

21st Century Trusteeship and Governance

Discussion paper

July 2016

The Pensions
Regulator

Introduction

The boards of occupational pension schemes carry out an important and difficult role. In aggregate, they are responsible for managing £1.8 trillion of assets on behalf of 32 million members and their role is becoming increasingly challenging in the face of fast-paced changes and growing complexity.

Effective trusteeship and governance are key underpinning factors in achieving good member outcomes. It is therefore essential that those who are responsible for running pension schemes and are entrusted with members' savings are the right people with the appropriate knowledge and skills, and have the right scheme management processes in place.

We are reassured by the dedication, skill and tenacity displayed by many trustee boards we meet, and we see examples of good governance in schemes of all benefit structures and sizes. But our ongoing surveys and engagement with schemes have also shown that not all trustee boards are meeting the standards of governance and administration we expect, or are finding it challenging to do so.

In the context of the changing pensions landscape and challenging economic environment – and with an eye to the needs of pension savers in the future – we are keen to examine in more depth how trustee boards can meet the challenge of scheme governance in the 21st century.

In the last year we have opened a debate with industry to consider what more can be done to support the trustees of pension schemes to fulfil their duties and improve outcomes for savers. We commissioned research and talked to trustees and stakeholders to better understand what drives effective trusteeship and governance. In this discussion paper we present what we have learned from our engagement and research, and explain what we will do next.

In line with our statutory objective to promote and improve understanding of the good administration of work-based pension schemes, our focus over the next year will be to use what we have learned to better support trustees through a more targeted communication and education strategy. While our research suggests there are many factors driving good governance and that there is not one single solution which will deliver it, education and training as a means of building trustee knowledge and skills are a key ingredient of a well-governed scheme.

Introduction

The findings of our research have already informed some of our education activities over the last year, in particular the development of our guides to support the new DC code, which cover a broad range of governance elements, but we need to do more to help trustees help themselves.

In parallel to refocusing our approach to education and training, we will also consider what else can be done (including changes to the legislative framework) to help trustees meet the standards of trusteeship and governance we expect of them. We are also keen to consider what steps could be taken in cases where trustees cannot or will not meet expected standards, in particular whether consolidation of sub-standard schemes should be given some consideration.

To help inform our thinking, **we welcome your views** on the topics and questions raised in this discussion paper by **9 September 2016**. The discussion questions are found throughout and then listed in total at Annex A for ease of reference, together with the contact details for responding. We are particularly interested to hear directly from trustees of occupational pension schemes, including professional and lay trustees.

Trustee landscape research and engagement

We commissioned two pieces of research to better understand trustees' ability to fulfil governance and administration roles in an increasingly complex pension environment.

In our quantitative research¹ conducted between March and May 2015, we carried out 800 in-depth interviews with trustees from defined benefit (DB), defined contribution (DC) and hybrid pension schemes with at least 12 members.

We followed this up with qualitative research² consisting of 30 in-depth interviews with scheme trustees, to deepen our understanding of the complex and sometimes contradictory issues identified in the first phase of research, in particular with regard to the structures and processes that promote the effective operation of trustee boards, the role of the chair, and the best way to deploy training and support tools to achieve effective trusteeship across schemes of all sizes and benefit structures.

We also observed some trustee boards. We sought examples of best practice and it gave us a deeper insight into the issues and challenges experienced by trustees day-to-day. A summary of the exercise and the key good practices/themes we observed are presented in Annex B.

We want to thank all the trustees who have taken the time to take part in our research or have invited us to attend their board meetings.

Finally, we held discussions with key stakeholders, trustees and industry experts through one-to-one meetings and workshops. These gave us a range of perspectives on trustees' weaknesses and strengths, the factors that affect their performance and what could be done to help trustees meet standards.

It is important to note that our findings are based on the accounts given by trustees in relation to their successes and challenges. We did not, for example, seek evidence to verify answers given. As such, the research findings should not be interpreted as a representation of levels of competence across the landscape. However, many of our findings are consistent with our other research and surveys on governance and administration³, what we have heard in our engagement with industry and the intelligence gathered from our ongoing involvement with schemes.

1
www.tpr.gov.uk/landscape

2
www.tpr.gov.uk/trustee-research

3
www.tpr.gov.uk/research

Key themes

Here we consider some of the key themes emerging from our research and engagement and their implications. For a complete overview of the findings, please refer to the research reports listed on the previous page.

