The Search for Quality: Group Personal Pension Plans or Master Trust?
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Why DC is important

Increasingly, savers in the private sector are saving for their retirement in Defined Contribution (DC) form – and this trend looks set to continue. The Pensions Policy Institute (PPI) predicts that the number of people saving in private sector DC schemes will exceed 16 million by 2020 – in 2011, 6.6 million were reported to be saving through DC. By contrast, less than 1 million people are currently saving for retirement through a private sector Defined Benefit (DB) scheme.

Employers can offer DC saving through contract-based pensions, such as Group Personal Pension Plans (GPPPs), or trust-based pension schemes. Trust based schemes can operate on a standalone basis for an individual employer but can also be part of multi-employer schemes, such as master trusts. Increasingly the realistic choice comes down to a GPPP or a master trust. But, how do employers choose between the two, seemingly competing, savings vehicles? As more and more employees’ retirement outcomes will be determined by their employer’s choice of DC arrangement, understanding the similarities and differences between them is increasingly important.

The difference between contract and trust-based schemes

**Contract-based schemes:** Under contract-based arrangements, the employer selects the pension scheme but the contract is between the employee and the pension provider, often an insurance company. Independent Governance Committees (IGCs) have recently been introduced as an additional layer of protection for members of workplace contract-based pension schemes.\(^1\)

**Trust-based schemes:** There is no contract between the pension provider and the employee for trust-based schemes. Rather, the employer appoints trustees to hold a scheme’s assets on trust, with the scheme being governed by the trust deed and rules. Trustees are required to act impartially in the interests of the scheme members and to protect the assets from intervention by an employer.\(^1\)

**Master Trusts** (trust-based pension schemes established to provide benefits to multiple employers) do not fit easily into either model as, under these arrangements, the employer selects the master trust rather than sets up the pension scheme. At the same time, unlike the contract-based model, there is not an individual contract between the pension member and the pension provider.\(^2\)

Source: \(^1\) PPI Briefing Note Number 78, The impact of DC regulation on employer scheme choice
\(^2\) PPI Comparison of the regulatory frameworks for DC pensions
GPPP and master trust — sharing common ground

Structurally, there are of course differences between GPPPs and master trusts, but generally they work in a similar fashion:

- Employers decide what they want from their DC arrangement, according to their own philosophy, resources, benefit package, history and membership profile.
- They then select either a GPPP or master trust, and they and their employees pay contributions.
- Quality GPPPs and master trusts offer many of the same fundamental features, for example a suitable range of investment options, engaging member communication and decision-making support, together with good quality, robust administration.
- Both are required to meet regulatory requirements — although they operate in different governance and regulatory frameworks.
- Assessing value is a requirement of both GPPP and master trust governance bodies, namely the Independent Governance Committee (IGC) or the board of trustees, respectively.
- Both approaches can meet the criteria and provide a process for auto-enrolment, and both will need to comply with charge-cap requirements for their default funds in the scheme.

As such, GPPPs and master trusts can be equally attractive to employers in that they offer simplicity and ease of access to do all the complicated things that employers have to do around their DC pension obligations and provision for employees. For example, much of the operational and governance burden is passed to the GPPP or master trust — helpful for many employers who do not have the time, resource, or knowledge to operate their own DC scheme.

This is not to say that employers devolve all of their responsibilities. They remain in control of the scheme design and contribution levels, setting and monitoring objectives for the scheme in terms of whether they are delivering better member outcomes, and ensuring that there is a strong understanding of their employees’ needs, to inform matters such as the optimum investment design, the styles and methods of member engagement and confirming that the scheme is delivering value for money for members.
Differences – a move to greater convergence?

In both GPPPs and master trust arrangements, there are specified individuals who are responsible for delivering good member outcomes and value for money for members. All of them are working within clearly defined regulatory regimes. However, the regulatory and governance frameworks in which GPPPs and master trusts operate are somewhat different, reflecting the fact that two similar DC products have evolved in different regimes.

Regulation

GPPPs are regulated by the Financial Conduct Authority (FCA), which falls under the responsibility of Her Majesty’s Treasury. Master trusts are regulated by the Pensions Regulator (tPR), governed by the Department for Work and Pensions and in some cases they are regulated by both tPR and FCA.

The FCA is widely regarded as a rigid, yet thorough, regime. For employers thinking about GPPP, this can be attractive as the conditions for offering a product, and the checks and balances that go on around the sustainability and suitability of product providers, are extremely thorough. And, with a remit that goes beyond pensions, the FCA has a very strong focus on consumers and fair treatment – providers must be mindful of treating customers fairly in a GPPP context.

The Pensions Regulator (tPR) sets a framework for all trust-based schemes – and especially master trusts – to aspire to excellent governance. Trustee knowledge and experience are central in this regime and they must adhere to the tPR DC Code of Conduct. This has recently been updated and further developed and in the near future, it is likely that master trusts will need to demonstrate their schemes meet strict new criteria, particularly before entering the market.

