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# Pensions Lessons for Trustees 2022 – A Whole New Curriculum

September 2022

Our annual back-to-school publication is designed to assist pension scheme trustees with their business planning. It contains a reminder of recent developments, what action trustees should consider taking and what to look out for next.

## Welcome

Welcome to class registration. Here is your timetable for the week. We invite you to click on each topic to see what the lesson has in store.

| Monday | Tuesday | Wednesday | Thursday | Friday |
|---|---|---|---|---|
| **Music**<br>The Single Code of Practice – How to Orchestrate Compliance | **Map Reading**<br>ESG and Stewardship – A Long and Winding Road | **Assembly**<br>Data Protection – A Few Changes to Announce | **Maths**<br>De-risking – Many Angles to Consider | **Sports Day**<br>A Decathlon of Pensions Issues |
| | | **Lunch** | | |
| **Drama**<br>Dashboards – It Is All in the Staging | **Domestic Science**<br>TPR Powers – The Main Ingredients | **History**<br>GMP Equalisation and Conversion – Would the Ancient Greeks Have Solved It Differently? | **Art**<br>Value for Members – A Fresh Perspective | |
| | | | **Parents' Evening**<br>Transfers and Scams – Room for Improvement (Grade C) | |

# Music

The Pensions Regulator's (TPR) existing codes of practice and guidance can be difficult to navigate. The combination of this material into a single code should help to harmonise the requirements. However, the inclusion of new governance material and additional regulatory expectations turns compliance into a major (rather than a minor) piece of work for many schemes.

## The Single Code of Practice – How to Orchestrate Compliance

### What Is the Issue?

TPR's Single Code of Practice (Code) is expected to come into force this autumn. The Code consolidates and updates 10 of the existing 16 codes of practice and adds new governance requirements, stemming from legislation that came into force in January 2019. The regulations mandated the establishment and operation of an "effective system of governance including internal controls" and the Code details the processes, procedures and documents that pension schemes should have in place to comply with this requirement. All schemes will need to take action to comply with the requirements of the Code.

### Which Occupational Schemes Are Affected?

The Code will apply to all schemes in the public and private sectors, but not all obligations apply to all types of scheme.

### What Should Trustees Do Now?

We expect that all trustees will, by now, have made an assessment of the action that needs to be taken, based on the draft Code. Some trustees have made good progress in terms of reviewing and updating scheme policies, practices and procedures: other trustees are ready to take action as soon as the final version of the Code is published. If your scheme has not yet made significant progress, we suggest that you start by identifying areas of high risk and some "quick wins" to keep the momentum going.

### What Is Next?

Look out for the final Code (which we expect in the near future). Much of the draft Code is based on legislative requirements and established regulatory principles, and is, therefore, unlikely to change. However, there may be some refinements around regulatory expectations connected with the 2019 governance legislation. Keep an eye out for anything that impacts your scheme's action plan.

### Comment

It is important to maintain a sense of proportion. Each scheme is different: your legal adviser can help you to assess what is a reasonable and proportionate approach, which may save time and effort. Although many schemes already have a robust governance and risk management framework, the new obligation to carry out regular "own risk assessments" fine-tunes the requirements and places these issues on a more formal footing.

### Resources

- See our resources on the Code to help with your compliance plans.
- See TPR's webpage containing the draft Code and interim response to consultation.

# Drama

The script for pensions dashboards is almost finished. The pensions industry is now required to play its part in making this a perfect production fit for public viewing. Without making a song and dance about it, let's get this show on the road!

## Pensions Dashboards – It Is All in the Staging

### What Is the Issue?

Pensions dashboards are online portals that allow people to see their occupational, personal and state pension information side by side. The aim is to engage the general public, and to provide better and easier access to pensions information, so that people make better informed decisions about their pensions savings. Among other things, dashboards will provide accrued and estimated pensions figures for each scheme (based on set criteria) and contact information so that individuals can find out more detailed information about their entitlement. Pension schemes will be legally required to connect with dashboards on their scheduled staging date and to comply with regulatory requirements and standards issued by the Money and Pensions Service (MaPS). Staging dates are linked to scheme type and size – the connection window for the first cohort of schemes (large master trusts) will close on 31 August 2023.

### Which Occupational Schemes Are Affected?

Pension schemes that are registerable with HMRC will be required to comply with dashboards requirements. There will be exceptions for schemes in a Pension Protection Fund (PPF) assessment period. The draft legislation currently covers schemes with 100 or more relevant members (i.e. deferred and active members), but further legislation will cover small schemes in due course.

### What Should Trustees Do Now?

Trustees should be aware of their staging date and have an action plan in place to ensure that they will be able to connect with dashboards at the required time. Consider TPR's initial guidance for trustees, which includes a checklist with suggested timeframes. Note that TPR expects dashboards to be a point of discussion at trustee meetings. Speak to administrators or software providers about connection options and assess whether your scheme will have any problems in returning the required value data to dashboards.

### What Is Next?

Action! We can expect things to move quickly. The Department for Work and Pensions (DWP) plans to lay the dashboards legislation before Parliament this autumn, and we expect MaPS to issue its dashboards standards and TPR to consult on its compliance and enforcement policy shortly after. We do not yet know when dashboards will be made available to the general public – the Secretary of State for Work and Pensions will determine when dashboards are camera-ready and a period of notice will be given to the pensions industry, to allow trustees and administrators some time to prepare for the anticipated increase in member enquiries.

Separately, trustees of schemes with defined contribution (DC) benefits will be interested in the outcome of the Financial Reporting Council's consultation on changes to actuarial standards on statutory money purchase illustrations. The new standards are expected to come into force from 1 October 2023, and will establish more consistency in how schemes present DC information on dashboards.

### Comment

Trustees will be responsible for dashboards failures and TPR can impose fines for every single failure – it is, therefore, important that trustees seek legal advice before entering into new contracts or agreeing to revised contractual terms.

