IMPORTANT NOTICE – TO BE READ IN CONJUNCTION WITH CONFIDENTIAL AAF 02/07 REPORT ON INTERNAL CONTROLS OF NEST

A report on the internal controls of NEST, prepared by NEST Corporation, to which is appended an assurance report on internal controls as at 31 July 2015 prepared by KPMG LLP (“the Reporting Accountants”) solely for NEST Corporation (“the Reporting Accountants’ Report”) is available for viewing subject to the following terms.

The Reporting Accountants’ Report has been prepared on a confidential basis in accordance with terms of engagement agreed by the Customer with the Reporting Accountants.

Following a request by NEST Corporation, the Reporting Accountants have exceptionally agreed to the posting of the Reporting Accountants’ Report on this website, on the basis set out in this Notice, to enable readers to verify that a report relating to the internal controls of NEST and prepared in accordance with the framework set out by the Institute of Chartered Accountants in England & Wales in Technical Release AAF 02/07 ‘A framework for assurance reports on third party operations’ as supplemented by the Master Trust Supplement, has been commissioned by NEST Corporation and issued by the Reporting Accountants, subject to the remaining paragraphs of this Notice, to which readers’ attention is drawn.

The Reporting Accountants wish readers to be aware that the Reporting Accountants’ work for NEST Corporation was designed solely to meet their agreed requirements and was determined by their needs at the time.

The Reporting Accountants’ Report should not be regarded as suitable to be used or relied on by any reader wishing to acquire any rights against the Reporting Accountants other than NEST Corporation for any purpose or in any context. In consenting to the posting of the Reporting Accountants’ Report on this website, the Reporting Accountants do not accept or assume any responsibility to any readers other than NEST Corporation in respect of the Reporting Accountants’ work for NEST Corporation, the Reporting Accountants’ Report, or any opinions that the Reporting Accountants may have formed and, to the fullest extent permitted by law, the Reporting Accountants will accept no liability in respect of any such matters to any readers other than the NEST Corporation. Should any readers other than the NEST Corporation choose to rely on the Reporting Accountants’ Report, they will do so at their own risk.
I’m pleased to present this report on internal controls on behalf of NEST Corporation, the Trustee of the National Employment Savings Trust (‘the scheme or NEST’). In this report we detail the processes and procedures in place for the governance and administration of the scheme.

NEST Corporation has been set up by the government especially for auto enrolment. We’re here to make sure that every employer has access to a workplace pension scheme that meets the requirements of the new pension rules. But we do more than just meet the regulatory minimum. NEST is designed to make auto enrolment straightforward, whether you’re a member saving with NEST, an employer using the scheme for your workers, or a professional helping your employer clients.

This report has particular significance for us as it forms part of a suite of governance assurance measures we’ve undertaken in our members’ interests since the Scheme was established.

At NEST we take governance extremely seriously. Auto enrolment is bringing millions of people into workplace pension saving, many for the first time. So it’s important that we do all that we can to build and safeguard confidence in pensions for this new generation of savers. Robust governance standards that are clearly implemented across the industry are one step towards this goal.

NEST is already one of only a handful of schemes to have achieved Pensions Quality Mark (PQM) READY status. That means employers choosing us for their workers can be assured that they’re getting a scheme with good governance, low charges and clear member communications. We also published a voluntary governance statement in 2014 setting out how we deliver against the quality features for defined contribution (DC) schemes identified by The Pensions Regulator (TPR). This first report against the master trust assurance framework builds upon these excellent foundations to demonstrate our continued commitment to scheme governance.

It’s important for our customers and members to understand that this report, together with the independent assurance from KPMG, as the next step in our governance assurance work, isn’t just a paper exercise for us. We’ve undertaken it thoroughly, transparently and in accordance with best practice. Everything we do is focused on our members’ interests. That’s why we’ve made sure this AAF report delivered value for money for our members and we have used it as an opportunity to learn and improve in our efforts to deliver member outcomes in a well-controlled environment.
NEST Corporation continues to work closely with government, industry, trade and consumer bodies to ensure our members’ interests are represented. NEST Corporation also continues its research-led approach to make sure we keep meeting member and employer needs.

