), substituted by S.I. 1997/786, and section 181(1) of the Pension Schemes Act 1993 (“the 1993 Act”) for definition of “money purchase benefits”. The definition of “money purchase benefits’ in section 181(1) of the 1993 Act was amended by the 2011 Act, section 29 and S.I. 2005/2053.

[65] S.I. 2013/2734.

[66] See S.I. 1996/1715, regulation 1(2), and section 1 of the 1993 Act, for definition of “public service pension scheme”. The definition of ‘public service scheme” in the 1993 Act was amended by S.I. 1999/1820.

[67] The definition of “public service pension scheme” was inserted by the Public Service Pensions Act 2013 (c.25), Schedule 4, paragraph 22(2).

[68] Inserted by regulation 20 of these Regulations.

(ii) one of the directors of the company is independent in relation to the scheme for the purposes of section 23 of the 1995 Act and is registered in the register maintained by the Authority (as defined in that Act) in accordance with regulations maintained under subsection (4) of that section;".

Appointment of service providers
14. The Administration Regulations are amended as follows—

(a) for the heading to Part II substitute "Advisers and Service Providers";

(b) after regulation 6 (duty to disclose information) insert—

"Appointment of service providers in respect of relevant schemes

6A.—(1) A relevant scheme must not require that administrative, fund management, advisory or other services in respect of the scheme are provided by a person identified in the scheme rules, or otherwise have the effect of restricting the choice of person who may be appointed to provide such services.

(2) Paragraph (1) overrides any provision of a relevant scheme to the extent that it conflicts with that paragraph.

(3) In relation to a relevant scheme which is not a money purchase scheme[69], this regulation applies only in relation to services which are provided in connection with the provision of money purchase benefits.".

Appointment of chair of trustees or managers
15.—(1) The Administration Regulations are amended as follows—

(a) in regulation 1(2) (interpretation) insert in the appropriate places alphabetically—

""chair" means the person appointed as chair of the trustees or managers of a relevant scheme, in accordance with regulation 22;

"professional trustee body" means a body which—

(a) was not established by an employer in relation to the scheme;

(b) is remunerated for its services as a trustee of the scheme; and

(c) has arranged a policy of insurance in relation to the exercise of its functions as a trustee of the scheme;";

(b) after regulation 21 insert—

"PART V

GOVERNANCE OF RELEVANT SCHEMES

CHAPTER 1

GENERAL

[69] See S.I. 1996/1715, regulation 1(2), substituted by S.I. 1997/786, for definition of "money purchase scheme".

Duty to appoint a chair of the trustees or managers

22.—(1) The trustees of a relevant scheme which is a trust scheme must appoint a chair of the trustees.

(2) The chair of the trustees must be—

(a) an individual who is a trustee of the scheme;

(b) a professional trustee body which is a trustee of the scheme; or

(c) where a company which is not a professional trustee body is a trustee of the scheme, an individual who is a director of that company and through whom the company exercises its functions as a trustee of the scheme.

(3) Where a relevant scheme is not a trust scheme, the managers must appoint one of their number to be the chair of the managers.

(4) The first chair of a relevant scheme must be appointed before the end of the period of three months starting with the date on which the scheme is established (but see also paragraph (6)).

(5) Where the chair ceases to hold office as chair for any reason, the trustees or managers must appoint a replacement in accordance with the provisions of this regulation, before the end of the period of three months starting with the date on which the chair ceases to hold that office.

(6) Paragraph (4) does not apply to a relevant scheme which was established before 6th April 2015 and, if the scheme has no chair on that date, the first chair must be appointed before the end of the period of three months starting with that date.".

(2) In the Register of Occupational and Personal Pension Schemes Regulations 2005([70]), in regulation 3(1) (registrable information) after sub-paragraph (d) insert—

"(da) in the case of an occupational pension scheme which is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 1996, the name of the person for the time being appointed as the chair in accordance with regulation 22 of those Regulations.".

Annual statement regarding governance

16.—(1) In the Administration Regulations after regulation 22([71]) insert—

"Annual statement regarding governance

23.—(1) The trustees or managers of a relevant scheme must prepare a statement within seven months of the end of each scheme year and that statement must—

(a) in relation to the default arrangement—

(i) include the latest statement prepared in accordance with regulation 2A (default investment strategy) of the Occupational Pension Schemes (Investment) Regulations 2005 ("the Investment Regulations");

(ii) describe any review undertaken during the scheme year in accordance with paragraph (2) of that regulation;

[70] S.I. 2005/597.Regulation 3(1) was amended by S.I. 2006/1733.
[71] Inserted by regulation 15 of these Regulations.