### Resources

- See our resources on pensions dashboards for more information.
- The Pensions Dashboards Programme's website contains up-to-date information, including useful webinars for background information.

# Map Reading

There is a lot to coordinate when it comes to environmental, social and governance (ESG) and stewardship. Trustees need to consult their map regularly to check the mountains of regulations and to confirm that their aims are plotted carefully, with any obstacles identified.

## ESG and Stewardship – A Long and Winding Road

### What Is the Issue?

ESG and stewardship are playing a greater role in the way in which pension trustees invest and manage scheme assets. At one time, trustees might have taken the opportunity to consider ESG factors when choosing their investment strategy, but they had some latitude. Now, there is a legal requirement on all trustees whose schemes are required to have a statement of investment principles (SIP) to have a policy on financially material considerations. Such considerations include ESG factors and climate change. Even trustees of those schemes that are not required to produce a SIP (for example, public sector schemes and those with fewer than 100 members) should have an appropriate investment strategy, and this would include consideration of ESG factors.

Trustees of the largest trust schemes (with £5 billion or more of assets), authorised master trusts and authorised collective DC schemes are also required to undertake mandatory governance and reporting in relation to the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD). Those trustees must also produce and disclose a TCFD report within seven months of their scheme year-end.

Trustees also need to consider each aspect of ESG. While there is a lot of data available in relation to governance and environmental factors (climate change in particular), the government identified through its March 2021 call for evidence on social factors that it is difficult for trustees to obtain data in relation to the S in ESG, when setting their policies. There is a steep gradient for the industry to climb, in this respect.

Alongside all of this, there has been an increased focus on effective stewardship by pension trustees, not least because trustees must include in their SIP a statement on their policy in relation to the exercise of voting rights, and engagement, in relation to scheme investments. One of the main reported approaches to managing social factors by respondents to the government's March 2021 call for evidence was active ownership – i.e. effective stewardship.

### Which Occupational Schemes Are Affected?

ESG and stewardship are relevant to all pension schemes, whether set up under trust or statute and regardless of size of membership or whether the scheme is closed or open.

### What Should Trustees Do Now?

Trustees should take care to consider all aspects of E, S and G when setting their investment strategy. A good starting point for smaller schemes is to put in place a responsible investment strategy. Our handy guide provides some tips.

Trustees may wish to check key contracts. Do your contracts with investment managers align with your investment beliefs? What happens if something goes wrong and investments are not in line with trustee policy – who is responsible for the fallout? Do your trust deed and rules contain any restrictions that might prevent you from investing in your chosen manner? Do you have a breach response plan in the event that you are accused of breaching your own ESG policy or of investing inappropriately?

Trustees may also wish to consider whether to become a signatory to the UK Stewardship Code 2020. This is encouraged by TPR.

## What Is Next?

From 1 October 2022, trustees of trust schemes with assets of £1 billion or more as at 1 March 2021 will also become subject to the TCFD governance and reporting requirements.

As part of their compliance with the TCFD requirements, trustees will also be required, from 1 October 2022, to select and calculate a portfolio alignment metric for the assets of their scheme. A portfolio alignment metric is defined as being a metric that gives the alignment of the scheme's assets with the goal of limiting the increase in the global average temperature to 1.5 degrees Celsius above preindustrial levels. The DWP has updated its statutory guidance in relation to climate change risks and opportunities to reflect this.

In relation to ensuring that each element of E, S and G is given due consideration, the DWP has said that it will establish a minister-led task force to identify reliable data and metrics in relation to social factors and to ensure that focus on social factors continues to grow throughout the investment chain.

The DWP has published stewardship guidance relating to SIPs and implementation statements. That part of the guidance relating to SIPs is in force now. The part of the guidance relating to implementation statements is statutory guidance, meaning trustees should have regard to it. It comes into force on 1 October 2022.

## Comment

ESG and the factors that need to be considered are constantly evolving. The DWP noted in the outcome of its March 2021 call for evidence that since the Russia/Ukraine conflict, there has been a greater interest from large funds in investing in the defence and nuclear sectors, whereas previously trustees might have divested from those industries as part of their ESG policy. Trustees need to continually monitor, review and update their policies and key documents.

## Resources

TPR has published guidance on climate change. See also our resources on ESG for more information.

# Domestic Science

Trustees should now don their aprons as we look at what TPR is cooking up. The Pension Schemes Act 2021 introduced a new recipe of powers for TPR, allowing it to turn up the heat on trustees and others. We remind you of what is in force, what we are waiting for and what actions trustees should take.

## TPR Powers – The Main Ingredients

### What Is the Issue?

TPR has the powers to dish out financial penalties of up to £1 million in the following circumstances:

- Failure to comply with a contribution notice
- Where there has been "avoidance of an employer debt" and/or "conduct risking accrued scheme benefits"
- The provision of false or misleading information to TPR and/or pension trustees
- Failure to comply with the notifiable events regime

The key points to note about the two new offences of "avoidance of an employer debt" and "conduct risking accrued scheme benefits" are that:

- Anybody who is involved with the running of a defined benefit (DB) pension scheme or a scheme employer can be caught by these offences. There is no requirement to be "connected" or "associated" with a scheme employer in the same way as there is for contribution notices.
- In relation to the offence of "conduct risking accrued scheme benefits", it is not necessary for there to have been any intention to risk accrued scheme benefits – the person just had to know, or ought to have known, that the action they took would have had the prohibited result.

Not only do the two new offences of "avoidance of an employer debt" and "conduct risking accrued scheme benefits" both carry the risk of a financial penalty of up to £1 million, but they also carry the possibility of a criminal penalty of an unlimited fine and/or imprisonment of up to seven years.

There has been concern within the pensions industry around how and when TPR would use its new penalty powers and which power it would use when more than one option is available to it. We are waiting to see how this pans out.