This report offers information and assurances about our processes. It details the robust controls we have in place to assist us in delivering high quality services to employers and members alike.

We hope that this will contribute towards building a safer and more secure pension saving landscape for the automatically enrolled generation. We look forward to supporting millions more members in saving confidently for their retirement.

Chair of NEST Corporation
12 October 2015

This report considers the control framework as at 31 July 2015. It’s been prepared in accordance with the Institute of Chartered Accountants in England and Wales (ICAEW) master trust supplement to AAF 02/07 standard.

We summarise the 38 control objectives from the master trust supplement in section 4. We then demonstrate the procedures and controls that we use to meet these objectives in section 5. These processes and controls have been, and reported on, by KPMG LLP.

This report looks at the controls operated by NEST Corporation over the affairs of the master trust, which include monitoring operational controls performed by third parties. However, this report does not include those operational controls which are the responsibilities of the third party service providers, and which are included in their own control reports.
As Trustee of the National Employment Savings Trust, we are responsible for the identification of control objectives relating to governance and administration in the operation of NEST and the design and implementation of the procedures and controls to provide reasonable assurance that the control objectives are achieved. These objectives are derived from the DC code of practice and DC regulatory guidance and are set out in the ICAEW technical release 'Assurance reporting on master trusts (Master Trust Supplement to ICAEW AAF 02/07)'.

In carrying out those responsibilities we have regard not only to the interests of employers and members of NEST, the needs of the trust business and the general effectiveness and efficiency of the relevant operations.

We have evaluated the effectiveness of NEST Corporation’s procedures and controls having regard to the Institute of Chartered Accountants in England and Wales Technical Release AAF 02/07 and the criteria for master trusts set out therein.

We set out in this report a description of the relevant procedures and controls together with the related control objectives which operated as at 31 July 2015 and confirm that:

- the report describes fairly the procedures and controls that relate to the control objectives referred to above which were in place; and
- the procedures and controls described are suitably designed such that there is reasonable assurance that the specified control objectives would be achieved if the described procedures and controls were complied with satisfactorily.

Chair of NEST Corporation
Signed on behalf of NEST Corporation
12 October 2015
Controls framework

Organisation overview

NEST is a low-cost, Trust-based occupational pension scheme which was established in 2010 to support the Government’s pension reforms; and specifically to facilitate the automatic enrolment of eligible jobholders into a workplace pension scheme. NEST offers easy online access; clear communications; high quality governance and an award winning investment strategy.

NEST Corporation is the trustee of NEST (the ‘Trustee’). It is made up of a number of members, who we call ‘Trustee Members’. As Trustee, NEST Corporation has a fiduciary duty to run the Scheme in the best interests of its members. The Trustee Members are appointed by the Secretary of State for Work and Pensions. The Trustee receives advice and assistance on the development and operation of the Scheme from a “Members’ Panel” which represents the member’s perspective of the Scheme and an “Employers’ Panel” which represents participating employers. In addition to consulting the panels in connection with the operation and development of the Scheme, the Trustee also consults them when specifically required to by legislation e.g. when making changes to the NEST Rules.

Unlike any other occupational pension scheme trustee, the Trustee has a Public Service Obligation (PSO) to accept any employer who wishes to use NEST in order to meet its employer duties, provided the employer is willing to agree to the terms and conditions of the Scheme. Employers participate in the Scheme on acceptance of the employer terms and conditions. These terms and conditions are reviewed on at least an annual basis and as necessary following a change to relevant legislation.

Once a member is enrolled into the Scheme, they can log in to their own individual member account where they can review the personal details held, make additional voluntary contributions, change their investment fund and cease contributions. A member can continue using NEST throughout their working life, regardless of a change of employment or of personal circumstances.

Since the staging process for automatic enrolment began in October 2012, NEST Corporation has enrolled over 2 million members into the Scheme from more than 20,000 employers.