Board effectiveness and the importance of diversity

Research findings

- ▶ To be effective, boards need a diverse mix of trustees who bring a balance of skills and experiences, professional backgrounds and interests.
- ▶ Non-professional trustees were found in three quarters of schemes and professional or corporate trustees were represented on half of the boards.
- ▶ Schemes with only professional trustees were more likely to have better governance arrangements.
- ▶ Professional trustees were reported to have a positive impact, bringing knowledge and expertise, commitment and impartiality to trustee boards. However, their use could also introduce risks such as conflicts of interest or over-reliance on a single individual.
- ▶ Three in four schemes that had recruited a member-nominated trustee (MNT) in the last 12 months reported that they had found it relatively easy to find a suitable candidate, despite the fact that over half of these appointments only involved a single candidate.
- ▶ Large schemes were more likely to be able to achieve their ideal board composition than small schemes.

Our landscape research has shown that diversity is a key benefit of the trustee model and that all types of trustees, whether lay or professional, have something valuable to bring to the running of pension schemes.

In particular, professional trustees (ie trustees who charge for their services or hold themselves out to be experts in trustee matters) can help improve the effectiveness of trustee boards (although we have seen that they can also bring risks that need to be carefully managed) and indeed many schemes have a professional trustee on their board.

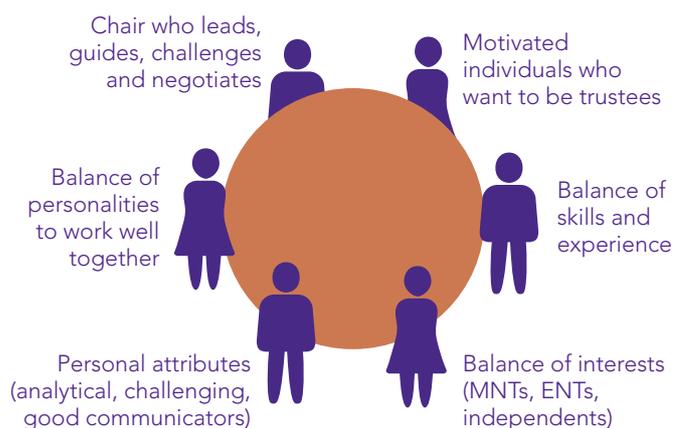
Key themes

Our scheme return data also suggests a trend in the ‘professionalisation’ of trustees, with the proportion of schemes without a professional trustee decreasing in the last five years. While the increased incidence of professional trustees might be partly driven by small DC schemes without professional trustees being more likely to wind up, increased governance requirements and the greater complexity associated with running pension schemes are also a key factor.

We do not expect all trustees to be professionals (although we do expect all trustees to behave professionally). However, unlike lay trustees, professional trustees are remunerated or hold themselves out as experts so it is therefore right to expect higher standards from them. Yet there is no barrier to entry into the market – anyone can become a professional trustee and unlike other professions, there is also no independent body regulating standards. While we have met many competent professional trustees in our engagement with schemes and have witnessed first-hand the significant benefits they can bring to scheme governance, we have also come across a few who are clearly unfit for the role. We therefore need to consider whether greater scrutiny and safeguarding is required, particularly given the trend in the professionalisation of trusteeship.

Initiatives such as those from the Association of Professional Pension Trustees (APPT) Council and the Pensions Management Institute (PMI) who are looking to introduce a new qualification for professional trustees (Diploma in Pension Trusteeship)⁴ can help raise standards among those who hold themselves as professionals. However, this qualification is not mandatory for all professional trustees.

The make up of an effective trustee board



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<http://bit.ly/PMI-Dip>

Q1: There are currently no barriers to entry for professional trustees. Should there be? For example, should all professional trustees be required to be qualified or registered by a professional body?

The role of the chair

Research findings

- ▶ Four in five schemes had a chair of trustees.
- ▶ Chairs of trustees were said to play a vital role in setting the approach to governance and scheme management.
- ▶ Their role required good leadership, communication, negotiation and people management and mentoring skills in addition to pensions knowledge.