### Which Occupational Schemes Are Affected?

Schemes providing defined benefits, which operate in the private sector, are affected by all of these issues. In addition, trustees of occupational DC schemes and public sector schemes need to be alive to the penalty relating to the provision of false or misleading information to TPR.

### What Should Trustees Do Now?

- Trustees should make sure they understand TPR's new powers and undertake training as appropriate.
- Trustees should familiarise themselves with TPR's new policies (links below), but bear in mind that these are simply policies. They do not bind TPR to act in a particular way and TPR retains discretion to consider each case on its own merits.
- Implement a process so that any notifiable events submission is made in a timely manner.
- Put in place arrangements so that anyone who is responsible for providing information to TPR is aware of the importance of ensuring that the information is accurate and not misleading.
- Trustees may want to check their indemnity policies to see whether they are covered for any of the new financial penalties and, if they are not, discuss appropriate indemnity arrangements with the scheme's employer. Remember that trustees are personally liable for a financial penalty and cannot pay this out of scheme assets.
- Finally, consider putting in place an information sharing agreement between trustees and the employer (or updating an existing one) to facilitate greater compliance with the new requirements.

## What Is Next?

Still in draft are TPR's enforcement policy and amendments to its prosecutions policy, so watch out for finalised versions of these.

In September 2021, the government consulted on draft regulations that would make changes to the existing notifiable events regime. Those regulations were expected to be in force from April 2022, but the final form of the regulations is still awaited. Once in force, the regulations will provide a better form of early warning system for TPR than currently exists in relation to corporate activity that might have a detrimental impact on a DB pension scheme. There will be an obligation on the employer or connected party to notify TPR and the pension trustees of certain types of corporate activity before a transaction completes and to provide a statement setting out details of the proposal along with any mitigation offered to the pension scheme. The exact timing of the notifiable event submission and the accompanying statement is likely to require the input of legal advice.

## Comment

The act allows for further regulations to be implemented that would increase the maximum financial penalty from the current figure of £1 million, so it remains to be seen whether the maximum penalty remains at £1 million.

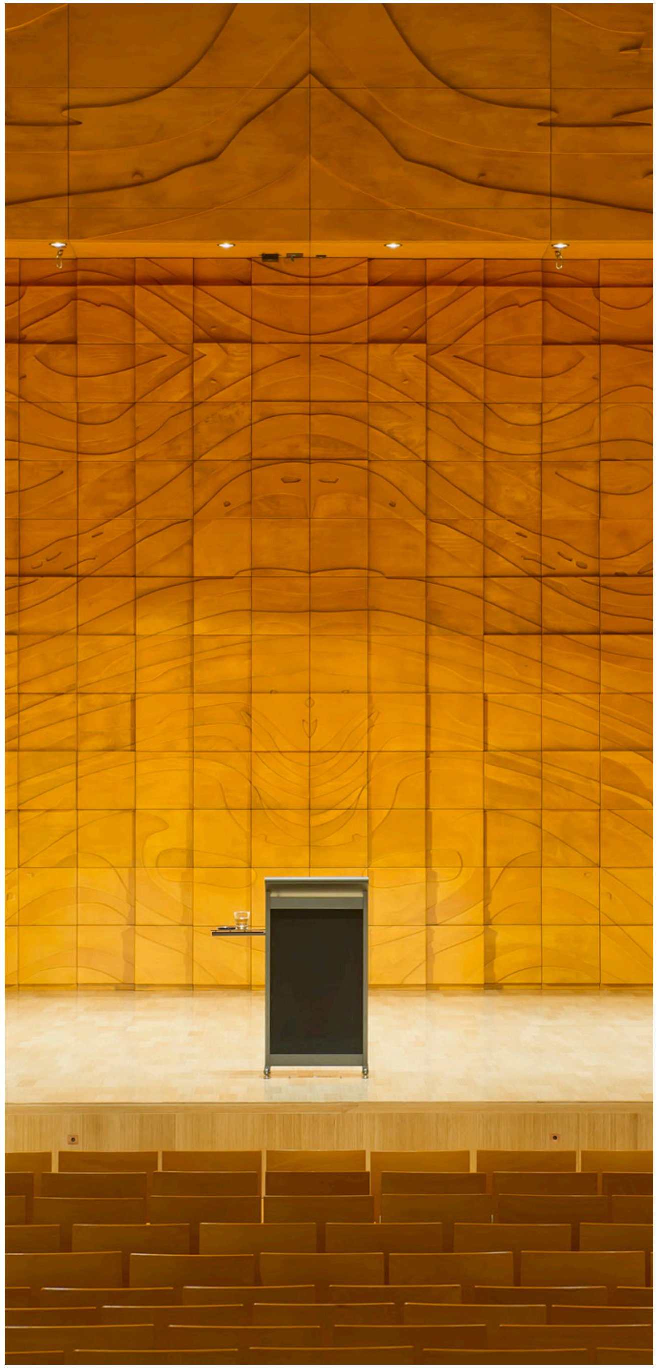
It is also worth noting that where circumstances exist that would allow TPR to impose a financial penalty on a company, TPR could instead impose the penalty on a director, secretary or other officer involved in the decision-making process. This new provision is another way in which TPR will be able to pierce the corporate veil and it could apply equally to trustee directors of a corporate trustee, as well as directors of the scheme employer.

## Resources

See our resources on the Pension Schemes Act 2021 for further information.

See also:

- TPR's criminal offences policy, which provides guidance on TPR's approach to investigating and prosecuting the new criminal offences of "avoidance of an employer debt" and "conduct risking accrued scheme benefits".
- TPR's high fines policy in relation to TPR's avoidance powers. This sets out TPR's approach in relation to the financial penalties of up to £1 million that could be imposed for "avoidance of an employer debt" and "conduct risking accrued scheme benefits" (rather than the fines that could be imposed when avoidance is treated as a criminal offence). The policy also covers TPR's approach to financial penalties on a failure to comply with a contribution notice.
- TPR's high fines policy in relation to TPR's information powers. This sets out TPR's approach in relation to its power to levy a financial penalty of up to £1 million for failure to comply with the notifiable events regime, and/or knowingly or recklessly providing false or misleading information to TPR or pension trustees.
- TPR's overlapping powers policy, which sets out the approach that TPR will take when more than one penalty option is available to it.
- TPR's information gathering powers policy describing TPR's approach to how it will investigate an issue and gather information.