Restrictions

Under the Pensions Act 2008, certain restrictions were placed on the Scheme. These include an annual contribution limit, which is reviewed on an annual basis and updated in line with the average earnings index and, following a formula set out in the NEST Rules. This limit will be removed with effect from 1st April 2017. In addition to the annual contribution limit, restrictions on transfers into and out of the Scheme are in place until 1st April 2017.
Charges

There is no charge for initial set-up or on-going administration with NEST for either employers or delegates, i.e. a third party that the employer has asked to administer their pension arrangements for them. The Scheme has the same charges for all members, irrespective of who their employer is, the level of their contributions or the retirement fund that they invest in. These charges are made up of two parts:

- A contribution charge of 1.8 per cent on each new contribution into a member’s retirement fund; and
- An annual management charge (AMC) of 0.3 per cent on the total value of a member’s fund each year, which is reflected in the unit price.

Every three years, the Trustee also reviews a Value for Money report collating information from investment reports and market data to assess the quality of service provided compared to the costs and charges applied to the membership.

NEST Corporation’s operating model

NEST Corporation operates an outsourced business model and has outsourced many of the key services in relation to the running of the Scheme. This report focuses on the controls operated by NEST Corporation over the affairs of NEST, which includes monitoring the operational controls performed by the third parties. These operational controls are not included in this report as they are the responsibility of the third party service providers and are included in their own internal controls reports. The main operations outsourced to the third party service provider by NEST include but not limited to:

- **Scheme Administration**, including onboarding of new employers, maintenance of member records, processing of contributions and the payment of member benefits. This is undertaken by Tata Consultancy Services (TCS)
- **Fund Administration**, the set of activities which support the running of the investment funds that we offer to members, including directing the right contributions to the right investment managers, and working out the unit prices of the Scheme’s investment funds. This is undertaken by State Street Bank (SSB or Fund Administrator)
**Fund Management**, managing the investments used by NEST Corporation as building blocks to make up the investment funds that we offer to members. This is undertaken by a range of fund managers:

- global developed equities - UBS Global Asset Management
- global real estate equities - Legal & General Investment Management
- sterling liquidity (money market investments) – BlackRock
- sterling corporate bonds – Royal London Asset Management
- UK gilts - Legal & General Investment Management
- UK gilts - State Street Global Advisors
- UK index-linked gilts - State Street Global Advisors
- global emerging market equities – Northern Trust Global Investment
- global emerging market equities – HSBC Global Asset Management
- Sharia-compliant global developed equities - HSBC Global Asset Management
- global ethical developed equities - F&C Investments
- ethical sterling corporate bonds – F&C Investments
- direct UK commercial property – Legal & General Investment Management

As a non-departmental public body, NEST Corporation is subject to the Public Contracts Regulations 2015 and has incorporated robust procurement processes where applicable.

**Market recognition**

NEST has been awarded a 4 Star rating in the automatic enrolment pension category from the leading independent financial research company, Defaqto. Their ratings are designed to show the level and quality of features and benefits in a financial product to help people make better financial decisions. The 4 Star Rating indicates that NEST provides a high quality offering in the automatic enrolment market. In addition, NEST has received numerous awards for our market-leading approach to communications, the NEST Connect service for intermediaries helping their employers with automatic enrolment and for our investment approach.
Organisational structure

NEST Corporation is sponsored by the Department for Work and Pensions (DWP). It’s accountable to Parliament through the DWP but acts at arm’s length from Government and is largely independent in its day-to-day operations.

NEST Corporation’s powers are derived from four sources: the Pensions Act 2008, which sets out its functions and powers as a Body Corporate; the Scheme Order, which sets out its powers as a Trustee; in trust and pensions legislation and under common law. A set of Scheme rules, contain further Trustee powers and duties. When taking a decision, NEST Corporation must be clear that it has the power to do so and the source of that power.

The Trustee

The Trustee comprises a Chair, a Deputy Chair and up to 13 other Trustee Members. The Trustee meets regularly through the year to develop and agree strategy, monitor and oversee performance, discuss and explore issues relevant to the governance and administration of the Scheme and to make decisions; dates for the meetings are agreed in advance and follow a formal agenda. On an annual basis, the Trustee carries out a board effectiveness review for the Trustee board as a whole, and also for each of its Committees that exercise delegated power. At least every three years, this Trustee effectiveness review is carried out by an external facilitator.

Newly appointed Trustee Members are expected to complete The Pension Regulator’s Trustee toolkit and also identify any gaps in their knowledge and understanding to help to ensure that training needs can be addressed and they can be kept up to date with issues regarding the Scheme’s operations and the legislative environment in which it operates. Trustee Members also complete on a regular basis a number of internal training programmes.