Our research has shown the crucial and multi-faceted role the chairs of pension scheme boards play. We think it is important that chairs take a leading role in the running of their scheme. Competent trustees and effective governance are the two main factors of a well-run scheme and in our view it should be the chair's responsibility to:

- ▶ provide support to the trustees on their board so they have the appropriate knowledge and skills which enable them to fulfil their role competently
- ▶ co-ordinate and lead the work of the trustees to make it more likely that effective processes are in place so that:
 - risks and conflicts of interest are identified and managed
 - third-party providers and advisers are held to account
 - the board is sufficiently engaged with key governance areas such as administration, record-keeping and investment

Q2: Do you think it is the role of the chair of trustees to support trustees and use their leadership skills to improve the likelihood of appropriate scheme processes being put in place? Given the crucial role played by chairs, do you think more needs to be done to raise the standards of trustee chairmanship? For instance, do you think that chairs should be required to meet a minimum standard through having minimum qualifications or experience or belonging to a professional body?

As our research indicates, not all trustee boards (particularly in small schemes) have a chair, although this is not relevant for schemes with a single trustee. From 6 April 2015 many DC schemes have been required to have a chair of trustees who is responsible for signing a chair's statement confirming the scheme's adherence to various governance requirements. In public service pension schemes, the pension board provides a report on compliance, governance and administration in their annual report. We believe that such reporting requirements will help improve the effectiveness of those running the scheme and help deliver better governance. This raises the question as to whether DB schemes could benefit from a similar regime.

Q3: Should DB schemes be required to appoint a chair and report on compliance with governance standards?

We have already reflected some of our findings on what makes an effective trustee board and the role of the chair in our DC guides on the trustee board⁵ and scheme management skills⁶. Although designed to provide practical help to trustees to meet the standards set out in the revised DC code of practice, many of the approaches and practices described in the guides will be of use to the trustees and managers of all types of pension schemes, whether DB or DC and whether private or public sector. As we continue our work on 21st century trusteeship and governance, some of the material in the guides will evolve to form part of an overarching approach to assisting trustee boards of all scheme types to improve their effectiveness.

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www.tpr.gov.uk/trustee-board

6
www.tpr.gov.uk/skills

Meeting TKU standards and the role of training and development

Research findings

- ▶ An interest and desire to take on the role of trustee was seen as the most important quality. Basic understanding of how pensions work was considered crucial but detailed knowledge was seen as less important than personal attributes.
- ▶ Trustee boards generally believed that their knowledge and skills were good but they recognised some deficiencies, particularly around investments and assessing value for money.
- ▶ Half of schemes with one or more non-professional trustees did not believe that all of these trustees had a level of Trustee Knowledge and Understanding (TKU) that met the standard in our TKU code of practice (found at www.tpr.gov.uk/code7).
- ▶ Trustees almost universally believed they have sufficient training opportunities, although half of lay trustees did not undertake formal training in the last year.
- ▶ The main barriers to accessing formal training were cited as lack of time and lack of perceived need.
- ▶ Those accessing formal training (including our online Trustee toolkit) reported a positive impact.
- ▶ Over half of all schemes and 73% of small schemes had not documented or formally assessed trustees' learning needs in the last year. Some schemes relied on more informal approaches, including leaving it to trustees themselves or advisers to initiate training.
- ▶ Almost half of trustees saw training, information and education as a key route to raising standards. One in ten thought qualifications were key.
- ▶ Professional and corporate trustees were more likely to have relevant qualifications. A third of non-professional trustees had no relevant qualifications.

Key themes

We are concerned by some of the gaps identified in our research as we believe that good levels of trustee knowledge and understanding are a prerequisite for effective trusteeship and good governance in trust-based schemes. And while we acknowledge it is unrealistic to expect all trustees on the board to know all topic areas in detail, it is important to ensure basic knowledge is spread across the entire board to mitigate against risks of significant knowledge gaps or the board becoming over-reliant on a particular trustee or adviser.

We are therefore keen to explore how we can help all trustees have the skills and knowledge they need to fulfil their duties competently.

We were struck by the statistic that the trustee boards of almost one in five schemes were either not familiar with our TKU code or did not know whether their non-professional trustees had the level of knowledge and understanding that met the standards set out in our code. This suggests that we may need to explain more clearly what we expect trustees to do in practice to meet the TKU standard.

Q4: How can we help trustees to be aware of, understand and apply the TKU framework?