# Assembly

It is time to gather everyone together. A special trustee assembly has been called to announce some incoming data protection legislation. Please take your seats and we will outline the key issues and some new terminology.

## Data Protection – A Few Changes to Announce

### What Is the Issue?

The Data Protection and Digital Information Bill (Bill) was introduced into Parliament on 18 July 2022. The Bill will amend current UK data protection legislation, including the UK GDPR and the Data Protection Act 2018.

The introduction of the Bill follows a wide-ranging consultation, "Data – a New direction", that the government ran in 2021. The aims of the Bill include providing organisations with greater flexibility on how to comply with some aspects of data protection legislation, improving the clarity of the framework and reforming the Information Commissioner's Office (ICO). Among other things, changes are also proposed to the legislation governing cross-border flows of personal data and "data mapping" obligations.

The explanatory notes accompanying the Bill explain that the government's view is that the current legislative requirements can lead to a "box-ticking" compliance regime, rather than one that encourages a proactive and systematic approach.

As a general rule, the Bill is intended to introduce more flexibility and reduce burdens on organisations (while maintaining high data protection standards), rather than add to them. We hope that this plays out in practice, given the efforts that have gone into ensuring that pension schemes comply with data protection legislation, particularly since the introduction of the GDPR.

### Which Occupational Pension Schemes Are Affected?

All occupational pension schemes.

### What Should Trustees Do Now?

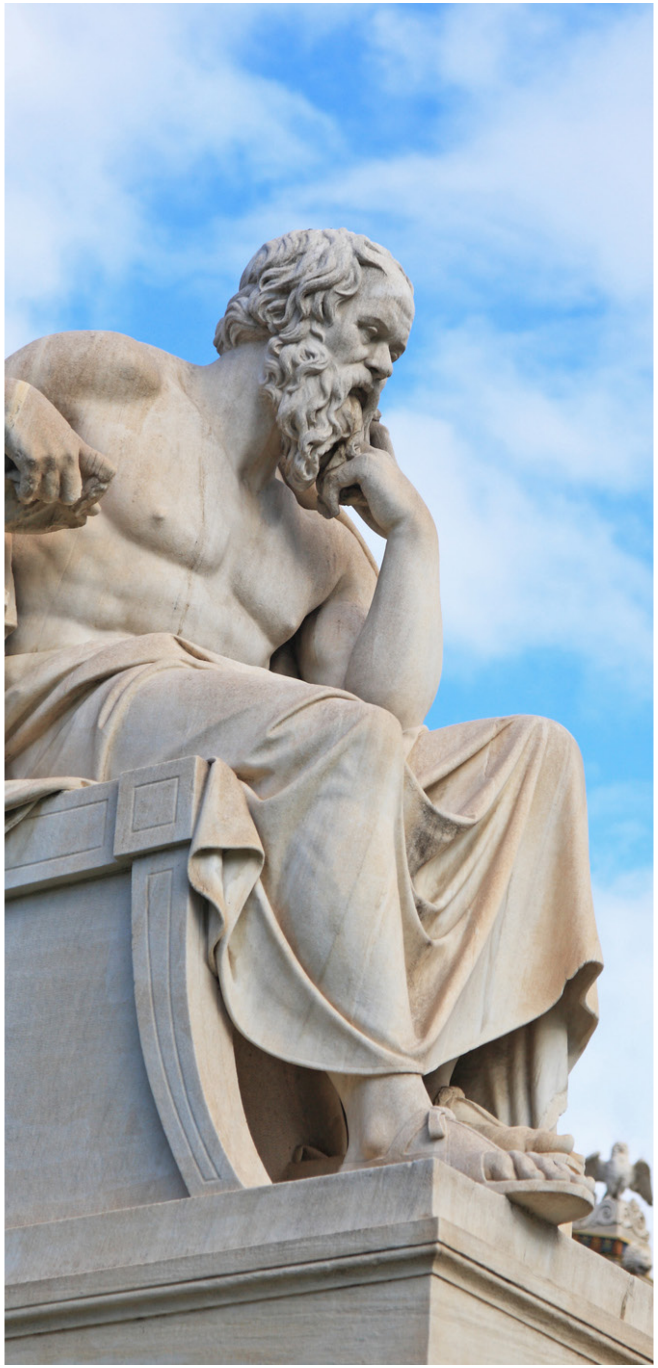
Data protection legislation and regulation is a fast-moving area and this is one reason why relevant policies and documentation need to be regularly reviewed and updated. At the time of writing, the Bill has a way to go before its provisions are finalised and can come into force, and some elements are likely to change as it makes its way through the parliamentary process. However, in time, we anticipate that amendments will need to be made to pension schemes' existing data protection policies and documentation, including privacy notices and policies concerning responses to subject access requests. For example: the Bill proposes that the Information Commissioner will be replaced with a new body corporate called "the Information Commission"; Data Protection Impact Assessments will be replaced with "assessments of high risk processing"; and data protection officers will be replaced with "senior responsible individuals". Updates will be necessary to refer to the new terminology and requirements.

### Comment

The government will have to tread carefully with its reforms to the data protection regime, particularly the proposed changes to the rules concerning international data transfers, to avoid jeopardising the existing agreements with the EU, which currently allow the free flow of personal data between the UK and the EU.

### Resources

The passage of the Bill can be tracked on the UK Parliament website.



