Summary
- TPR has completed the authorisation process of DC master trusts, but the 37 that are authorised (and any new master trusts that occur) can expect to be subject to continued regulator scrutiny.
- Further master trust consolidation is expected.
- The development of decumulation products within master trusts will be a significant area of focus.
- Master trusts are expected to be 'trailblazers' for the industry as a whole in terms of ESG, technology and diversity.

Masters of their own destiny

The Pensions Regulator's authorisation of DC master trusts is now complete. What's next for these retirement saving vehicles?

Thirty-seven is the magic number for DC master trusts it turns out; the total amount to be authorised by The Pensions Regulator (TPR). Eighty-seven master trusts existed at the start of TPR's authorisation process; fewer than half were there at the end.

There are now a total of 16 million savers in the authorised master trusts, which are now "better protected" due to the authorisation regime, TPR states.

Despite applications closing for existing master trusts, new master trusts can apply to enter the market at any time. However, new schemes will be more intensely supervised than existing schemes because they will not have an operational track record.

Supervision

Continued scrutiny is something DC master trusts, new and old, will have to get used to, as "the most pressing priority for master trusts post-authorisation will be ensuring that they retain their authorised status", Redington director for DC and financial wellbeing, Jonathan Parker, says.

In May, TPR stated that authorised schemes will be required to send the chair's statement, annual reports and accounts, scheme funder accounts and a supervisory return to the regulator on a yearly basis.

"Once authorised, master trusts will immediately be supervised by us," TPR head of master trust authorisation and supervision, Kim Brown, said at the time. "The supervision of authorised master trusts is vital to ensure the new standards imposed in this market are not only demonstrated to us as part of the application process but also continue to be met in the future."

As part of the reporting process, schemes must also alert the regulator to any 'significant events' which mean a master trust may no longer meet the authorisation criteria or 'triggering events' that may pose an immediate threat to the operation of the scheme.

This scrutiny is a key part of the new master trust regime, Smart Pension director of policy and communications, Darren Philp, says.

"Authorisation is very much the beginning of the process and TPR will be supervising master trusts to ensure they still meet the authorisation criteria and continue to improve standards across the industry. This is a new way of regulating for TPR, so it will take a bit of time to bed in, but the new supervisory regime should ensure that the strides made in improving standards are locked in and built on," he explains.

TPR will soon be issuing each master trust with its own first supervisory report, summarising its views on the master trust and areas that the regulator feels may require additional work from the trustees, Sackers partner, Claire van Rees, notes.

Master trusts will be subject to different levels of supervision oversight depending on the level of risk TPR considers them to have. Those subject to one-to-one oversight will have regular dialogue with TPR.

"There are concerns from some that the level of information likely to be required in the supervisory returns could be onerous to provide, although the details of how the returns will work does still seem to be a work in progress.

"Trustees shouldn't feel their job is going to be easier now that they have authorisation – we expect the work involved to maintain high standards

of governance and oversight to meet the supervisory expectations to be significant," van Rees warns.

Consolidation

This intense scrutiny is expected to be a factor for further consolidation in the near future.

"We believe there will be some consolidation of smaller and niche master trusts, as well as those that didn't intend to become master trusts but were caught by TPR's definition. We have seen a persistent level of M&A and structural activity in the insured provider market over recent years and expect this will continue and lead to some consolidation of larger plans," Aon head of DC product EMEA, Tony Pugh, predicts.

The development of a secondary switch market, where employers transfers their staff from one master trust to another, is also expected to lead to industry consolidation.

The further round/s of consolidation could see 10 fewer master trusts as a result, LifeSight head of proposition development, David Bird, suggests.

Decumulation products

For those left standing, the products and services they offer are likely to evolve. An expected area for development is with decumulation products.

"The governance of master trusts is currently focused on accumulation," Pasa chair, Kim Gubler, says, "but as more people build up savings within them it seems a natural step to offer these savers a vehicle to deal with decumulation within that same structure. Some master trusts already offer this. We believe this is likely to increase as master trusts mature."

The People's Pension director of policy, Gregg McClymont, agrees that it is the very early stages of a regulatory regime for decumulation in occupational pensions, "so that leaves a blank canvas when it comes to the master trust arena".

There is also a question of relevance and timing for the mass auto-enrolment market pension funds because for some time there is likely to be only a small number of people retiring, even fewer of whom will have decent-sized pots, he adds.

Whether collective DC (CDC) will feature within DC master trust decumulation structures in the future is subject to debate.

Atlas Master Trust head of client strategy, Anish Rav, is firm in his view that master trusts will not use CDC, while Bird states: "Currently there doesn't appear to be enough demand from the market to persuade the regulator to introduce the regulations to permit it. If it was to happen, we would expect it to happen sooner for the post-retirement phase, rather than for the savings phase."

For a existing master trust to utilise CDC, the Pension Schemes Bill 2019 would need to pass into law; the master trust would need to make significant changes to its trust deed and rules; it would have to apply to TPR for authorisation as a collective money purchase scheme; must be able to prove that any collective and non-collective benefits are separated; and then there would be a whole new set of other requirements around the calculation of benefits, appointment of actuary, production of viability certificates etc, Parker warns. "This would be a significant undertaking for any master trust so it is likely to be a number of years before we see the first 'CDC master trusts'," he adds.

However, the Department for Work and Pensions had positive feedback from master trusts expressing their interest in offering CDC, van Rees notes.

Trailblazers

While it is currently the Royal Mail leading the way with CDC, as opposed to master trusts, TPR does expect them to be 'trailblazers' in a number of ways.

"We would love *[master trusts]* to fully embrace approaches to tackle climate change and ESG, look for innovation within at-retirement products and, because of the size and nature of their membership, we think they could also be leaders in promoting diversity within a trustee board," TPR executive director, David Fairs, stated at the recent Pensions Age Western Conference.

"This will be a key battleground for master trusts as they look to differentiate themselves in an increasingly competitive marketplace," Philp says. "As competition increases and, quite rightly, with an ever-increasing focus on value for money, master trusts will differentiate themselves based on factors such as technology, ESG and board diversity, and will end up leading the industry by raising standards across the piece."

Bird expects activity in all the areas stated by Fairs in the coming months and years, "but it is not yet clear whether the impetus for these changes will come from master trusts themselves, or if it will be forced upon them by the regulator," he says.

These changes could see the third generation of DC emerge within the next five years, which better address adequacy, coverage, engagement and technology, The Thinking Ahead Institute predicts.

'DC 3.0' will emerge out of further industry consolidation, resulting in large master trusts, it adds.

Master trusts will need to stop being 'isolated islands', Mercer Money proposition partner, Roger Breeden, agrees and instead will need to evolve "to make use of smart technology and regulatory data sharing developments to provide a member first experience".

As Rav says: "*[Authorisation]* provides employers and members with reassurance that master trusts meet the minimum requirements to operate, but the focus now has to be on getting the best member outcomes, which means putting the member at the front and centre of all future developments."

Written by Laura Blows