Newly-appointed trustees generally have a period of six months from being appointed to acquire the appropriate knowledge and understanding. However, even a new trustee is accountable in law and must be equipped to make the decisions with which he or she might be faced. Our research suggests that not all trustees have the required standard of TKU. Possible solutions to drive up compliance with this requirement could include making it mandatory for trustees to pass all relevant modules in the Trustee toolkit within six months. Another option would be to introduce a six-month probationary period for new trustees, with the appointment being formalised once the trustee has demonstrated they have sufficient TKU. This could encourage trustee boards to prioritise training and ensure new trustees undertake sufficient training in their first months.

Q5: Do you have any views as to how we can help new trustees bring their knowledge and skills up to the required standard within the statutory period? For instance would it be useful to make completion of the Trustee toolkit or other equivalent learning tool within six months mandatory? Or would the introduction of a six-month probationary period for new trustees help to meet standards of TKU? What are the difficulties associated with these options and how could these be solved?

Some of the trustees and stakeholders we talked to also suggested that all trustees, not just professionals and chairs, should be able to demonstrate a minimum level of competence. Qualifications were the second most widely mentioned route to raise the standard of trusteeship in our trustee landscape research (over 10% of schemes).

Q6: How can trustees demonstrate they have the minimum level of competence required to fulfil their role? For instance, do you think holding relevant qualifications is the right way to demonstrate competence? What are the difficulties associated with this option and how could these be solved? Are there other options?

Our research shows that the pace of change is one of the key challenges faced by many trustees in maintaining a sufficient level of knowledge and understanding to perform their role competently. Making qualifications a prerequisite for the role could help improve the standard of trustees appointed onto boards but continuous development is as, if not more, crucial to ensure boards remain effective. The new DC code outlines our expectations in relation to trustee boards maintaining training and development plans. Nevertheless, a more formal approach such as a Continuous Professional Development (CPD) framework could help ensure that training governance is better embedded in board operations and that trustees undertake the training they need. It could also help strike a better balance between helping trustees meet the required standards and discouraging people from becoming trustees.

Q7: Do you have a view as to whether a CPD framework would assist trustees to meet the challenges of scheme governance? What are the difficulties associated with this option and how could they be solved?

In line with our objective to improve governance and administration, we will continue to focus our efforts on supporting trustees in complying with their duties. The research underscores the importance of accessible and relevant training in helping trustee boards gain and maintain the knowledge and skills they need to fulfil their duties.

We have redeveloped our Trustee toolkit, which aims to help trustees meet the minimum level of knowledge and understanding required in legislation, to make it more accessible and drive up usage. We have also developed various tools (eg a learning needs analysis tool and assessment history) to help trustee boards identify where knowledge gaps exist and what they can do to address them, as well as to evidence levels of training among their scheme's trustees.

To support the pension board members of public service pension schemes, we have also delivered extensive educational engagement and developed a range of educational tools, including a new toolkit aimed at pension boards and scheme managers.

Lack of time was shown to be a key barrier to some trustees taking up training. Whilst there will always be a need for us to provide comprehensive written guidance, we are mindful of the importance of making that guidance as accessible as possible (in particular to those schemes who do not have access to extensive advice to help them interpret and apply regulatory requirements). We are therefore increasingly using tailored tools and products to get our messages through and support trustees. For instance:

- ▶ Our revised covenant guidance was accompanied by a series of downloadable and self-contained resources and tools such as checklists and user-friendly summaries and scenarios.
- ▶ Alongside our 2016 Annual Funding Statement we published a presentation summarising the statement's key messages which can be downloaded to use in trustee meetings and discussions.
- ▶ We regularly produce short educational videos which we make available on our YouTube channel and our website.

Key themes

- ▶ Our new DC code is intended to be used primarily online so trustees can easily identify the area they wish to focus on and link directly to the relevant practical guidance and underlying legislation as best suits them.

We plan to produce further educational material to help trustees identify the training they need and use training effectively such as a learning and development web page. We also have a dedicated trustee LinkedIn page, and templates such as study planners and learning logs.

Q8: What further education tools and products would you find useful to receive from us?

Managing conflict of interests

Research findings

- ▶ One in ten newly appointed MNTs had been co-opted or volunteered by management.
- ▶ Over half of chairs were selected by the employer.
- ▶ Some professional trustees explained that they can be under pressure to prioritise the employer's interest, although their professional integrity ensured that they acted impartially.
- ▶ The approach to selecting external advisers varied across schemes. In some schemes, particularly small ones, there was no formal process and appointments were made based on existing personal relationships or recommendations.

