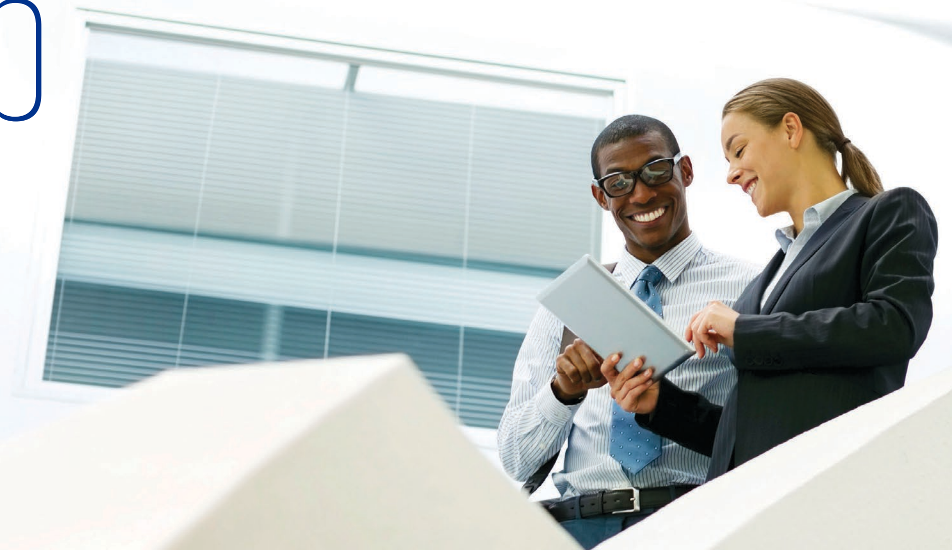
Pensions accounting, assurance and regulatory round-up



Private sector occupational pension schemes

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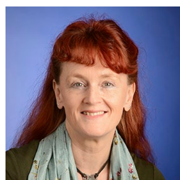
August 2021

Introduction

Welcome to the most recent edition of our Pensions accounting, assurance and regulatory round -up for private sector occupational pension schemes. This update covers a range of topics and considers developments from the Pensions Regulator ("TPR"), the Department for Work and Pensions ("DWP") and the wider pensions industry.

If you have any queries or would like to discuss any of the matters herein further, please do get in touch with your usual contact at KPMG, Anne or Sarah, or email us.



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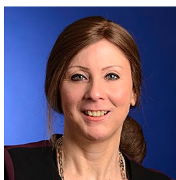

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TPR

TPR: Interim response to the Single Code of Practice

On 24 August 2021 TPR released its response to the consultation on the draft single code of practice. Amongst other new areas, the new code takes account of changes introduced by the Occupational Pension Schemes (Governance) (Amendment) Regulations 2018 (the 'Governance' Regs) aiming to improve standards of governance.

Recap on key points

— The term 'governing body' as a simplification to refer to trustees and managers of occupational schemes, managers of personal pension schemes and managers / boards of public service schemes was introduced.

— The Governance Regs introduced three new requirements:

- An effective system of governance ("ESOG")
- The need for internal controls to support the effective system of governance. Robust and measurable internal controls should be put in place to manage risks
- An Own Risk Assessment ("ORA") for all schemes with over 100 members. The ORA is perhaps the most significant additional requirement, in terms of trustees' time and effort, coming out in the new code and is a separate requirement to having a risk register. TPR expects governing bodies to use this to assess how well their policies and procedures address various risks, financial and operational, that their scheme faces.

— The draft code also made mention of unregulated investments and the Regulator seemed to impose what turned out to be a controversial 20% "limit" for schemes.

TPR's Interim Response

TPR received 103 responses and over 10,000 individual answers to questions.

— Own risk assessment seemed to receive the greatest attention with most respondents appearing to have correctly understood the purpose of the ORA as a review of a scheme's existing risk controls. Concerns were raised about the amount of work it would entail, the timeframe, what the finished product would look like and the burden it would place on smaller schemes. TPR responded by saying it remains of the view that trustees should prepare their first ORA in a timely fashion, i.e. taking the legislative timescales as a maximum but preparing the document in a shorter timescale as a matter of best practice, but added that it will also consider how often governing bodies should review the ORA.