(iii) explain any changes resulting from such a review; and

(iv) where no review was undertaken during the scheme year, give the date of the last review;

(b) describe how the requirements of regulation 24 of these Regulations (requirements for processing financial transactions) have been met during the scheme year;

(c) in relation to the charges and transaction costs which the trustees or managers are required to calculate in accordance with regulation 25(1)(a) of these Regulations—

(i) state the level of charges and transaction costs applicable to the default arrangement during the scheme year or, where the scheme has more than one default arrangement, state the range of the levels of charges and transaction costs applicable to those arrangements;

(ii) state the range of the levels of charges and transaction costs applicable to all funds which are not part of the default arrangement and in which assets relating to members are invested during the scheme year;

(iii) indicate any information about transaction costs which the trustees or managers have been unable to obtain and explain what steps are being taken to obtain that information in the future; and

(iv) explain the trustees' or managers' assessment, in accordance with regulation 25(1)(b), of the extent to which the charges and transaction costs represent good value for members;

(d) describe how the requirements of sections 247 and 248 of the 2004 Act (requirements for knowledge and understanding) have been met during the scheme year and explain how the combined knowledge and understanding of the trustees or managers, together with the advice which is available to them, enables them properly to exercise their functions as trustees or managers of the scheme; and

(e) be signed on behalf of the trustees or managers by the chair.

(2) Where the first statement prepared by the trustees or managers of a relevant scheme in accordance with this regulation relates to a scheme year which ends before 5th April 2016, this regulation applies to that statement as if references to "the scheme year" in sub-paragraphs (a) to (d) of paragraph (1) were to the part of the scheme year starting on 6th April 2015.

(3) In this regulation "default arrangement" has the same meaning as in the Investment Regulations.".

(2) In the Occupational Pension Schemes (Disclosure of Information) Regulations 2013, in Part 5 of Schedule 3 (information to be included in the annual report) after paragraph 33 insert—

"**34.** Where the scheme is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 1996, the statement which the trustees or managers are required to prepare by regulation 23 of those Regulations (annual statement regarding governance).".

Requirements for processing financial transactions

17. In the Administration Regulations, after regulation 23([72]) insert—

"Requirements for processing financial transactions

24.—(1) The trustees or managers of a relevant scheme must secure that core financial transactions are processed promptly and accurately.

(2) A "core financial transaction" includes (but is not limited to)—

(a) investment of contributions to the scheme;

(b) transfers of assets relating to members into and out of the scheme;

(c) transfers of assets relating to members between different investments within the scheme;

(d) payments from the scheme to, or in respect of, members.

(3) In relation to a scheme which is not a money purchase scheme, this regulation applies only in relation to the provision of money purchase benefits.".

Assessment of charges and costs

18. In the Administration Regulations, after regulation 24([73]) insert—

"Assessment of charges and transaction costs

25.—(1) The trustees or managers of a relevant scheme must, at intervals of no more than one year—

(a) calculate—

(i) the charges; and

(ii) in so far as they are able to do so, the transaction costs,

borne by members of the scheme, according to the funds in which assets relating to those members are invested; and

(b) assess the extent to which the charges and transaction costs represent good value for members.

(2) In this regulation (and in regulation 23), "charges" and "transaction costs" have the meanings given in regulation 2(1) of the Occupational Pension Schemes (Charges and Governance) Regulations 2015.

(3) In relation to a scheme which is not a money purchase scheme, this regulation applies only in relation to charges and transaction costs which relate to the provision of money purchase benefits.".

Requirements relating to default arrangement

19. In the Investment Regulations—

(a) in regulation 1(2) (interpretation)([74]) insert the following in the appropriate places alphabetically—

[72] Inserted by regulation 16 of these Regulations.
[73] Inserted by regulation 17 of these Regulations.
[74] There are amendments not relevant to these Regulations.