Our research shows that conflicts of interest are a topical issue. There are many circumstances in which they can arise, whether it is because some employers seem to have an influential role in the appointment of MNTs; some professional trustees may feel under pressure to treat the interests of the employer who pays their wage as a priority; or some schemes seem to have a very informal approach to appointing advisers and providers.

Key themes

Our revised DC code of practice and our guidance on conflicts of interest stress the importance of schemes having effective arrangements, including a written policy, to identify and manage conflicts. Nevertheless, this continues to be a challenging area. Our latest DC scheme research suggests that not all schemes, particularly small ones, have a written policy or maintain a register of trustee interests. The trustees we interviewed in our landscape research also explained that they understood the importance of having appropriate procedures in place but often described the difficulties associated with managing conflicts of interest and tensions within the scheme and between different parties. Efforts to deal with one source of potential conflict or lack of impartiality could sometimes result in further conflicts themselves.

Given the potential pervasiveness of conflicts and the difficulty some schemes face in dealing with them, this raises the question as to the best way to prevent adverse impacts from conflicts of interest. This could involve having robust processes in place to manage them or prevent them from happening in the first place, for instance by changing or improving the framework within which schemes operate such as appointment processes.

Q9: What do you think is the best way of managing conflicts of interests? How could the system be improved to reduce the likelihood of conflicts arising in the first place?

Engagement with key governance activities and working with third parties

Board engagement

Research findings

- ▶ The type and frequency of board interactions was found to vary.
- ▶ Almost half of trustee boards reported to meet at least quarterly but 7% of boards met less frequently than annually or had never met.
- ▶ Formal board meetings were not the only means of interaction.
- ▶ Time spent on duty also varied significantly by scheme size and benefit type. The trustee boards of half of 'DC only' schemes spent less than five days per year on their duties.

Our research shows there was a wide range of practices in relation to the frequency and degree of formality of board interactions and the amount of time spent on various areas of governance.

A low frequency of formal board meetings should not necessarily be interpreted as an indicator of low engagement with scheme governance overall. Other, less formal forms of interaction can be equally effective and more efficient in some circumstances. Time spent on trustee duties should also be proportionate to the complexity and risk profile of the scheme.

It is nevertheless worrying that some trustees appear to have little engagement with the other trustees on the board or with the ongoing management of the scheme, as we discuss in the following pages.

Administration and investment governance

Research findings

- ▶ Trustee boards described a wide range of approaches to key governance activities such as administration and investments.
- ▶ Trustee boards of smaller schemes or those with only lay trustees tended to be less engaged and activities were not planned in detail.
- ▶ Trustees often relied heavily on third parties.
- ▶ The vast majority (84%) of boards received formal reports on administration standards at least annually.
- ▶ The administrator typically attended board meetings at least annually, although 17% never did so.

In particular, we are concerned that the degree of continued interaction and involvement with administration processes was often said to be minimal, especially among smaller and medium-sized schemes. This echoes the findings of our previous governance and administration surveys and in particular our latest research⁷, which show that administration and record-keeping are seen as low priority by some schemes, particularly at the smaller end of the spectrum.

In our trustee landscape research, we found many examples of schemes with good administration processes (particularly among large schemes) such as formal and rigorous tendering processes, regular reviews of costs, strong negotiations of fees and services, proactive monitoring of service delivery through effective use of Service Level Agreements (SLAs) and high degree of interaction with administrators. However, we also came across examples of weaker administration governance processes such as a lack of strategy for assessing value, informal approaches to appointing administrators, lack of regular monitoring of activity (eg through attendance of administrators at board meetings and effective use of SLAs), reactive approaches to problems and general lack of detailed involvement.

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www.tpr.gov.uk/dc-2016

Approaches to investment governance were also found to vary in their degree of informality and the level of trustee involvement. While some schemes were found to have detailed formalised processes and actions, including regular reviews of the investment strategy, fund performance and advisers, others had basic and infrequent processes and actions such as little ongoing monitoring beyond annual reports and a lower degree of trustee involvement. Some trustees explained that they found it challenging to get involved in the development or review of the investment strategy and were more disengaged from the detail due to the complexity of the topic.

Whilst it is reasonable to expect that trustees primarily focus on strategic issues and leave the detailed operational day-to-day management of the scheme to third parties, it is nevertheless vital that they actively engage with them to ensure appropriate systems, reporting and controls are in place. Having a third party provider or adviser in place does not necessarily guarantee that governance is effective and good outcomes are being delivered for members. It is the responsibility of the trustees and their chair to hold third parties to account and scrutinise performance and outputs to ensure they are getting a quality service and value for money and that risks are being appropriately managed.