# History

Guaranteed minimum pensions (GMPs) ceased to accrue in 1997. At that time, the pensions industry would not reasonably have expected to be dealing with so many complications 25 years later. When will we be able to confine GMPs to the pensions history books?

## GMP Equalisation and Conversion – Would the Ancient Greeks Have Solved It Differently?

### What Is the Issue?

Many schemes have made a good start with equalising benefits for the effect of GMPs (referred to as GMP equalisation) for current and upcoming benefit payments and transfer requests. Having tackled the future, these schemes are now looking to the past, and assessing the extent to which they are required to equalise previous transfer payments. A former member may have left the scheme some time ago and transferred their benefits to another pension arrangement, but their cash equivalent transfer value was underpaid, as it did not take account of GMP equalisation adjustments. The so-called *Lloyds 3* court judgment ruled that there was an obligation to top up the transfer to the correct amount if the transfer was paid using the statutory transfer power in the cash equivalent legislation (a "statutory transfer").

Trying to unravel the past actions of a pension scheme is not always easy. For example, judgment calls are required where the calculation or payment of top ups to statutory transfers is hampered by missing data, the former member has died, or there is no receiving scheme able and willing to accept the top up. One issue that our clients have raised is the extent to which the top up can (or should) be paid as a lump sum, i.e. direct to the former member. This is a complex area and advice should be sought if pension scheme trustees are considering making lump sum payments instead of topping up the original transfer payment to the receiving scheme.

The tax treatment of top ups to transfer payments, or lump sums in lieu of a top up, can also cause headaches. HMRC provided some (limited) assistance in its April 2022 newsletter. As regards lump sums, it explains how a lump sum can be paid as an authorised payment if it meets the conditions to be a winding up lump sum payment, or is not more than £10,000 and meets the criteria set out in The Registered Pension Schemes (Authorised Payments) Regulations 2009 for a "relevant accretion" or small lump sum payment.

### Which Occupational Pension Schemes Are Affected?

Pension schemes that have paid transfers in respect of former members, where the members accrued benefits between 17 May 1990 and 5 April 1997, which include rights to GMPs (and those transfers did not take account of GMP equalisation adjustments).

### What Should Trustees Do Now?

Speak to administrators and scope out the data available regarding past individual transfers out and examine the history of bulk transfer activity. Agree strategies (with legal advice where appropriate) for addressing shortfalls in past transfer value payments and tackling the practical issues with calculating and paying amounts due. Another top tip is to review the wording in discharge forms (forms that individuals may be asked to sign where a transfer or a top up is paid), to ensure that they are worded in a way that offers the best protection against future claims.

## What Is Next?

There has recently been some ironing out of certain GMP conversion issues – one of the methods that can be used to achieve GMP equalisation. The Pension Schemes (Conversion of Guaranteed Minimum Pensions) Act 2022 has received Royal Assent and HMRC has issued guidance on some of the tax consequences of GMP conversion. However, at the time of writing, we are still waiting for the regulations that will bring the main provisions of the act into force. HMRC has also acknowledged that it needs to carry out further work on the tax implications of GMP conversion for members who have not yet retired.

## Comment

How would the ancient Greeks have dealt with GMPs? Would Pythagoras have devised a theorem? Would Archimedes have found a solution, worthy of shouting "Eureka"? Maybe Aesop would have written a fable about it? The moral of the story is that trustees need to keep plugging away at scheme-specific solutions against a backdrop that is not ideal.

## Resources

Our publication "Some Transfers Are More Equal Than Others" considers statutory transfers and the court's conclusions regarding non-statutory transfers and bulk transfers.

# Maths

Maths is not everybody's favourite subject, but this may be a good time to factor in some calculations to reassess the scheme's de-risking options. (The Scheme Actuary is well qualified to deal with any difficult sums that may arise.)

## De-risking – Many Angles to Consider

### What Is the Issue?

The de-risking market is growing and evolving, which may open options that have not previously been available or affordable for DB schemes. We have seen a huge growth in the buy-in/buyout market over the last couple of years, with growth driven by improved scheme funding levels and competitive insurer pricing. Longevity transactions are also a growth area with insurer appetite extending beyond pensioners. Enhanced Transfer Value exercises and Pension Increase Exchanges continue to be an option for some schemes.

### Which Occupational Schemes Are Affected?

Our focus is on options for DB schemes.

### What Should Trustees Do Now?

Discuss de-risking options with your advisers, if you have not done so recently. Assess whether new options are available or whether any existing de-risking plans could be accelerated.

Consider what preparatory work can be undertaken to put your scheme in the best position to negotiate with insurers when pricing and conditions are favourable. This may include data cleansing exercises, or the preparation of benefit specifications.

### What Is Next?

Trustees should remain alert to developments and keep an open dialogue with advisers.

### Comment

The pace of change is fast. Commercial DB consolidators are still in their infancy, but may offer solutions for schemes where an "end-game" plan is in place but buyout is not affordable. Seek legal advice at an early stage when considering a de-risking option.

### Resources

Pensions partner Victoria Jeacock discusses more de-risking options in her short video.

# Art

It is said that a picture paints a thousand words. On this basis, it is a shame that we cannot present you with an image that encapsulates all the recent changes and proposals affecting DC schemes – this really would be a masterpiece.

## There Is a Lot on the DC Palette

A lot has been happening in the world of DC this year. We had the "stronger nudge" to pensions guidance requirements, which came into force on 1 June 2022 and which (perhaps controversially) captures very small pots and additional voluntary contributions. We have also witnessed a number of consultations involving changes to the charge cap (affecting schemes used for auto-enrolment) as the government continues its drive to remove barriers to investing in illiquid assets.

In terms of disclosure, since 1 October 2021, it has been a requirement for trustees to calculate and disclose the return on investments for their default and self-select funds, net of transaction costs and charges. The DWP has also drawn up proposals to introduce additional disclosures in the chair's statement and in the SIP.