As part of the Pension Schemes Bill 2016, tPR is set to have greater powers to authorise and supervise master trusts. The introduction of the Bill will also require master trusts to demonstrate five key criteria: that persons involved in the scheme are fit and proper, that the scheme is financially sustainable, that the scheme funder meets certain requirements in order to provide assurance about their financial situation, systems and processes requirements, relating to the governance and administration of the scheme are sufficient, that the scheme has an adequate continuity strategy.

Governance

Similarly, there are differences in how GPPPs and master trusts are governed. In 2015, the FCA introduced Independent Governance Committees, or IGCs, for GPPPs. Master trusts will have their own trustee board.

In a GPPP Independent Governance Committee, there has to be a minimum of five members, and the majority, including the Chair, have to be independent. With a master trust board, there must be a minimum of three trustees on the board, the majority of which, including the Chair, should be independent.

In both cases, they are focussed on good governance and specifically how they are delivering value for money for members – in other words are the amounts deducted from members’ accounts fair value in return for the benefits received, by way of investment options, education and support and administrative processes.

The commitment to governance has, historically, been viewed as stronger in a master trust arrangement as the responsibilities are legislated for under established Trust Law. By contrast GPPPs have been driven and overseen by the product providers and although IGCs are now required, these are relatively new and are guided by FCA-set rules rather than long-standing legislation.

While the two governance structures are different, there are signs that similarities will, over time and in spirit, balance the technical and structural differences. For example, in setting the rules for IGCs, the FCA worked closely with the Department for Work and Pensions to ‘ensure that all members benefit from the same good quality standards regardless of type of workplace scheme’. Additionally there is growing industry recognition of the commitment to ‘sincere governance’, or the desire to do the right things by members, in both arrangements.

Responsibility for members

GPPPs originally grew in popularity as employers aimed to ease their governance and administration burden compared to trust-based alternatives: under a GPPP, the contracts belong to the individual members, therefore leavers cease to be a concern for an employer. However, the development of master trusts provided an alternative approach which enabled schemes to transfer many of the trustee duties and responsibilities. Leavers remain members of a master trust, and so there is a role for the employer to play. As such, they can maintain access to evolving benefits and economies of scale provided by master trusts.

Some employers feel that the transfer of member responsibility is too great under a GPPP and prefer to retain some of the control they would maintain through a master trust. For example if there is a future change of scheme provider, it is often a simpler process to transfer the existing membership and their accrued benefits under a trust-based arrangement. This is the trust based “transfer without consent” route for which there is no corresponding option in relation to GPPPs.

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Communication
One area of marked difference between GPPPs and master trusts, as a result of the different regulatory regimes in which they operate, is the statutory requirements around member communication.

As the FCA governs the contract for GPPP, it is very prescriptive about member communications and how they are delivered. This is driven by a need to ensure people have all the right information about their pension scheme, and that they are aware of every eventuality and risk. However, there has been criticism that the volume of information it requires to do this can sometimes make the communication unclear and impenetrable.

By contrast, tPR is considered to be less prescriptive and more pragmatic. It sets out an expectation that member communications adhere to the DC Code and are accurate, clear, and relevant and ideally provided in plain English. Additionally, trustees are encouraged to take account of innovations in technology that may be available to them and appropriate for their members – flexibility and consideration of the format of communications is important in a master trust arrangement.

Whether considering a GPPP or a master trust, employers would do well to look beyond the statutory requirements for member communication, which is just one area of member engagement. Ultimately, it is important that members receive information in a way that works for them as not all employees are homogenous and their needs around accessing information will be different. Information, education and guidance are all key components of a member engagement programme and should be available both offline and online.

Cost and value for money
Historically, GPPPs have been considered cheaper than trust-based schemes. The growth and development of master trusts have challenged this, and in today’s environment there is increasing convergence in charging structures between the two. Legislation around members introduced via auto-enrolment has brought in charge-caps for both arrangements. Additionally, assessments of value for money for members are required. While there is no clear definition of value in a DC context, it is increasingly expected to be considered relative to members’ needs in each scheme.

The attention and scrutiny on value for money for members is driving costs down and requiring IGCs and trustee boards to justify additional costs relative to the services they are providing and the benefits of doing so. The market is also very competitive right now, providing opportunities for employers to negotiate a good deal for their own GPPP or master trusts.

The search for quality
The similarities and differences between GPPPs and master trusts pose several challenges for an employer’s selection process. Clearly, there are strengths and weaknesses with both offerings and with greater convergence of the two expected in future – in terms of regulation, governance, charging structures and delivery of value for money for members – deciding which vehicle to use can be difficult.

We would suggest that, ultimately, the search for either a GPPP or a master trust is a search for quality: the quality of services, relative to the needs of each individual scheme and its members.

Employers need to be clear on their objectives and their understanding of their membership; and then look beyond the statutory requirements, look beyond the differences of the two and consider what the provider, whether GPPP or master trust, can deliver to meet those objectives.

About Aon Defined Contribution
Aon offers expertise across the range of DC issues, including strategy reviews, investment consulting, provider selection and monitoring. We also offer a range of DC products, including BigBlue Touch, a GPPP, The Aon MasterTrust and also a proposition for ‘own trust’ based schemes.

For more information, contact Tony Britton or Milan Makhecha.
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