Working with advisers

Research findings

- ▶ Nine in ten schemes employed advisers but one in ten schemes reported they could rarely or never afford to appoint advisers – those tended to be small schemes.
- ▶ Trustees rarely disagreed with advisers although many scrutinised advice in detail. However, not all lay trustees were confident in their ability to challenge professional advisers.
- ▶ Some trustees, particularly in small schemes, commonly accepted advice without any detailed consideration and failed to regularly review the quality and value for money of the service they received.

In a similar vein, the research highlights the significant reliance that trustees place on advisers and the benefits that they can bring to running pension schemes. However, trustees remain responsible for the work carried out on their behalf and it is therefore vital that they critically engage with their advisers to ensure they make informed decisions and receive value for money. It is therefore concerning that some trustees do not feel equipped to challenge the advice they receive.

Improving engagement with governance and third parties

Given these findings, supporting trustees in delivering good governance processes and working effectively with third parties remains a key priority for us.

For instance, we intend to revise the online tool we developed to help DC trustees assess their scheme against the quality features so that trustees can assess themselves against the standards of conduct and practice set out in the new DC code. We will also produce a self-assessment tool for public service pension schemes to assess the quality of their governance and administration arrangements – the primary audience for this is those less knowledgeable scheme managers/boards whom we want to help identify practical steps going forward.

We have already produced a DC guide on investment governance⁸ to help trustees better understand their role in overseeing scheme investments and a guide on value for members⁹ to support trustees assess value for money in adviser, administration and investment costs in that area. We also published guidance to provide practical help on what a proportionate and integrated approach to risk management might look like for DB schemes and how trustees can use it as part of their plans for meeting their scheme's funding objectives.

We plan to develop further guidance on setting an investment strategy to help trustees understand and manage investment risk and engage critically with investment advisers.

We will provide tools to assist chairs and trustees in getting the most out of their advisers (eg checklists of questions) and promote good examples of administration practices.

Although our primary focus is on educating and enabling trustees, we will also continue to take enforcement action where appropriate. In particular, we view basic governance activities such as completing the scheme return or preparing the chair's statement as essential requirements for trustees – failure to meet these requirements may indicate wider governance failings in a scheme.

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www.tpr.gov.uk/invest

9
www.tpr.gov.uk/value

Key themes

We will therefore seek to enforce for such failures. In view of our latest DC schemes research, which suggests that a third of micro DC schemes and almost one in five small DC schemes are unsure about the requirements for the chair's statement, we anticipate that some of those schemes may find themselves facing penalties for non-compliance.

Q10: What do you think are the key challenges faced by trustees in engaging effectively with administration and investment governance and third party providers and advisers? What could we do to help them in addition to what we outline above?

Small schemes

Research findings

- ▶ Large schemes generally displayed better governance than medium and small schemes and schemes used for automatic enrolment were generally better run. For instance, small schemes were found to be less likely to have the support of external advisers, meet TKU standards and were less prepared for the new DC governance standards and charge controls.
- ▶ Trustee boards of DC only schemes were least likely to display good governance and less emphasis was placed on the governance of the DC element in schemes with both DB and DC elements.

The correlation between scheme size and governance behaviours is a theme that runs through all our surveys and research, with smaller schemes often associated with lower quality of governance and administration.

That is not to say that only large schemes are well governed nor that they are well governed in every respect. Some small schemes are run by very motivated and competent trustees and deliver good outcomes for their members. However, small schemes tend to face greater time and cost constraints and have less access to expert advice and it is therefore often more challenging for them to achieve good governance and keep up with legislative and regulatory changes.

Key themes

While we acknowledge that small schemes may need to approach governance processes differently from large schemes (although size is not the only factor that drives a proportionate approach – some small schemes can be complex and require more involved processes), we expect the principle of good governance to apply equally to schemes of all sizes.

We are concerned that the relative poor performance of some small schemes creates a whole class of pension scheme members who may be subject to unfavourable outcomes just because of the size of scheme they belong to. Supporting the trustees of small schemes through education and taking enforcement action against non-compliance with governance requirements are intended to help these schemes deliver better outcomes but may not address some of the underlying issues around their ability to achieve good value. We are therefore keen to have a debate with industry as to what other solutions may be needed to safeguard member benefits in those schemes.