""default arrangement", means an arrangement, within the meaning of regulation 3 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015 (default arrangement) which would be a default arrangement within the meaning of that regulation if that regulation were modified as follows-

(a) in paragraph (1)(a) omit "qualifying", and for "relevant jobholders" substitute "workers";

(b) in paragraph (2)(b) omit "subject to paragraph (3),";

(c) omit paragraphs (3) and (4); and

(d) in paragraph (6)-

  (i) in the definition of "relevant date" omit the words after "regulation 1(2)"; and

  (ii) omit the definitions of "relevant jobholder" and "staging date":

""relevant scheme" has the same meaning as in the Occupational Pension Schemes (Administration) Regulations 1996;";

(b) after regulation 2 (statement of investment principles) insert—

"Additional requirements in relation to default arrangement

2A.—(1) The trustees or managers of a relevant scheme must prepare a statement of the investment principles governing decisions about investments for the purposes of the default arrangement, and that statement must be in writing and must cover at least the following matters—

(a) the aims and objectives of the trustees or managers in respect of such investments;

(b) their policies in relation to the matters mentioned in regulation 2(3)(b) in respect of the default arrangement; and

(c) an explanation of how the aims and objectives mentioned in sub-paragraph (a) and the policies mentioned in sub-paragraph (b) (together "the default strategy") are intended to ensure that assets are invested in the best interests of the group of persons consisting of relevant members and relevant beneficiaries.

(2) The trustees or managers must review both the default strategy and the performance of the default arrangement—

(a) at least every three years; and

(b) without delay after any significant change in—

  (i) investment policy; or

  (ii) the demographic profile of relevant members.

(3) The trustees or managers must, in particular, review the extent to which the return on investments relating to the default arrangement (after deduction of any charges relating to those investments) is consistent with the aims and objectives of the trustees or managers in respect of the default arrangement.

(4) The trustees or managers must revise the statement prepared in accordance with paragraph (1) after every review.

(5) For the purposes of this regulation and regulation 4A, a person is a relevant member or a relevant beneficiary if assets relating to that member or, as the case may be, that beneficiary (as defined in regulation 4), are invested in the default arrangement.";

(c) after regulation 4 (investment by trustees) insert—

"Investments relating to a default arrangement

4A. Where regulation 4(2) does not apply([75]) to a relevant scheme, the assets allocated to the scheme's default arrangement must be invested—

(a) in the best interests of relevant members and relevant beneficiaries; and

(b) in the case of a potential conflict of interest, in the sole interest of those members and beneficiaries.".

CHAPTER 2

ADDITIONAL GOVERNANCE REQUIREMENTS FOR RELEVANT MULTI-EMPLOYER SCHEMES

Definition of "relevant multi-employer schemes"

20. The Administration Regulations are amended as follows—

(a) in regulation 1(2)([76]) insert in the appropriate place alphabetically—

""relevant multi-employer scheme" means a relevant scheme in relation to which some or all of the participating employers are not connected employers, or which is promoted as a scheme where participating employers need not be connected employers, except where—

(a) the scheme has distinct sections relating to employers which are not connected and each of those sections is governed by different trustees or managers (or, where the scheme does not currently have participating employers which are not connected employers, it will have such sections when there are participating employers which are not connected employers); or

(b) the scheme is established under section 67 of the Pensions Act 2008([77]) (duty to establish a pension scheme – National Employment Savings Trust).";

(b) after regulation 1(2) insert—

"(2ZA) For the purposes of the definition of "relevant multi-employer scheme"—

"connected employers" means two employers who are—

(a) part of a group of companies consisting of a holding company and one or more subsidiaries within the meaning of section 1159(1) of the Companies Act 2006([78]) (meaning of "subsidiary" etc); or

(b) partnerships, each having the same persons as at least half of its partners.

([75]) See regulation 7 of S.I. 2005/3378.
([76]) There are no relevant amendments.
([77]) Section 67 was amended by the Finance (No. 3) Act 2010 (c. 33), section 30(2).
([78]) 2006 c.46.

"participating employer" means any employer currently or previously participating in the scheme in accordance with the scheme rules;".