Trustee Members identify, monitor and manage conflicts of interest in accordance with the conflicts of interest policy and the statutory provisions.

Delegation of authority

The Trustee has a power to delegate any of its activities to its committees, or to the Chief Executive Officer. A documented Schedule of Reserved Powers and Delegations, which details the reserved and delegated powers of the Trustee, is reviewed annually.

Delegation to Committees

A number of Committees have been established, each of which is chaired by a Trustee Member and on which Trustee Members sit and representatives from the Executive Team attend. A Committee meeting cannot take place unless an agreed minimum quorum is achieved.

The terms of reference for each Committee outline the responsibilities of each Committee, and also require the Committee to report back to the Trustee on the areas it is responsible for.
The responsibilities of each Committee are detailed below:

- **The Audit Committee** is responsible for the integrity of the financial statements for NEST Corporation and the Scheme; for approving and monitoring the internal control framework; and for the effectiveness of audit and compliance functions.

- **The Determinations Committee** is responsible for decision making on the second stage of cases made through the Scheme’s internal dispute resolution procedure; for ensuring that the processes for dealing with disputes are fit for purpose; and for determining on these cases.

- **The Investment Committee** is responsible for the overall investment strategy and additions or changes to approach or to the investment funds made available to members. The Committee also monitors investment performance and operational investment risks.

- **The Nominations and Governance Committee**’s role is to ensure sound corporate governance within NEST Corporation; lead the recruitment for the appointment of the CEO of NEST Corporation; and, to provide support and assistance, as required, for the recruitment of Trustee Members by the Secretary of State.

- **The Risk Committee** is responsible for advising on overall risk strategy and considering all aspects of risk, and the management of those risks, that could affect NEST Corporation and the Scheme.

- **The Remuneration Committee** is responsible for setting the remuneration of the CEO and for providing advice on setting the remuneration of other employees of NEST Corporation, together with oversight of NEST Corporation’s organisational culture and values. The Secretary of State determines the fee levels for Trustee Members.
The Propositions Committee is responsible for overseeing the strategic development of the Scheme, in respect of the proposition offered to members and to ensure that the proposition offered meets the needs of our members, employers and target market.

Delegation to the Chief Executive Officer (CEO)

The Trustee has delegated a number of powers to the CEO including a broad power to be responsible for the efficient and effective day-to-day operation of NEST Corporation and the Scheme. The CEO is supported in exercising these powers by eight Accountable Executives who assist with the delivery of the delegated functions. Although many powers are delegated to the CEO, the Trustee remains ultimately responsible for the operations of NEST Corporation and the Scheme.

To help ensure that delegated powers are being properly exercised, the Trustee receives feedback and assurance from the CEO, and the other Accountable Executives, directly and via its Committees.
NEST People and culture

NEST Corporation recognises that its greatest asset is the people who work in the organisation. Recruitment and retention of staff, and the working environment are therefore both key areas of focus for the Trustee and Executive Team alike.

Recruitment into NEST Corporation follows a thorough employee vetting process designed to ensure that the candidate displays the competence to successfully undertake a role and subscribes to NEST Corporation’s mission and values. New employees are briefed on the operation of NEST Corporation through an induction process that includes training on what is expected of them whilst working in a regulated environment.

The working environment within NEST Corporation is based on a culture established in accordance with a set of ethical principles. These are expounded in a Code of Conduct which is issued to all members of staff, and backed up with specific policies addressing such areas as:

- Data protection;
- Information security;
- Competition law;
- Anti-bribery and corruption
- Procurement;
- Conflicts of interest;
- Equality, diversity and dignity at work;
- Gifts and hospitality;
- Travel and expenses;
- Conducting political activities;
- Staff share dealing policy;

On an annual basis or when a new employee has joined their directorate, the Accountable Executive will seek confirmation that their teams have read and understood the NEST Corporation Code of Conduct.

NEST Corporation recognises that it has a responsibility to foster a culture in which acting with integrity is the norm and which enables staff at all levels of seniority to act in an open and honest manner. This is supported by a comprehensive system of internal communication and briefing including a fortnightly summary of current NEST Corporation news and key outcomes from Committees.

