



2019 DC research response

Background

Our vision for the future of occupational pensions is one where all savers are in schemes that have excellent standards of governance and deliver good value. The vast majority of the 11 million defined contribution (DC) savers are members of master trusts. By the end of the year, we will have a set of authorised master trusts under supervision, ensuring that all the master trusts in the market reach the standards we expect.

Our aim is to reduce the number of poorly run schemes, focusing on raising standards of trusteeship and encouraging the consolidation of DC schemes that can't or won't meet those standards.

In Spring 2019, we surveyed DC schemes to understand the extent to which the trustees met the five key governance requirements (KGRs) introduced in 2015 legislation, and to measure how they are performing against our expectations as set out in our DC code of practice 13¹. The survey also asked questions about the winding up of pension schemes, cyber security, climate change, awareness and influence of TPR interventions/interactions and perceptions of TPR's new operating model.

The survey follows similar studies carried out in previous years. In particular, we have compared this year's results with those of 2018, meaning that we can identify trends. The survey findings are consistent with those from previous years and support our existing assessment that whilst most DC savers are in schemes with relatively good governance and administration, there is a long tail of smaller schemes that do not meet the standards that we expect.

This commentary accompanies the full research report² which details all the survey results. It is intended to draw out the key themes and areas of concern we have identified.

1 <https://tpr.gov.uk/en/document-library/codes-of-practice/code-13-governance-and-administration-of-occupational-trust-based-schemes-providing-money-purchase>

2 www.tpr.gov.uk/-/media/thepensionsregulator/files/import/pdf/dc-research-summary-report-2019

Governance

The survey shows an increasing number of members are in well run schemes, with nearly three quarters of DC savers in schemes that meet all their key governance requirements. However, this is mainly attributable to larger schemes and the fact that there are more members in master trusts than in 2018. The number of small and micro schemes that meet all the KGRs remains alarmingly low; just 1% of small schemes and 4% of micro schemes. This segment of schemes continues to give us particular cause for concern.

The results were similar for meeting DC code expectations, which go beyond just the KGRs. A greater number of large and medium schemes are meeting our expectations although investment governance and administration were the worst performing areas across all schemes. These are both specific areas that we are addressing through our regulatory initiatives, starting with default investment governance and record-keeping.

To address our broader governance concerns, we have published a consultation entitled 'The Future of trusteeship and governance'³. In this, we propose several measures to reduce the number of poorly run schemes, including:

- Stronger requirements around trustee knowledge and understanding, skills and ongoing learning and development.
- Scheme governance structures for effective decision making, including greater diversity on trustee boards, and an aspiration to see an accredited professional trustee on every board in the future⁴.
- Driving DC consolidation for those schemes that are unable or unwilling to meet the standards of trusteeship and governance we expect.

Smaller schemes have historically been hard for us to influence through traditional communications. As part of being a clearer, quicker and tougher regulator, we will take a more directive style of communication with this hard to reach group – clarifying priorities and providing 'simple steps' for complying with the fundamentals of good governance. We have already taken this approach to ensure that savers are in schemes where default investment strategies are properly governed. The survey showed that direct scheme-specific interventions (excluding scheme return) typically were more likely to prompt trustees to spend more time on governance and administration than accessing information or guidance, when based just on those experiencing each one.

3 <https://www.thepensionsregulator.gov.uk/en/document-library/consultations/future-of-trusteeship-and-governance-consultation>

4 <https://appt.co.uk/wp-content/uploads/2019/03/20190306-FINAL-STANDARDS.pdf> <https://www.gov.uk/government/publications/protecting-defined-benefit-pension-schemes>

Governance continued...

Trustees of small and micro schemes are more likely to be lay trustees and be more reliant on their advisers and service providers to support compliance. We therefore think it is important we seek to communicate more clearly with intermediary groups on how they can support lay trustees to improve scheme governance.

This more directive approach will also help us to encourage consolidation with this group of schemes. In the survey, one in five single employer schemes told us they had considered winding up. Small schemes that had considered winding up were more likely to meet the KGRs, indicating that the small schemes with poorest governance are not considering winding up, and will need to be more directly encouraged to do so.

Cyber security

Three quarters of schemes reported that they had more than half of the expected cyber security controls in place, with almost all medium and large schemes and all master trusts having controls in place. Whilst one in seven schemes reported experiencing cyber attacks or breaches in the previous year, only a very small percentage of members were in a scheme that reported personal data being altered, destroyed or taken.

The data collected on cyber security allows us to compare pension schemes' experience against that of other sectors and will enable us to monitor trends over time. We will combine the findings of this survey alongside that of our defined benefit (DB) and public service pension scheme (PSPS) surveys, to determine our key messages going forward, so we can be clearer in our expectations of trustees. It is vital that schemes consider their cyber footprint. Pension schemes share large amounts of data with third parties such as administrators, employers and legal advisers. An awareness of the security processes that these bodies have in place is necessary too. Cyber security is not just about reducing the risk of incidents occurring, but also requires preparation for when things go wrong. Schemes need to have an incident response plan and the trustees must be aware of the contingencies in place.

Climate change

Only 20% of schemes reported that they take account of climate change in their investment strategies and approaches. This gives us a clear baseline for improvement as part of a strategy for improving the consideration of Environmental Social and Governance (ESG) factors in pension scheme investment strategies. Earlier this month we published updated investment guidance⁵ which reflects the new legal requirements on DC scheme trustees to publish their policies on ESG and report how those policies have been acted on. We have published our commitment to the Green Finance Strategy in a joint statement with other regulators⁶, and with government have established a joint working group to develop guidance for pension schemes on reporting in-line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

Conclusion

The pattern of results this year solidifies our assessment that smaller DC schemes struggle to meet the standards of governance and trusteeship we expect, and to deliver value for their members. This strengthens our view that ensuring all DC savers do receive value for money will require shrinking the DC market, getting more savers into larger, better run and better value schemes.

5 <https://www.thepensionsregulator.gov.uk/en/trustees/managing-dc-benefits/investment-guide-for-dc-pension-schemes>

6 <https://www.thepensionsregulator.gov.uk/en/document-library/statements/climate-change-joint-statement>

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