Additional requirements for relevant multi-employer schemes
21. In the Administration Regulations after regulation 25([79]) insert—

"CHAPTER 2

RELEVANT MULTI-EMPLOYER SCHEMES

Annual statement regarding governance: relevant multi-employer schemes

26. Where a relevant scheme is a relevant multi-employer scheme, the statement prepared in accordance with regulation 23 must include such of the following additional information as is relevant to the scheme—

(a) how the requirements of regulation 27(2) (majority of trustees and chair to be non-affiliated) have been met during the year;

(b) where a trustee who is non-affiliated (within the meaning of regulations 27 and 28) was appointed during the year, details of how the requirement of regulation 28(1) (open and transparent appointment process) was met;

(c) details of the arrangements in place during the year to meet the requirement of regulation 29 (representation of the views of members to the trustees or managers).

Appointment of trustees

27.—(1) A relevant multi-employer scheme which is a trust scheme must have at least three trustees (but see also paragraphs (4) to (7)).

(2) A majority of the trustees of a relevant multi-employer scheme which is a trust scheme, including the chair of the trustees, must be non-affiliated (but see also paragraphs (4) to (7)).

(3) Where there is a chair of the trustees at the time any other trustee is appointed, the chair must be consulted on the appointment.

(4) In relation to a company which is not a professional trustee body and which is a trustee of a relevant multi-employer scheme, this regulation applies as if—

(a) the company were not a trustee of the scheme; and

(b) each individual who is a director of the company and through whom the company exercises its functions as trustee were a trustee of the scheme.

(5) A new relevant multi-employer scheme must meet the requirements of paragraphs (1) and (2) before the end of the period of three months starting with the date on which the scheme is established (or, if later, the date on which the scheme becomes a relevant multi-employer scheme which is a trust scheme).

(6) Where a trustee of a relevant multi-employer scheme—

(a) ceases to be a trustee for any reason; or

[79] Inserted by regulation 18 of these Regulations.

(b) in the case of a trustee who was non-affiliated, ceases to be non-affiliated,

the requirements of paragraphs (1) and (2) must be met before the end of the period of three months starting with the date on which the former trustee ceases to be a trustee or, as the case may be, the trustee ceases to be non-affiliated.

(7) Where a relevant multi-employer scheme was established, or became a relevant multi-employer scheme, before 6th April 2015 and the requirements of paragraphs (1) or (2) are not met on that date, the requirement in question must be met before the end of the period of three months starting with that date.

(8) In this regulation and in regulation 28, "non-affiliated" means independent of any company which provides advisory, administration, investment or other services in respect of the relevant multi-employer scheme (but see also regulation 28).

Appointment of trustees: trustees who are non-affiliated

28.—(1) The appointment process for a trustee who is to count as non-affiliated for the purposes of regulation 27(2) must be open and transparent.

(2) For the purposes of paragraph (1), an appointment process which is open and transparent includes (but is not limited to) a process which—

(a) includes advertisement of the vacancy for a trustee in at least one appropriate national publication;

(b) includes engagement of the services of a recruitment agency to assist in the selection of candidates; or

(c) meets the requirements of section 241(2) or, as the case may be, 242(2) of the 2004 Act (nomination and selection of member-nominated trustees and member-nominated directors of corporate trustees).

(3) For the purposes of determining whether a person is non-affiliated, the following matters must be taken into account—

(a) whether the person—

(i) is a director, partner or employee of a company which provides advisory, administration, investment or other services in respect of the scheme (a "service provider") or a company which is connected to a service provider; or

(ii) has been such a director, partner or employee during the period of five years ending with the date of the person's appointment as a trustee;

(b) whether the person receives any payment or other benefit from a service provider, other than a payment or other benefit in respect of a role in the governance of a personal pension scheme and in which the person is required to act in the interests of some or all of the scheme members;

(c) whether or not, in the person's relationship with a service provider, the person's obligations to the service provider conflict with their obligations as a trustee of the relevant multi-employer scheme and whether their obligations as a trustee will take priority in the case of a conflict.

(4) A trustee who is an individual is not to count as non-affiliated for the purposes of regulation 27(2) for—

(a) any one period of more than five years; or

(b) subject to paragraph (5), for more than ten years in total.

(5) No period of appointment of a trustee who is an individual is to be taken into account for the purposes of paragraph (4)(b) if more than five years have elapsed since the trustee last held office as a trustee of the relevant multi-employer scheme.

(6) Paragraphs (1) to (5) apply to an individual who is a director of a corporate trustee and to whom regulation 27 applies as if he or she were as a trustee as they apply to a trustee who is an individual.