NEST Corporation believes that the principal ways in which it can drive engagement with its ethical principles and the culture of integrity is to help ensure that employees remain competent to carry out their roles, and that they are well supported by management to do this, and to prepare for future career development. To this end, NEST Corporation has a learning and development budget, used to address both identified training needs and to help staff develop skills required to enable them to further their careers. Ongoing assessment of competence and performance is assured by a formal annual appraisal process for staff at all levels.
Risk management framework

NEST Corporation has a Risk Directorate that is responsible for establishing and embedding NEST’s Risk Management Framework. The Risk Management Framework is designed to help all parts of the organisation identify, assess, manage and monitor significant risks that exist within their environment, including operational, financial, and regulatory and compliance risks. The Risk Management Framework is reviewed annually to ensure it accurately reflects NEST Corporation’s risk management objectives and is approved by the Risk Committee.

Risk registers

Across the organisation, each Executive Director must maintain a risk register and nominate a Risk Coordinator who will liaise with the Risk Directorate to ensure that risks are identified, included in the risk register and that the risk register remains accurate.

Once a risk has been identified, it is assessed for impact and likelihood on a scale of 1 to 5 using a risk scoring matrix which contains descriptive examples to ensure risks are rated consistently across the organisation. All risks have a named owner who is responsible for accurately describing and rating the risk. All risks contained on a risk register are reviewed on an ongoing basis for continued relevance, to ensure that the risk ratings remain accurate and to take account of any additional mitigating activities that have taken place or are planned.

Commitment to Risk Management processes at a senior level is high; NEST’s Executive Team are presented with a Risk Dashboard every month that highlights key risks from across the organisation and outlines any key changes and areas of particular interest. The dashboard is used to initiate conversations about risk; helping to raise awareness and drive mitigation activities.

The Risk Committee

The Risk Committee is chaired and attended by Trustee Members and meets on average six times a year. The Committee provides independent oversight of the Risk Management Framework and challenge to the control strategies surrounding key risks. They undertake ‘deep-dives’ and scenario analyses of specific areas of risk as a method of gaining assurance that risks are being managed effectively.

The Committee also receives a copy of the Risk Dashboard to ensure they have oversight of the highest rated risks across NEST Corporation and NEST.
Operating an outsourced model

NEST Corporation operates an outsourced model enabling it to obtain, and effectively scale, services from third party suppliers. NEST Corporation’s approach to its outsourcing model is designed to provide effective internal controls for investment and fund administration, Scheme administration and IT.

A vital mechanism of the outsourced model is how NEST Corporation appoints, monitors and manages key service providers and suppliers to assist in delivering a quality pension scheme. NEST Corporation’s Purchasing Policy provides the framework for how procurement of these key service providers and suppliers is undertaken. The purchasing policy is aligned to legislation, The Public Contracts Regulations 2015. On the basis stipulated by the contractual agreement the performance of key service providers and suppliers is assessed by the relevant business area.

Business Continuity and Disaster Recovery plans and associated policies are in place, not only for NEST Corporation but also specifically for each of its key service providers. These plans are reviewed on at least an annual basis with the aim of ensuring that they remain fit for purpose.

Investment

The investment objectives for the Scheme are set out in its Statement of investment principles (SIP) which the Trustee is required to prepare under section 35 of the Pensions Act 1995. The SIP is reviewed every 3 years, with the last review in April 2015, and without delay following a change in investment approach. The Members’ and Employers’ Panels are consulted prior to any changes to the SIP.

Based on NEST Corporation’s understanding of the diverse needs of NEST membership, NEST Corporation has developed an approach to investment that offers:

- a well-constructed default strategy that has clear return objectives and a carefully managed risk profile, called the NEST Retirement Date Fund
- a selection of clearly differentiated fund choices for those who have different risk appetites, investment objectives or want an approach that matches their beliefs or faith.

The day-to-day management of NEST members’ funds is performed by external fund managers, each of which is authorised and regulated by the Financial Conduct Authority (FCA) or the regulatory body in the country the fund is domiciled. The funds and fund managers are selected through a competitive tender process. Professional advice from the Trustee’s in-house investment team and independent external investment advisers is obtained and considered in the selection of these funds and fund managers. As part of this selection, a due diligence process is performed to ensure that the assets are invested with sufficient security and liquidity and that each of the fund managers is of the appropriate quality and calibre to ensure the quality and profitability of the assets.