From 1 October 2022, trustees of DC schemes used for auto-enrolment are required to produce simplified annual benefit statements covering no more than two sides of A4. See the statutory guidance and illustrative template.

## Value for Members – A Fresh Perspective

The new value for member assessment is an additional area of work that trustees may be addressing at present (depending on their scheme year-end date).

### Which Occupational Schemes Are Affected?

DC schemes with less than £100 million total assets, which have operated for at least three years, unless TPR has been notified that the scheme is in the process of winding up. (Note that for hybrid schemes, total assets include the DB element.)

### What Should Trustees Do Now?

Trustees of affected schemes are required to conduct a rigorous value for member assessment for scheme years ending after 1 December 2021 to demonstrate that they offer value comparable with larger schemes. Schemes that cannot provide value for members should look at winding up the scheme, unless they can make immediate improvements.

The outcome of the detailed value for member assessment should be explained in the chair's statement and published on a publicly accessible website. It also has to be reported to TPR in the scheme return.

### What Is Next?

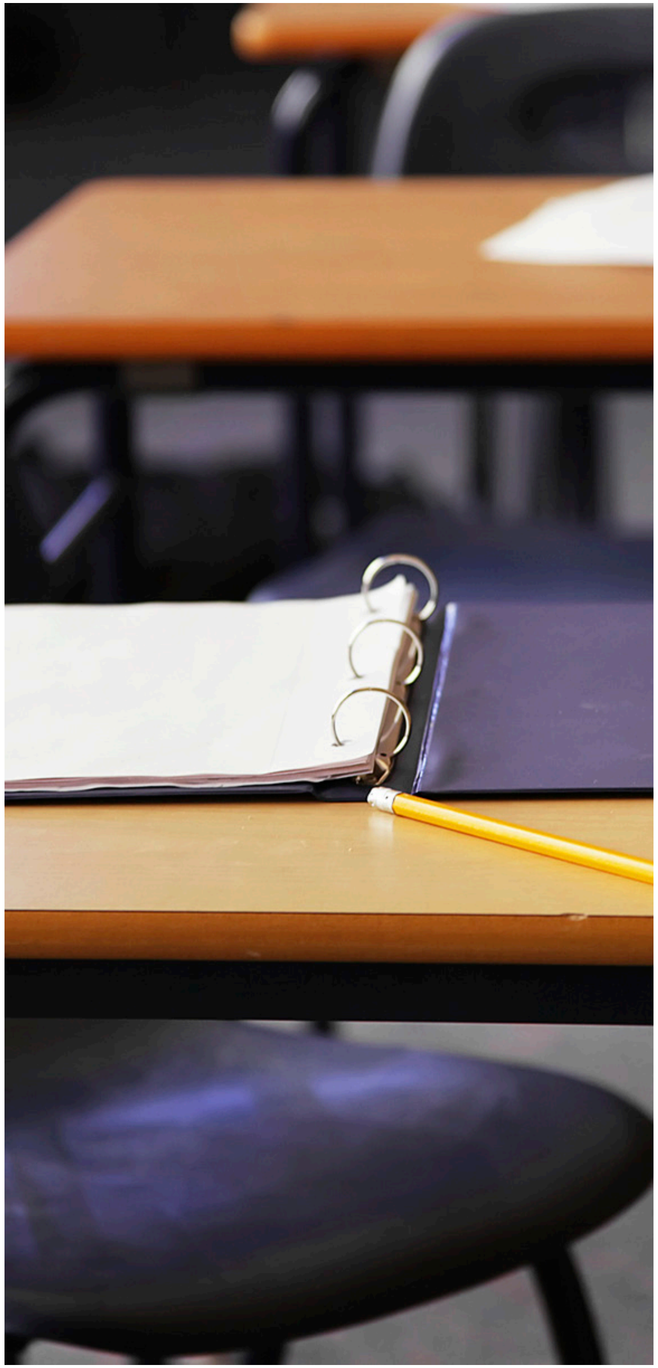
TPR has confirmed that compliance with value for member assessments will be the subject of a regulatory initiative in the coming year. Trustees should be prepared to answer questions about how they have conducted their assessments and to justify the conclusions they have reached.

### Comment

Trustees should seek advice if they need help with any part of their assessment. TPR is unlikely to brush over compliance failures – we can expect regulatory action.

### Resources

The DWP's statutory guidance covers value for member assessments and the reporting of new investment returns, and TPR's guide covers regulatory expectations.



# Parents’ Evening

Parents’ evening offers a time for review and appraisal: an assessment of what is working well and where improvements can be made. It is not always a comfortable process. Transfer problems and pension scams have been causing a great deal of discomfort within the pensions industry for some time and the latest changes to legislation are creating new challenges. Government and industry both want to achieve the same thing: to put an end to pension scams and to ensure that members are making informed decisions, but it is proving difficult to make the grade. In spite of all the efforts from different parties, we are left with a sense of “could do better” for members.

## Transfers and Scams – Room for Improvement (Grade C)

### What Is the Issue?

The rules concerning the payment of transfers changed at the end of November 2021, when the Occupational and Personal Pension Schemes (Conditions for Transfers) Regulations 2021 came into force. These regulations brought in a new system of checks and balances, involving the raising of red or amber flags if certain circumstances indicate a risk of pension scam activity. In summary, if a red flag is raised, the statutory transfer cannot proceed; if an amber flag is raised, the statutory transfer can only proceed if the member has obtained guidance from MoneyHelper.

The pensions industry is still grappling with practical issues concerning the application of these new rules. For example, concerns that the payment of even a small incentive by the receiving scheme to encourage an individual to transfer their benefits should raise a red flag, or that the presence of overseas investments in the receiving scheme raises an amber flag. The DWP and TPR issued a joint statement in response to these concerns and TPR has updated its guidance on dealing with transfer requests.

### Which Occupational Pension Schemes Are Affected?

All schemes paying transfers.