— On unregulated investments, the Regulator received strongly argued comments concerning "the 80% or 20% rule" which some had interpreted as a restriction on illiquid investments. TPR reiterate that its intention had been, and remains, to protect members of poorly run, and typically small, schemes from investments in poor quality or inappropriate assets. In setting out that expectation (20% limit) it "inadvertently created a position that would affect well governed, typically larger, schemes that hold unregulated assets as part of a well-managed investment strategy." As a result, TPR confirms it will not be proceeding with this expectation in the way it is drafted.

A final publication date for the new code has not been confirmed, but TPR states it does not expect to lay the new code in Parliament before Spring 2022. It is, therefore, unlikely to become effective before Summer 2022.

David Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice, said: "I'm confident the feedback received during our new code consultation will help ensure the final version provides a clear, up-to-date and consistent source of information on scheme governance."

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TPR

TPR: Climate-related guidance consultation

On 5 July 2021 TPR published a consultation seeking views on its proposed approach to the new requirements for the governance and reporting of climate-related risks and opportunities, together with the draft monetary penalty policy.

Guidance on governance and reporting of climate-related risks and opportunities

The guidance should be used alongside the statutory guidance issued by the DWP "Governance and reporting of climate-change risk: guidance for trustees of occupational schemes" and sets out TPR's expectations and what evidence it will want to see from scheme trustees. TPR state that it will be looking for clear evidence that trustees:

— are taking proper account of climate change when making decisions about the scheme, and that those advising them are helping to do this;

— have carried out their analysis in a way that is consistent with the Taskforce on Climate-Related Disclosure ("TCFD") recommendations so that savers and others can be confident in it;

— have seriously considered the risks and opportunities that climate change will bring to their scheme, in its particular circumstances; and

— have decided what to do as a result of this analysis and have set a target to help achieve that goal.

Aimed at trustees who are required to comply with the new Climate Change regulations, TPR also state that those that are not required may wish to voluntarily follow the guidance in this consultation.

The consultation sets out example steps TPR expect trustees to take and then report on, together with example scenarios to help trustees navigate their way through the climate change requirements.

Breaches of the Climate Change Governance and Reporting Regulations

The second part of the consultation is a proposed appendix to TPR's Monetary Policy. The Climate Change Governance and Reporting Regulations require TPR to issue a mandatory penalty where the climate change report is not published on a publicly available website, accessible free of charge, within the required timeframe.

The minimum penalty for a breach of the publication requirement is set in legislation and is £2,500. The maximum penalty is £5,000 for individuals or £50,000 in any other case (for example, corporate bodies). TPR sets out its general approach to the mandatory penalty as follows:

— All schemes receive the minimum penalty of £2,500;

— Any consecutive penalty will normally be at least £5,000 to reflect the seriousness with which TPR view repeated or ongoing breaches of the legal requirements;

— Where the scheme has a professional trustee, the minimum penalty will generally be £5,000 as TPR expect higher standards; and

— TPR will also consider, in each case, whether it would be appropriate to issue a penalty higher than the minimum amount, applying the same approach that it adopts when determining the amount of a discretionary penalty. Factors which TPR will take into account include:

  – Nature of the body being fined.

  – Impact of the breach: both the number of members affected, and the significance of any detriment suffered.

  – Whether TPR consider that a higher amount penalty might be more effective in changing the behaviour of the person in breach.

  – The reasons for the failure.

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TPR: Climate-related guidance consultation (cont.)

For example, TPR state that it would be more likely to consider a higher fine in cases where the failure to comply with publication requirements is based upon a failure to comply with the underlying governance requirements.

If there are underlying breaches of the governance requirements, TPR add that it may also consider issuing a discretionary penalty for the underlying breaches, in addition to issuing the mandatory penalty.

In considering whether to impose a discretionary penalty TPR will adopt the approach set out in the Monetary Penalties Policy in respect of other discretionary penalties.

A number of the provisions in the regulations state that trustees must take certain steps 'as far as they are able'. This means that to meet this requirement, trustees must take reasonable and proportionate steps, taking into account costs and time commitments.

The DWP statutory guidance states trustees must carry out the following activities as far as they are able:

- undertake scenario analysis
- obtain scope 1, 2 and 3 greenhouse gas emissions and other data relevant to the trustees chosen metrics
- use that data to calculate those metrics
- use those metrics to identify and assess climate-related risks and opportunities
- measure the performance of the scheme against the target set by the trustees.