NEST Corporation receives regular AAF 01/06 or ISAE 3402 assurance reports from the Fund Administrator and all of the fund managers and assesses the findings of these reports with the aim of checking the adequacy of suppliers’ controls and that these controls are being effectively operated.
The Scheme Management and Assurance (Investment Admin) team monitor the performance of NEST funds on a daily basis with the aim of ensuring that members’ money is managed responsibly. Regular monitoring by the Scheme Management and Assurance (Investment Admin) team and the Investment Directorate is designed to ensure that decisions are made in the best interests of members and that the data available to the Investment Committee is based on accurate and complete information. On a quarterly basis, the Investment Committee is presented with Management Information (MI) on fund performance, fund strategy and the current investment risk environment.

Administration

The administration of the Scheme is outsourced to Tata Consultancy Services Limited (TCS or Scheme Administrator). The Scheme Management and Assurance (Scheme Admin) team and the Scheme Administrator Contract Manager provide assurance to the Trustee, CEO and Executive Team on an ongoing basis that this relationship continues to work effectively.

The Scheme Administrator’s role includes managing employer participation, enrolling members, collecting contributions, managing accounts, passing funds to and from the fund administrator and managing retirement and death processes. Each of these processes is designed by the administrator and agreed by NEST Corporation, based on a set of functional specifications established by NEST Corporation and underpinned by contractual requirements designed to ensure that the service provided is in line with market best practice.

The Trustee recognises ensuring contributions are paid in a timely fashion is of primary importance. As a result, TCS and NEST Corporation together have devoted significant effort to developing processes and controls designed to ensure contributions are received in time and that appropriate action is taken in the event that contributions are late.

The Scheme Administrator provides detailed feedback to NEST Corporation on a monthly basis with the aim of providing adequate assurance that services are being provided in line with levels of service that members and participating employers deserve. The Scheme Administrator also provides the Trustee with an AAF 01/06 assurance report detailing the adequacy and operation of their internal control framework.

NEST Corporation IT Services and Information Security

The work of NEST Corporation IT and Information Security teams aims to ensure that NEST Corporation and its outsourced providers operate in an efficient and secure IT environment. To support this aim, all NEST Corporation IT users are required to undertake information security training, supported by policies on data protection, information security and records management. NEST Corporation is certified against ISO 27001.

IT infrastructure is outsourced to an external IT service specialist, Capita, who is also certified against ISO 27001. Access to the NEST Corporation IT network is through a series of logical access controls, established by NEST Corporation and administered by the outsourced provider, and is regularly reviewed to help ensure that access rights are granted appropriately.

One of the contractual responsibilities of the IT Service Provider is to help ensure that NEST Corporation’s systems and data are backed up in accordance with the Business Continuity Disaster Recovery (BCDR) policy that is in place and that there are appropriate recovery time objectives in place, designed to ensure that systems are operational following a disaster event, these arrangements are tested regularly.
Communications

NEST Corporation produces clear and concise communication materials, for both members and employers, that are designed to be easy to understand and engaging. These communications are underpinned by NEST’s Golden Rules of Communication document. This document details 8 rules, such as use of practical language, and real life examples, that have been incorporated into all standard communication templates to help ensure that all communications are relevant to their audience.

For employers, a suite of communications relevant to the setting up and management of the Scheme is available through the NEST Public Area Website (PAW) and an online help centre.

For members, the communications issued to them are tailored to their needs at each stage of their journey to retirement. On joining the Scheme, members are provided with information on investment choices and about how their level of contributions is a key factor in determining the overall size of their pension fund via the NEST Member Welcome Pack, and on an annual basis thereafter via the Annual Statement. As members approach retirement they receive information on the options available to them starting from 6 months before their retirement date. The ‘taking your money out of NEST’ document is reviewed on an annual basis to check compliance with legislative and regulatory requirements.

Information relating to NEST’s costs and charges is available from the PAW which can be accessed by both members and employers at any stage. This information is reviewed on an annual basis to help ensure it remains accurate and takes into account NAPF guidance on Pension charges.