(7) Where a trustee who is to count as non-affiliated for the purposes of regulation 27(2) is a professional trustee body and is not an individual—

(a) the trustee is not to count as non-affiliated for any one period of more than five years;

(b) a nominated individual must act as representative of the trustee; and

(c) the nominated individual may not act as representative of the trustee for more than ten years in total.

(8) For the purposes of paragraph (2)(a), two companies are "connected" if they are—

(a) part of a group of companies consisting of a holding company and one or more subsidiaries within the meaning of section 1159(1) of the Companies Act 2006; or

(b) partnerships, each having the same persons as at least half of its partners.

Representation of members

29. The trustees or managers of a relevant multi-employer scheme must make arrangements to encourage members of the scheme, or their representatives, to make their views on matters relating to the scheme known to the trustees or managers.".

PART 4

COMPLIANCE

Interpretation of this Part

22. In this Part, "relevant provision" means-

(a) a provision in Part 2 of these Regulations;

(b) regulation 6A and a provision in Part V of the Administration Regulations;

(c) regulations 2A and 4A of the Investment Regulations.

Amendment of the Register of Occupational and Personal Pension Schemes Regulations 2005

23. (1) Regulation 3 of the Register of Occupational and Personal Pension Schemes Regulations 2005([80]) is amended as follows.

(2) At the end of paragraph (e) delete "and";

(3) After paragraph (g) insert—

"(h) in the case of an occupational scheme which is a relevant scheme within the meaning of the Occupation Pension Schemes (Scheme Administration) Regulations 1996, whether the trustees or managers of that scheme have prepared the statement that they are required to prepare in accordance with regulation 23 of those Regulations; and

(i) in the case of an occupational scheme in respect of which the requirements of Part 2 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015 apply to one or more of its members, whether the trustees or managers of that scheme have complied with those requirements in respect of each member to whom they apply.".

Compliance notices

24.—(1) The Regulator must issue a compliance notice to a trustee or manager of a relevant scheme in any of the circumstances of non-compliance in paragraph (2).

(2) The circumstances mentioned in paragraph (1) are—

(a) receipt of an indication pursuant to regulation 3(h) of the Register of Occupational and Personal Pension Schemes Regulations 2005 that the trustee or manager has not prepared the statement that they are required to prepare by regulation 23 of the Administration Regulations[81];

(b) receipt of an indication pursuant to paragraph 3(i) of the Register of Occupational and Personal Pension Schemes Regulations 2005 that the trustee or manager has not complied with Part 2 of these Regulations; or

(c) if for any other reason the Regulator is of the opinion that that trustee or manager is not complying with, or has not complied with any relevant provision.

(3) A compliance notice is a notice directing the trustee or manager to whom it is issued to take, or refrain from taking, the steps specified in the notice.

(4) The steps mentioned in paragraph (3) may be any steps that the Regulator reasonably requires with a view to ensuring that any non-compliance in the circumstances mentioned in paragraph (2) is remedied or not repeated.

(5) A direction in a compliance notice may be expressed to be conditional on compliance by a third party with a specified direction contained in a third party compliance notice under regulation 33.

(6) A compliance notice may, in particular—

(a) state the period within which any step must be taken or must cease to be taken;

(b) require the trustee or manager to provide within a specified period specified information relating to the non-compliance;

(80) S.I. 2005/597.
(81) Inserted by regulation 16 of these Regulations.

(c) require the trustee or manager to inform the Regulator, within a specified period, how the person has complied with or is complying with the notice;

(d) that if the Regulator is of the opinion that the trustee or manager fails to comply with the requirements of the notice, the Regulator must issue a penalty notice under paragraph (1) of regulation 26;

(e) give the trustee or manager to whom it is issued a choice between different ways of remedying, or preventing the recurrence of, the non-compliance.

(7) A compliance notice must—

(a) state which of the circumstances of non-compliance in paragraph (2) applies and, if the circumstance in paragraph (2)(c) applies, state which relevant provision it is asserted was not, or is not being, complied with; and

(b) contain a statement of the matters which it is asserted constitute the non-compliance and of the evidence on which that belief is based.

Third party compliance notices

25.—(1) Where in any of the circumstances of non-compliance in paragraph (2)–

(a) the Regulator is of the opinion that the non-compliance is or was, wholly or partly, a result of a failure of someone other than the trustees or managers ("the third party"), and

(b) that failure is not in itself a contravention of a relevant provision,

the Regulator must issue to the third party a third party compliance notice.