The primary purpose of the provision to carry out activities ‘as far as you are able’ is to recognise that all the information needed to carry out these activities may not be available immediately. Trustees will need to explain the steps taken to ensure compliance with legal obligations, any obstacles encountered, and the impact of those obstacles. Any gaps in data must be fully explained.

The amount of any discretionary penalty will be calculated in line with the current Monetary Policy and will depend upon the person(s) concerned, the band level (see overleaf) and any aggravating or mitigating factors.

Likely band levels are set out in the consultation as follows:

Band level (nature and impact/ potential impact of breach)	**Examples**	**Type of person**	**Range (£)** (subject to statutory minimum)
1	Failing to get the climate change report signed by the chair	Individual	0–1,000
		Any other case	0–10,000
2	Failing to disclose scheme resilience in the scenarios analysed	Individual	2,500
		Any other case	0–25,000
3	Multiple breaches of the requirements to have proper governance of the risks and opportunities arising from climate change, with at least one breach in each of the four core areas (Governance, Strategy, Risk management, Metrics & targets).	Individual	5,000
		Any other case	50,000

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TPR: Climate-related guidance consultation (cont.)

Trustees will need to publish their report on a publicly available website, free of charge within seven months of the end of any scheme year where the scheme was subject to the requirements. TPR point out that as well as including the website address in the annual report, trustees should also include a short summary explaining where the link will take the reader. In addition, trustees may include a brief explanation of what the report is, why it is important and a high level summary of the main findings.

Conclusion

David Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice, said: "We want to work with trustees, and their advisers, to ensure climate-related risks and opportunities are considered as key elements of scheme governance and we would welcome feedback on the best way to deliver this."

The consultation closed on 31 August 2021.

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TPR

TPR: Annual Funding Statement 2021

On 26 May TPR published their Annual Funding Statement for 2021, providing guidance for schemes having valuations between 22 Sept 2020 and 21 Sept 2021 (Tranche 16 valuations).

Analysis shows that over the three years to December 2020, funding levels remained broadly unchanged but improvement has been seen in the three years to March 2021, although the position for individual schemes will vary. Trustees will need to assess whether they are ahead or behind their targets and remain focussed on their journey towards longer term targets.

The statement includes guidance and regulatory expectations on the approach to valuations and sets out what TPR expects of trustees and employers and what they, in turn, can expect from TPR. It also includes an update on recent issues. The new DB funding code is not expected to come into force until late 2022. The second consultation on the new code will be published after the regulations flowing from the Pension Schemes Act 2021.

Within the statement, consideration is given to:

1 Actuarial assumptions and scheme demographics

Trustees need to understand the assumptions used in modelling and consider a range of outcomes, the key variables and the sensitivity of the results. Scenario analysis aligned to that of the sponsoring employer is encouraged with trustees having an awareness of the impact of change not only on scheme investments but also on the employer covenant and potentially mortality.

Inflation

Forthcoming changes in the way inflation is measured (alignment to CPIH) from 2030 may mean that assumptions need to be adjusted.

Mortality

COVID -19 may have had an immediate impact on mortality but this is believed to be generally low. There may also be longer term effects from long COVID and the effect of the pandemic on non-COVID healthcare. However, a positive effect on mortality may be seen due to vaccine development and improved lifestyle choices. Scenario analysis may be helpful in understanding the position. Trustees will need to decide whether to retain current mortality assumptions or update them with justifications. TPR state that 'trustees should ensure their mortality assumptions are balanced, evidence-based and derived using a sound methodology'.

Post valuation experience

Trustees may take experience, either positive or negative, between the effective date of the valuation and the date of its signing into account in finalising recovery plans but must use justifiable assumptions and ensure that the recovery plan is appropriate and in the best interests of members. In allowing for post valuation experience, trustees should take a consistent approach at each valuation done. TPR note that their expectation would be for favourable post-valuation events to lead to reduced recovery plan lengths rather than reduced employer contributions.

2 Investment considerations

Liquidity

In a maturing market, trustees need to monitor liquidity. TPR advocate a proportionate approach including stress testing, exposure to margin/collateral calls through derivatives and assessment of assumptions relevant to high stress scenarios regarding liquidity and asset valuation.

Cessation of banking benchmark for cash-like investments

Referencing discount rates, the statement notes the phasing out of LIBOR and EURIBOR rates.

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TPR: Annual Funding Statement 2021 (cont.)