Before a new communication is issued to an employer or member it is subject to the Marketing, Communications and Approval (MCAP) process. This process is designed to ensure that any communication issued is consistent with specified brand guidelines and messaging in addition to legislative and regulatory requirements. Communications are reviewed for ongoing accuracy and completeness.
Monitoring activity

Monitoring activity is carried out throughout NEST Corporation to give assurance to the Trustee, Audit Committee, CEO and Executive Team that the Scheme is being operated by NEST Corporation and by its suppliers in accordance with relevant legislative and regulatory requirements and adequate controls are in place and operating effectively.

Using the ‘Line of Defence’ model for monitoring and audit functions, the first line of defence monitoring is primarily undertaken by our Scheme Administration and Investment Administration teams. Their activity is designed to ensure that the activities of our outsourced providers are compliant with legislation, regulation and the terms of the outsourcing contracts.

The second line of defence is provided by the compliance team and by specialist teams within the Risk Directorate (Financial Crime Prevention, Information Security) who provide assurance that within NEST Corporation the policies and processes in place are sufficient for the purposes of compliance with regulatory and legislative requirements.

The third line of defence is the internal and external audit and assurance functions. External audit activities of NEST Corporation are conducted by the National Audit Office (NAO) and external audit of the Scheme, and the assurance of this AAF 02/07 report, is conducted by KPMG. To help ensure absolute independence of internal audit activity of NEST Corporation and the Scheme, this function is outsourced to Ernst and Young.

Both functions design and carry out an annual audit plan, reviewing the operation of NEST Corporation and the Scheme, where appropriate, and the activities of both the 1st and 2nd Line of defence to help ensure that they are carrying out their activities competently and in a compliant manner. Both internal and external auditors have unrestricted access to any aspect of the organisation; in addition the heads of all second and third line functions have unrestricted access to the CEO and Chair of Audit Committee.

Where second or third line monitoring identifies failings in process or practice, these failings are evaluated and action points are agreed with the appropriate member of the Executive Team and assigned to a named individual to resolve. On a quarterly basis, all monitoring and audit functions throughout NEST Corporation report findings of their investigations, and escalate any issues, to the Audit Committee. Actions assigned through monitoring or audit activity are tracked and process owners are made aware that failure to complete actions in the timeframe set by the monitoring function will result in them being required to provide an explanation to the Audit Committee.
Summary of control objectives

Set out below is a summary of the control objectives that the Trustee of NEST has identified as being relevant to the governance and administration in the operation of NEST. Section 5 of this report that follows describes the procedures and controls which are designed to meet these control objectives.

**Safety of assets and records**

**Commercial and business risks**

1. Discontinuance plans, which address how member assets or entitlements are safeguarded in the event of the master trust or any key service provider failing, are documented, approved and maintained.

**Business and disaster recovery**

2. Data and systems are backed up regularly, retained offsite and regularly tested for recoverability. Business and information systems recovery plans are documented, approved, tested and maintained.

3. The capacity of an administration system to take on new business is assessed, approved and regularly monitored.

4. New business take-ons are properly established in accordance with master trust’s rules and contractual arrangements.

**Data quality and security**

5. Member data is complete and accurate and is subject to regular data evaluation. Data transmissions are secure and appropriate measures are implemented to counter the threat from malicious electronic attack.

6. Physical and logical access to computer systems, and member and master trust records and data, is restricted to authorised persons.

7. IT equipment is maintained in a controlled environment and the maintenance and development of systems, applications and software is authorised, tested approved and implemented.

**Protection of assets**

8. Member assets or entitlements are safeguarded from loss, misappropriation and unauthorised use in accordance with a defined policy.

9. Cash is safeguarded and all payments are suitably authorised and controlled.

10. Financial protection available to members in the event of default is assessed and documented, and communicated to employers and members on request.

11. Investment decisions relating to the selection of investments on regulated markets and unregulated investments are researched, authorised and monitored.
Assessing value

Assessment of value for money

12. A value for money review is undertaken and this review is documented, approved and findings actioned.

Communication of costs and charges

13. A complete and accurate list of the types of costs and charges incurred by members and employers is documented, monitored and approved.