(2) The circumstances mentioned in paragraph (1) are—

(a) receipt of an indication pursuant to regulation 3(h) of the Register of Occupational and Personal Pension Schemes Regulations 2005 that the trustees or managers have not prepared the statement required by regulation 23 of the Administration Regulations .

(b) receipt of an indication pursuant to paragraph 3(i) of the Register of Occupational and Personal Pension Schemes Regulations 2005 that the trustees or managers have not complied with Part 2 of these Regulations;

(c) an indication that the trustees or managers are unable to confirm whether they are complying or will be able to comply with that Part; or

(d) if for any other reason the Regulator is of the opinion that the trustee or manager is not complying with, or has not complied with any relevant provision.

(3) A third party compliance notice is a notice directing the third party to take, or refrain from taking, the steps specified in the notice.

(4) The steps mentioned in paragraph (3) may be any steps that the Regulator reasonably requires with a view to remedying or preventing a recurrence of the failure mentioned in paragraph (1).

(5) A third party compliance notice may, in particular—

(a) state the period within which any step must be taken or must cease to be taken;

(b) require the third party to provide within a specified period specified information relating to the failure;

(c) require the third party to inform the Regulator, within a specified period, how the third party has complied with or is complying with the notice;

(d) state that, if the Regulator is of the opinion that the third party fails to comply with the requirements of the notice, the Regulator must issue a penalty notice under paragraph (1) of regulation 26;

(e) give the third party a choice between different ways of remedying or preventing the recurrence of the third party's failure.

(6) A third party compliance notice must—

(a) state which of the circumstances of non-compliance in paragraph (2) apply and, if the circumstance in paragraph (2)(d) applies, state which relevant provision it is asserted was not, or is not being, complied with; and

(b) contain a statement of—

(i) the matters which it is asserted constitute the non-compliance, and

(ii) the matters which it is asserted constitute the failure by the third party,

and the evidence on which that belief is based.

Penalty notices

26.—(1) The Regulator must issue a penalty notice to a person where it is of the opinion that the person has failed to comply with—

(a) a compliance notice under regulation 24;

(b) a third party compliance notice under regulation 25; or

(c) a relevant provision.

(2) A penalty notice is a notice requiring the person to whom it is issued to pay a penalty within the period specified in the notice.

(3) The amount of a penalty is to be determined by the Regulator but—

(a) subject to paragraph (3)(b) must not exceed-

(i) £5,000 if the person is an individual, or

(ii) £50,000 if the person is a body corporate or a Scottish partnership or any other person.

(b) The amount of a penalty must be at least £500 and must not exceed £2,000 where, in relation to a first failure in connection with a scheme year.

(i) a penalty notice is issued because the circumstance in regulation 24(2)(a) occurs, or—

(ii) for any other reason the Regulator is of the opinion that a trustee or manager has not prepared the statement required by regulation 23 of the Administration Regulations.

(4) A penalty notice must—

(a) where it is issued to trustees and managers, be issued to all the trustees and managers of the relevant scheme and specify their joint and several liability for the penalty;

(b) state the amount of the penalty;

(c) state the date, which must be at least 4 weeks after the date on which the notice is issued, by which the penalty must be paid;

(d) state the period (if any) to which the penalty relates;

(e) if the notice is issued under paragraph (1)(a) or (b), specify the failure to which the notice relates;

(f) if the notice is issued under paragraph (1)(c), specify the provision or provisions that have not been complied with;

(g) notify the person to whom the notice is issued of the right of the review process under regulation 29 and the right of referral to a tribunal under regulation 30.

Penalty notices: recovery

27.—(1) Any penalty required by a penalty notice is recoverable by the Regulator.

(2) In England and Wales, any such penalty is, if the county court so orders, recoverable under section 85 of the County Courts Act 1984([82]) or otherwise as if it were payable under an order of that court.

(3) In Scotland, any such penalty is enforceable as if it were an extract registered decree arbitral bearing a warrant for execution signed by the sheriff court of any sheriffdom in Scotland.

(4) The Regulator must pay into the Consolidated Fund any penalty recovered under this section.