### What Should Trustees Do Now?

Speak with administrators to confirm the steps that are being taken to comply with the new transfer rules. Legal advice may be necessary regarding the payment of transfers to pension arrangements offering incentives or with overseas investments. Assess options for paying non-statutory transfers under the scheme rules as an alternative to a statutory transfer (TPR has amended its guidance to indicate this may be appropriate, even where there is a red or amber flag, provided that due diligence has been carried out and the risk of a pension scam is low).

Confirm the administrators’ approach to compiling “clean lists” of receiving pension arrangements where due diligence analysis shows no risk of pension scam activity. Transfers to a scheme on a clean list can proceed without carrying out certain additional checks. Confirm that those lists are regularly reviewed to ensure that they remain up to date and that the schemes continue to present a low risk.

### What Is Next?

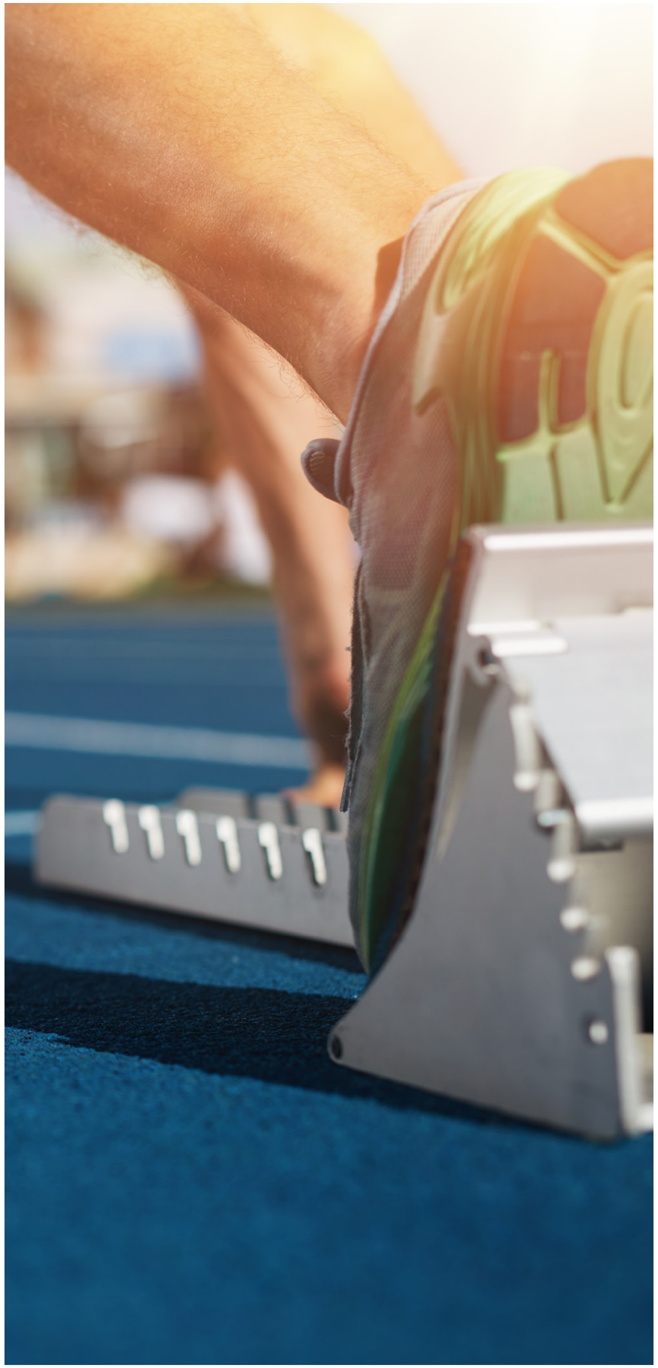
The DWP confirmed that it is conducting a review of the regulations and is required to publish a report within 18 months of them going live. In light of the controversy concerning these regulations, we anticipate future changes following that review.

## Comment

Given the uncertainty about how these regulations should be applied in practice, it is disappointing that the DWP has given no indication that its review of the regulations will be brought forward. While the joint statement from the DWP and TPR, together with the revisions to TPR guidance, provide some reassurance, ultimately these do not rewrite the underlying legislation. We do not yet know how The Pensions Ombudsman or courts would interpret the regulations if, for example, a member takes a statutory transfer to another pension arrangement, subsequently regrets the decision to transfer and goes on to claim that the trustees had no power to pay it due to the presence of a red flag.

## Resources

See our publication "New Rules on Pension Transfers – Urgent Action Required".



# Sports Day

It is sports day! To complete this week's pensions timetable, trustees should sprint through our pensions decathlon. We highlight 10 industry developments – some of which require action. Ready? Go!

## 1. Cost of Living – A Very High Jump

Some members are opting out of pension schemes due to increases in the cost of living. Trustees may wish to keep an eye on opt-out figures for their schemes and ensure that communications are clear on when a member is able to rejoin the scheme or whether there are any options for reducing contributions.

High inflation may also result in questions from pensioners about how pension increases are calculated and whether discretionary increases can be granted. Trustees should be clear on their powers in the scheme documents and take legal advice if considering any discretionary payments.

## 2. DB Funding – Back Out of the Starting Blocks

The DWP is consulting on draft funding and investment regulations, which supplement the Pension Schemes Act 2021 requirements for trustees of DB schemes to put in place a funding and investment strategy and produce a written statement of strategy. When this is in force, DB schemes will be required (as a minimum) to be in a state of low dependency on their sponsoring employer by the time they are significantly mature. Generally, this means that investments would be broadly matched with benefit payments out of the scheme, without the need for employer contributions. The DWP proposes that TPR should determine what is meant by scheme maturity. Under the proposals, trustees would be required to agree their funding and investment strategy with the sponsoring employer and to set this out in a statement of strategy, which would include an assessment of whether the strategy is being met. The statement of strategy would also need to include a covenant assessment and be submitted to TPR within 15 months of the effective date of an actuarial valuation, along with a copy of the valuation (whether or not the scheme is in deficit).