Q11: What should be done with those schemes that are unwilling or unable to deliver good governance and member outcomes? In particular, should small schemes be encouraged or forced to exit the market or to consolidate into larger scale provision? Is regulatory intervention required to facilitate this or can it be achieved through existing market forces?

What we will do next

Our research shows that many trustees are dedicated, hard-working and manage their schemes efficiently and competently. We have also seen that some trustees are finding it harder to meet the standards we set and we are concerned that this could create poor outcomes for the members of these schemes or adversely affect the sponsoring employers. Driving up the standards of trusteeship and improving scheme governance therefore remains a priority for us.

Good governance relies on a number of factors and there is not one single solution which will lead to improvements across the board. However, we have also found that engaged and competent trustee boards are more likely to govern their schemes well and that education and training can play a vital role in helping trustees acquire the knowledge and skills they need.

Over the next year we therefore plan to increase our focus on educating and supporting trustees. As a risk-based regulator, education remains the most efficient way of reaching out to the thousands of schemes that make up the pension landscape, although we will also take enforcement action where appropriate, particularly in relation to failures to meet basic governance requirements.

We are not looking to impose new standards of governance or add to the burden on trustees – trustee duties are already set out in legislation and trust law, and our existing codes and guidance explain these legal requirements and outline the standards we expect trustees to meet. Our focus is to make sure that our education and communications are sufficiently clear to help all trustees understand what these standards are and act accordingly.

To achieve this, we intend to be more targeted in terms of the audiences we talk to and the content and format of our products and the channels we use.

Our landscape research, engagement with schemes and our other data (such as the scheme return and chair's statement) provide us with the information we need to segment the trustee universe so that we can establish different approaches according to the size, type and risk profile of schemes as well as other relevant factors.

What we will do next

In particular, we aim to focus our engagement on poorly performing schemes and disengaged trustees. We will focus our educational material and messages on those areas which we have identified to be of concern to us in this paper such as the role of the chair, the importance of training and development and meeting TKU standards, and the importance of prioritising key governance areas such as administration, record-keeping and investments and engaging critically with third parties.

Another key message from the trustee research is that good governance and the importance of board effectiveness are universal and are equally relevant to DB, DC and public service pension schemes although they may be applied differently depending on the particular characteristics of each scheme.

In the future, we aim to produce key overarching pieces of guidance to cover the principles or issues common to all schemes and produce separate guidance to cover issues which are specific to particular types of schemes. This would help streamline the amount of material we produce and make it more focused.

Q12: Would you find it useful to see overarching guidance covering issues common to all schemes, with more specific issues being covered in separate guidance?

We will continue to monitor the effectiveness of our communications and education approach in driving up standards of trusteeship and the quality of governance to identify what works and what doesn't. In parallel to refocusing our education approach, we will also work closely with our government partners and industry to consider what other solutions may be required (including changes to the legislative framework), particularly if some schemes are not improving despite additional targeted support. Responses to the questions we have raised in this paper will help inform our thinking in this area.

Q13: Do you have any other thoughts on the issues raised in this paper or on how standards of trusteeship and the quality of governance can be improved?

Annex A

Discussion questions at a glance

1. There are currently no barriers to entry for professional trustees. Should there be? For example, should all professional trustees be required to be qualified or registered by a professional body?
2. Do you think it is the role of the chair of trustees to support trustees and use their leadership skills to improve the likelihood of appropriate scheme processes being put in place? Given the crucial role played by chairs, do you think more needs to be done to raise the standards of trustee chairmanship? For instance, do you think that chairs should be required to meet a minimum standard through having minimum qualifications or experience or belonging to a professional body?
3. Should the requirement to appoint a chair and report on compliance with governance standards be introduced for DB schemes?
4. How can we help trustees to be aware of, understand and apply the TKU framework?
5. Do you have any views as to how we can help new trustees bring their knowledge and skills up to the required standard within the statutory period? For instance would it be useful to make completion of the Trustee toolkit or other equivalent learning tool within six months mandatory? Or would the introduction of a six-month probationary period for new trustees help to meet standards of TKU? What are the difficulties associated with these options and how could these be solved?
6. How can trustees demonstrate they have the minimum level of competence required to fulfil their role? For instance, do you think holding relevant qualifications is the right way to demonstrate competence? What are the difficulties associated with this option and how could these be solved? Are there other options?
7. Do you have a view as to whether a CPD framework would assist trustees to meet the challenges of scheme governance? What are the difficulties associated with this option and how could they be solved?
8. What further education tools and products would you find useful to receive from us?
9. What do you think is the best way of managing conflicts of interests? How could the system be improved to reduce the likelihood of conflicts arising in the first place?