Penalty notices: recovery from bodies corporate and Scottish partnerships

28. —(1) Where any penalty required by a penalty notice is recoverable from a body corporate or Scottish partnership, and-

(a) the compliance failure which is the subject of that notice occurred by reason of an any act or omission of the body or partnership, and

(b) that act or omission was done with the consent of, connivance of, or is attributable to any neglect on the part of an officer of the body corporate or the partnership,

the Regulator may require the officer to pay the penalty required by the notice.

(2) In this regulation, officer means—

(a) in relation to a body corporate—

(i) any director, manager, secretary or other similar officer of the body, or a person purporting to act in any such capacity, and

(ii) where the affairs of a body corporate are managed by its members, any member in connection with his functions of management, and

(b) in relation to a Scottish partnership, the partners.

(3) Where the Regulator requires any person to pay a penalty by virtue of paragraph (1), they may not also require the body corporate, or Scottish partnership, in question to pay a penalty in respect of the same act or omission.

[82] 1984 c. 28.

Review of penalty notices

29. —(1) The Regulator may review a notice to which this paragraph applies—

(a) on the written application of the person to whom the notice was issued, or

(b) if the Regulator otherwise considers it appropriate.

(2) Paragraph (1) applies to—

(a) a compliance notice issued under regulation 24;

(b) a third party compliance notice issued under regulation 25; and

(c) a penalty notice issued under paragraph (1) of regulation 26.

(3) The period within which—

(a) an application to review a notice may be made under paragraph (1)(a) is 28 days, starting from the day a notice is issued to a person; and

(b) a notice may be reviewed under paragraph (1)(b) is 18 months, starting from the day a notice is issued to a person.

(4) On a review of a notice, the effect of the notice is suspended for the period beginning when the Regulator determines to carry out the review and ending when the review is completed.

(5) In carrying out a review, the Regulator must consider any representations made by the person to whom the notice was issued.

(6) The Regulator's powers on a review include power to—

(a) confirm, vary or revoke the notice;

(b) substitute a different notice.

References to First-Tier Tribunal or Upper Tribunal

30.—(1) A person to whom a penalty notice is issued under regulation 26 may, if one of the conditions in paragraph (2) is satisfied, make a reference to the Tribunal in respect of—

(a) the issue of the notice;

(b) the amount of the penalty under the notice.

(2) The conditions are—

(a) that the Regulator has completed a review of the notice under regulation 29; or

(b) that the person to whom the notice was issued has made an application for the review of the notice under paragraph (1)(a) of regulation 29 and the Regulator has determined not to carry out such a review.

(3) On a reference to the Tribunal in respect of a notice, the effect of the notice is suspended for the period beginning when the Tribunal receives notice of the reference and ending—

(a) when the reference is withdrawn or completed; or

(b) if the reference is made out of time, on the Tribunal determining not to allow the reference to proceed.

(4) For the purposes of paragraph (3)(a), a reference is completed when—

(a) the reference has been determined; and

(b) the Tribunal has remitted the matter to the Regulator.

(5) In this regulation "the Tribunal", in relation to a reference under this regulation, means–

(a) the Upper Tribunal, in any case where it is determined by or under Tribunal Procedure Rules that the Upper Tribunal is to hear the reference;

(b) the First Tier Tribunal in any other case.

Signed by authority of the Secretary of State for Work and Pensions

Name

Parliamentary Under Secretary of State

Date

Department for Work and Pensions

Annex D Glossary

Active member	A member of a pension scheme who is at present accruing benefits under that scheme.
Active member discount (AMD)	A charge structure whereby active members of a scheme are charged a lower amount than they would be if they were not contributing.
Additional Voluntary Contributions (AVC)	An extra pension contribution which a member may choose to make to increase their retirement income, often within a Defined Benefit scheme.
Administration	The day to day running of a pension scheme. This may include collecting contributions and payment of benefits.
Adviser	A professional who renders financial services to clients.
Annual management charge (AMC)	An annual charge levied on the value of the scheme fund. It may cover a combination of the sales, administration and fund management costs of the fund.
Annuity	The fixed sum of money paid to individuals each year upon retirement. This is typically for the rest of their life based on their total accumulated pension savings.
Automatic enrolment	Employers are be required to make arrangements by which eligible jobholders become active members of an automatic enrolment scheme with effect from the automatic enrolment date. Automatic enrolment is not applicable if the jobholder is an active member of a qualifying scheme on that date.