TPR has been waiting for these regulations before launching its second consultation on the draft DB funding code, which is planned for autumn 2022. We understand that TPR expects the new code to be operational from September 2023 and it will apply to schemes with valuation dates after the code becomes effective.

## 3. TPR Pole Vaults Into the CMA Arena

The Competition and Markets Authority (CMA) Order in Relation to the Investment Consultancy and Fiduciary Management Markets sets out a requirement for pension trustees (with limited exceptions) to:

- Set objectives for their investment consultants
- Run a competitive tender exercise where manageable assets of 20% or more are (or become) subject to fiduciary management services
- Submit a compliance statement to the CMA by 7 January each year

The DWP has now published regulations, which come into force on 1 October 2022, incorporating the requirements of the CMA order (with a few tweaks) into pensions legislation. TPR will take over the CMA's role of monitoring and ensuring compliance with the order. Going forward, pension trustees will make their annual compliance statement to TPR via additional questions on the pension scheme return. TPR has published updated guidance for trustees on setting objectives for investment consultants and tendering for fiduciary management services.

## 4. Contracts – We Are Raising a Red Flag

Trustees should seek legal advice before entering into any new or amended contracts – including investment agreements and contracts with service providers. This should be done at an early stage to maximise opportunity for discussion and negotiation, and to allow time for trustees to understand their liabilities, costs, exit terms, etc. Where possible, trustees should ask for an early draft of a contract, even if they have been told that it will contain "standard terms".

## 5. Trust Registration Service – Keeping on Track

HMRC established the Trust Registration Service (TRS) in compliance with the EU's fourth money laundering directive. Originally, the intention had been that all UK express trusts, including registered pension schemes, would be required to register on the service if they incurred a liability to certain specified UK taxes. HMRC subsequently relaxed the requirements in relation to registered pension schemes, although the legislation was not updated to reflect this until recently, when it was amended to take account of the requirements of the fifth money laundering directive. Legislation now requires that all UK express trusts, regardless of whether they incur certain taxes, must be registered on the TRS from 1 September 2022. New trusts must be registered within 90 days of creation. The exemption in relation to registered pension schemes still applies, as does the exemption in relation to death benefit schemes. However, if you are the trustee of an unregistered scheme, such as a directors' executive top up scheme, you should ensure that your scheme is registered on the TRS.

## 6. HMRC Migration – One for Trustees to "Discus"

In other HMRC news, the new Managing Pension Schemes service is now set up so that pension schemes registered on the old Pension Schemes Online service can be migrated over to the new service. This is something that trustees, as HMRC "Administrator", need to do and it is unlikely that scheme administrators would be able to do this on trustees' behalf. Trustees may receive correspondence from their scheme administrator with instructions on how to perform the migration. If they do not receive any information from the scheme administrator, trustees will still need to be proactive and undertake the migration process. You can follow the instructions on HMRC's website. Trustees will need their Scheme Administrator ID and government gateway user ID and password in connection with the scheme and should contact HMRC if they do not have these details. While there is no urgency (at the moment) to migrate each pension scheme onto the new system, it could take some time to get together all of the information that is needed, including personal data such as date of birth, national insurance number and unique tax reference of all of the directors of the current scheme employers. At some point in the future, any schemes that have not been migrated over will be de-registered, so early action is recommended in case any problems are encountered along the way.

## 7. Equality, Diversity and Inclusion – A Marathon, Not a Sprint

We can expect to see material emerging from the diversity industry group established by TPR to help develop best practice on equality, diversity and inclusion on trustee boards. In TPR's latest report and accounts, it is noted that 65 industry volunteers are working on this initiative. Among other things, the industry group will produce tools to aid with trustee recruitment, to encourage a wide range of perspectives, knowledge and skills on trustee boards, which should discourage "group think".

## 8. Small Pot Consolidation – A Long Jump for the Pensions Industry

The small pots industry co-ordination group issued a progress report on its work to date to find a low-cost automated solution for consolidating small deferred DC pension pots. The number of small deferred pots has spiralled as a result of auto-enrolment and cause inefficiencies in the pensions system. This issue is a particular concern for master trusts – according to research by the Pensions Policy Institute, the number of small deferred pots will grow to 27 million by 2035 in master trusts alone. This project has a long way to go – we can expect a lot more research and calls for evidence, and the solution will eventually require changes to legislation.

## 9. CDC Schemes – Over the First Hurdle

On 1 August 2022, the legal and regulatory framework was put in place for applications to be made to TPR to operate a Collective DC (CDC) scheme. Currently, the legislation only allows for single and connected employer schemes to operate as CDC schemes, but the government says that there is enthusiasm for operating different models, including multi-employer schemes and "decumulation only" vehicles. We may see industry consultation on the expansion of CDC before the end of the year. This is an important market development, offering an alternative to traditional DB and DC models.

## 10. PPF Sets a Steady Pace

Following a court decision last year that the PPF compensation cap was unlawful on the grounds of age discrimination, the PPF notes in its 2021-22 report and accounts that it continues to work on removing the cap for all PPF pensioners, but that the work is complex and will take some time. The cap is no longer applied to new PPF retirees, but it does still apply for those receiving compensation from the Financial Assistance Scheme (FAS). However, the PPF states that both PPF and FAS members will be entitled to an increase in their compensation if they are not receiving at least 50% of the value of their accrued benefits, pursuant to the judgment in Hampshire.

The PPF should shortly be issuing its invoices for the 2022-23 levy year. The levy is payable within 28 days of receipt. Those levy payers that are struggling to pay within the 28-day period due to cash flow being impacted by COVID-19 can apply for a waiver of interest that would otherwise be payable for late payment. This is provided payment of the full invoice could be made within 90 days.

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