

What Are the Legal Requirements?

Trustees of occupational pension plans are required to exercise their powers of investment "in a manner calculated to ensure the security, quality, liquidity and profitability of the portfolio as a whole". This requirement applies equally across all types of pension provision – Defined Benefit (DB), Defined Contribution (DC), hybrid arrangements, additional voluntary contribution plans etc.

The concepts of "quality" and "profitability" have been explored in some depth by the Pensions Regulator and have been the subject of legislation through the DC charge capping and governance provisions which have applied since April 2015. Additionally, the Regulator has produced guidance material on how trustees should approach "value for member" assessments.

"Liquidity" of DC assets – or, in simple terms, the ability of members to access their money when they need it – should be a key consideration for trustees in designing fund options for members.

The concept of "security" is more difficult and has received much more attention in DB pension plans where employer covenant assessment, contingent assets and risk reduction methods form part of "business as usual". Assessment of security has not historically received the same attention in DC plans but Regulatory attention, together with the growth of DC pension provision in the UK (including issues around the underlying business models of some DC master trusts), has increased the focus.

What Does the Pensions Regulator Say?

The Pensions Regulator elaborates on asset security requirements in its code of practice on [Governance and administration of occupational trust-based schemes providing money purchase benefits](#).

"The law requires trustees to give due consideration to asset protection and to understand what would happen in the event of a problem. Given the complexity of this area, we expect trustee boards to assess the extent to which, and in what circumstances, any loss of scheme assets might be covered by indemnity insurance or similar arrangement, or a compensation scheme such as the Financial Services Compensation Scheme, and to communicate the overall conclusion about the security of assets to members and employers."

The accompanying guidance adds: *"It is likely that you will need to take advice to establish the levels of cover, and you may also need to take professional advice on the overall extent of coverage the scheme has, and the level of risk that the scheme potentially remains exposed to."*

For some trustees this could be one of the most difficult regulatory expectations to comply with, depending on the complexity of the pension plan's investment structure. Communicating the outcome to members may also present a challenge in some cases.

What Are the Misconceptions?

As highlighted in the report "[How safe are your DC assets?](#)" by the Security of Assets Working Party, there are a number of misconceptions surrounding DC assets:

- There is a popular misconception that all DC assets are protected by the Financial Services Compensation Scheme, whereas the level of protection for members varies.
- DC funds are commonly provided via "platforms", but not all trustees realise that they have no direct relationship with the fund manager, which can reduce the protections available.
- There may be a risk of 'cross-contamination' where DC assets are invested through life policies.
- Trustees do not own the assets held on platforms, merely a promise from the platform provider or fund manager.
- When moving platforms, the new contract may contain fewer protections than the existing contract. Trustees should read not only the application form, but all underlying terms and conditions which may be legally binding even if the trustees have not been provided with a copy.

What Action Should Trustees Take?

Where trustees have not established the position on asset security for their pension plan they are advised to add this issue to a forthcoming meeting agenda.

Trustees should consider which advisers need to be involved and work with these to put in place a project plan, broken down into funds and with a timetable for reporting findings to the trustees. For more complex funds, trustees may want to establish a sub-committee to oversee the project.

The project plan should include consideration of trustee training requirements. The complexity of asset security should not be underestimated and trustees need to be in a position to understand the output of adviser investigations and to assess whether action needs to be taken to reduce the level of risk exposure.

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