14. Disclosure of information on costs and charges borne by members is provided to employers at the point of selection and is complete and accurate.

15. Disclosure of information to members of costs and charges (rates (%) and amounts (£)) are complete and accurate.

Assessment of investment options

Appropriateness of the default strategies

16. The design and ongoing suitability of the default strategies is regularly reviewed and monitored. This review is documented and approved.

17. The performance of the default strategies and funds within the default strategies are regularly reviewed and monitored. This review is documented and approved.

Appropriateness of the other investment options (i.e., non-default strategy investment options)

18. The range and risk profile of other investment options are documented, approved and regularly reviewed for suitability. This review is documented.

19. The performance of other investments options is regularly reviewed against relevant investment objectives and (where available) industry benchmarks. This review is documented and approved.

Identification of investment objectives and assessment against them

20. A complete and accurate description of all investment options is maintained and approved.

21. A Statement of Investment Principles (SIP) is documented, approved and regularly reviewed.

People

Conflicts of Interest

22. Conflicts of interest are identified, recorded and managed in accordance with a defined policy which is regularly reviewed and approved.

Fit and proper trustees

23. Fitness and propriety requirements are recorded and managed in accordance with a defined policy which is regularly reviewed and approved.

24. The fitness and propriety of trustees is regularly reviewed and monitored prior to appointment and thereafter. This review is documented and approved.

25. Trustee skills and knowledge are managed and maintained in accordance with an approved training programme. The training programme is regularly reviewed and updated.
Governance

Resource planning

26. A plan is maintained and regularly reviewed to ensure that resources are properly allocated.

Scheme management

27. Roles, responsibilities and duties of all trustees, advisers and service providers are documented, approved and regularly reviewed.

28. Activities undertaken by all scheme advisers and service providers are properly managed and subject to regular performance reviews which are documented and approved.

Internal control framework

29. A risk management framework is established to identify, manage and monitor significant operational, financial, regulatory and compliance risks.

Core scheme transactions

30. Contributions benefit payments, investment transactions and calculations and related income and expenditure are completely and accurately processed in a timely manner and recorded in the proper period.

31. Contributions are invested in accordance with member instructions or the default policy.

32. Transaction errors are rectified and members are treated fairly as a result of that rectification.

Receipt of contributions

33. Late and inaccurate contributions are pursued and resolved.

Retirement process

34. Retirements are managed in accordance with a documented process which is regularly reviewed and approved.

35. Retirement products selected by members are monitored and the range of retirement products made available is reviewed regularly for ongoing suitability.

36. Members are regularly made aware of their investment choices, the importance of reviewing the suitability of their investment choices and that their level of contributions is a key factor in determining the overall size of their pension fund.

Communications

37. Scheme communications are accurate, clear and understandable and are produced in accordance with a documented communications plan. The plan is regularly reviewed and monitored.

38. Communications contain information to support the decisions members need to make at retirement.
We believe that the work involved in drafting this statement serves the interest of our members by giving them independent assurance, by the Reporting Accountant, about our control procedures.

We have decided not to publish the full details of our key controls and procedures, which make up this section in the full report, based on advice about the increase in risk of financial crime or data breach that full disclosure would cause. Making a judgement about the balance between this increase in risk and our core value of transparency, we conclude that publication would not be in members’ interests.

The control descriptions have been drafted to be objective and factual, so that they are a true representation of the control. In accordance with best practice they contain the level of detail required to enable them to be properly verified and tested, and so reveal:

- what the control is for;
- who operates the control;
- how the control is operated;
- the frequency of the control; and
- how the control is evidenced.

These controls are then given context by detailed process descriptions which show how the control fits into the overall operation of NEST Corporation.

The full version of this report details in 107 pages 229 key controls over 144 control procedures, spread across the 38 control objectives set out within the Master Trust assurance framework.

The result of the review of these controls is set out in the Reporting Accountant’s report, forming section 6 of this document.

The full report will be made available to the Pensions Regulator. Our Members’ and Employers’ panels will be briefed on the control structure and findings of the review.
Reporting accountant’s report

Introduction

Report by the Trustees of the NEST master trust

Controls framework

Summary of control objectives

Description of procedures and controls

Reporting accountant’s report