Bundled schemes	Making pension transfers the default action unless the individual indicates they would like to keep their pension pot in the scheme or transfer it to another pension scheme.
Commission	A payment, which may be either an upfront or on-going fee (often called trail commission) or both, for advice services agreed between a scheme provider and an adviser. The cost is recouped through member-borne charges.
Consultancy charging	An upfront fee for advice services agreed between an employer and an adviser. The cost is recouped through member-borne charges.
Contract-based schemes	Schemes where an employer appoints a pension provider, often an insurance company, to run the scheme. The scheme members will sign a contract with the provider who will make the majority of decisions about the way the scheme is run.
Contributions	The money paid by members and employers to the pension scheme.
Decumulation	The process of converting pension savings into a retirement income.
Default arrangement	An arrangement where the member is deemed to have not made an active choice.
Non-contributing members	In defined contribution schemes, this is someone who no longer contributes to the scheme but is not yet a beneficiary of that scheme. In some contract-based arrangements the member may be reclassified as a member of an Individual Personal Pension rather than a Group Personal Pension.
Defined Benefit (DB)	A scheme in which the benefits are defined in the scheme rules and accrue independently of the contributions payable and investment returns.
Defined Contribution (DC)	A defined contribution schemes' benefits are based on how much the member and employer pay into the scheme, and also on the performance of the investments made with that money.
Financial Conduct Authority (FCA)	The FCA is responsible for regulating the standards of conduct in retail and wholesale, financial markets and for supervising the infrastructure that supports those markets.
Group personal pensions (GPP)	A pension scheme which is organised through the employer, but still takes the form of individual contracts between the employee and the pension provider.
Hybrid schemes	A hybrid scheme is a mixture of defined benefit (DB) and defined contribution (DC).

Independent Financial Adviser (IFA)	Someone who is authorised to provide advice and sell a wide range of financial products.
Intermediaries	Advisers
Investment Manager	An individual (or company) to whom the management of all or part of a scheme's assets is delegated.
Investment Strategy	The rules and procedures for the selection of the range of investment products for a pension scheme.
Master trust	A multi-employer pension scheme where each employer has its own division within the master arrangement. There is one legal trust and, therefore, one trustee board.
Member	An individual who has contributed and/or continues to contribute.
Member borne deductions	All deductions paid by members of pension schemes to the pension provider or another third party, excluding transaction costs.
Memberships	The number of members in a scheme (an individual can be a member of multiple pension schemes).
Money purchase benefits	Where the rate or amount of the benefit is based on the payments made by the member and which are not average salary benefits.
Money purchase scheme	Pension scheme where all the benefits are money purchase benefits.
NEST	A defined contribution occupational pension scheme backed by the government. It has a public service obligation to let any employer that wishes to use it to do so, regardless of their size.
Occupational pension	A pension which is provided via a person's employment, normally taking the form of a trust arrangement.
Retail Distribution Review (RDR)	On 1 January 2013, the RDR introduced new rules from the then FSA on how financial advisory companies could operate. These rules included a stipulation that advisers are not able to take commission as a form of remuneration but instead will have to quote a fee for any advice given.
The Pensions Regulator (TPR)	TPR regulates occupational pension schemes in the UK.
Pension scheme	The arrangement by which an employer and, usually, an employee pay into a fund that is invested to provide the employee with a pension on retirement.
Stakeholder pension	Type of pension scheme introduced in 2001, required to meet a number of conditions set out in legislation, including a cap on charges, low minimum contributions, and flexibility in relation to stopping and starting contributions.

Total Expense Ratio	Another measure of scheme or fund charges, broader than the Annual Management Charge (AMC).
Transaction costs	Variable trading costs that a scheme incurs as a result of buying, selling, lending and borrowing investments. These costs cannot be predicted at the beginning of a reporting period as they are dependent on the level and nature of trading undertaken by a scheme, which in turn is influenced by market conditions.
Trustees	A member of the board of trustees responsible for the management, administration and investment of the pension assets.
Trust based schemes	A scheme that is managed by a board of trustees. The trustees have full responsibility for the management, administration and investment of the plan. The trustees' fiduciary duty is to act in the interests of members and while they can delegate tasks to various specialists, such as investment managers, the responsibility remains with the trustee.
Unbundled schemes	A pension scheme where there is separation in the provider of either the investment management or administration of a scheme.
Workplace pensions	A pension provided by an employer.

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