10. What do you think are the key challenges faced by trustees in engaging effectively with administration and investment governance and third party providers and advisers? What could we do to help them in addition to what we outline above?
11. What should be done with those schemes that are unwilling or unable to deliver good governance and member outcomes? In particular, should small schemes be encouraged or forced to exit the market or to consolidate into larger scale provision? Is regulatory intervention required to facilitate this or can it be achieved through existing market forces?
12. Would you find it useful to see overarching guidance covering issues common to all schemes, with more specific issues being covered in technical guidance?
13. Do you have any other thoughts on the issues raised in this paper or on how standards of trusteeship and quality of governance?

Please provide your comments to the questions by
9 September 2016 by email to 21Ctrustees@tpr.gsi.gov.uk.

When responding, please provide your contact details and advise in what capacity you are responding (eg individual/organisation; your role; type and size of scheme you manage or advise (where applicable)).

Our preference is for responses in electronic format but alternatively you can post your response to: Amanda Latham, Regulatory Policy Directorate, The Pensions Regulator, Napier House, Trafalgar Place, Brighton BN1 4DW.

Annex B

Observing 21st century trusteeship in action

In parallel to undertaking further qualitative research on trustee board dynamics and training, we attended and observed the meetings of 12 pension schemes between November 2015 and January 2016 to gain a deeper insight into the issues and challenges experienced by trustees in their day-to-day working and seek examples of good practice.

We attended the meetings at the invitation of the chairs of trustees, after we extended a request for volunteers to them via the Association of Member-Nominated Trustees (AMNT), the Association of Professional Pension Trustees (APPT) and other stakeholders. We would like to express our sincere thanks to the chairs of trustees and trustee boards who invited us to observe their meetings.

The schemes we saw varied across a range of characteristics such as scheme size, board size, meeting length and frequency, board structure and automatic enrolment status.

We were particularly pleased to observe that, on the whole, trustee boards of all sizes and types were working well together and confident in using their judgement to make informed, documented decisions about how best to govern their scheme, based on its particular risks and characteristics.

Some good practices/themes which stood out for us include:

- ▶ **Effective chairing:** we observed confident and knowledgeable chairs who skillfully managed board discussions, ensuring that enough space was given to trustee scrutiny and questioning and encouraging participation from all trustees.
- ▶ **Engaged trustees:** we saw well-prepared and enthusiastic trustees who had taken the time to read their pack in advance of the meeting and were able to contribute fully to the discussions.
- ▶ **Flexible and proportionate board structures and practices:** we observed different models and practices adapted to the particular characteristics of and challenges faced by the scheme such as establishing new sub-committees to better respond to change; regular reviews of control mechanisms to ensure that meeting frequency reflected need; forward planners to ensure training and meetings took place around key changes and events.

- ▶ **Constructive and robust relationships with advisers and service providers:** we witnessed trustees openly challenging and questioning their advisers to ensure a good understanding of what was being discussed or agreeing action plans with providers to get at the root of the problems identified in member complaints and improve the quality of their processes.
- ▶ **Focus on members:** it was clear that members' interests were at the heart of the discussions we observed, whether it was in relation to discussing recent successful negotiations with the third party administrator to secure a lower-priced contract and better value for money, or discussions on the annual chair's statement and the importance of making it a useful tool for members rather than just a compliance exercise.

Our observations only represent a snapshot of positive trustee behaviours and are not, nor are they intended to be, a comprehensive account of how to run an effective scheme. And of course, not all behaviours were observed in all schemes.

Nevertheless, we found this exercise extremely useful and have used what we have learned to inform our thinking and to improve how we communicate with and assist trustees. We will incorporate more detailed case studies from these observations in our future work, for example in educational material such as our Trustee toolkit and in the guidance and tools we produce on specific areas of trustee duties.

How to contact us

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www.tpr.gov.uk

www.trusteetoolkit.com

Free online learning for trustees

www.pensionseducationportal.com

Free online learning for those running public service schemes

21st Century Trusteeship and Governance

Discussion paper

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