3 Covenant considerations

Regarding covenant the Statement notes that 'short-term covenant visibility may have improved, but trustees must continue to be alert to the risks of weakening employer covenants and remain engaged with employers as uncertainties continue'.

The statement recognises that the impact of the experience of COVID-19 has been varied with the sector of the sponsoring employers business being a contributing factor. Trustees are urged to seek specialist covenant advice where, amongst other things, the assessment is complex or the scheme is heavily reliant on the covenant. Trustees should be conversant with TPRs guidance 'protecting schemes from sponsoring employer distress'.

Trustees approach to valuations will vary depending on the sponsoring employers COVID experience, which could range from little or no impact to a lasting effect resulting in uncertain future prospects. Stress testing, potentially looking at scenarios considered by the employer, is suggested, particularly in those situations where the future is less clear where trustees will need to determine the potential for significant deterioration in the covenant. Employers should be prepared to share financial projections and business plans with trustees to enable decision making. Trustees should, at a minimum, understand key variables and factors influencing the forecasts. In a situation where COVID-19 has an ongoing effect on the employer, trustees should not assume that the covenant will return to normal without justification. In framing recovery plans, trustees will need to balance sustainability of the employer with fair treatment to the scheme, for example by the employer pausing dividend payments. This is a theme we see coming though from guidance issued by TPR in the immediate aftermath of the COVID pandemic.

Brexit may also have impacted the covenant and trustees will need to factor changes into their considerations.

Conclusions from the above considerations will influence the recovery plan. TPR expects that, where the employer cashflow position allows, recovery plan lengths should be shortened. Any requests from the employer to reduce or defer contributions in the short term should be considered with care and offset by higher contributions at a later date rather than by extension of the recovery plan. Ongoing dividend distribution would be inconsistent with such a request, with repayment of deferred deficit contributions taking priority. Trustees should consider seeking mitigation for reduced or deferred deficit recovery contributions. Such mitigations could include suspension of distributions, contributions made dependent on certain triggers related to employer performance, putting contingent assets in place and ensuring that any support offered to other group companies is in the best interests of the scheme. Trustees need to be aware of any covenant leakage, seeking mitigations where deemed necessary.

TPR encourage frequent covenant monitoring with key indicators tracked, including developments in the wider group of a sponsoring employer. Suitable contingency plans should be made in conjunction with the employer so that they are ready for implementation should the need arise. TPR may seek evidence to demonstrate that liaison with the employer has taken place.

The need for vigilance extends to assessment of the impact of any employer corporate transactions, again trustees should be ready to react and seek mitigations and to ensure fair treatment of the scheme. Trustees should be made fully aware of such proposals and maintain an audit trail of their considerations in such situations which TPR may ask to see evidence of. Should a valuation be ongoing at the same time as a corporate transaction, this will be factored into the valuation but separate mitigation should be sought.

The statement refers to new and complex rules and procedures for distressed companies (indicating PPF guidance) and suggests that specialist advice is sought where relevant.

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TPR

TPR: Annual Funding Statement 2021 (cont.)

Managing risks

The importance of integrated risk management ("IRM") covering employer covenant, investment risk and funding plans and providing key information is reiterated. The Statement adds that climate change impacts on IRM should be considered, with assessment, mitigation and monitoring of climate risk critical to good outcomes. Climate change may impact on employer covenant, investment strategy and actuarial assumptions. TPRs climate change strategy is also mentioned noting that TPR expects all schemes to publish SIPs and Implementation Statements; TPR will use these documents to monitor how trustees identify and manage climate change risk.

The Statement goes on to discuss how setting a clear strategy for achievement of a long-term goal within an evolving IRM framework is beneficial in meeting the key objective of paying promised benefits. The trustees and the employer set a long-term funding target ("LTFT") targeting reduced dependency on the employer at maturity and high resilience to risk. A journey plan leads to the LTFT, with short-term investment and funding strategies also aligned and any departure from the target managed. This is a fundamental principle from TPR's proposed new Funding Code. The setting of a long-term strategy to achieve a long-term objective will become a legal requirement under the Pension Schemes Act 2021.

Scheme maturity will also need to be factored in, balancing assets and the level of underfunding with the scheme's ability to close any funding gap. As schemes become more mature, employers will need to fund the scheme to ensure these risk are adequately managed. The need for an Own Risk Assessment (ORA) for schemes builds on IRM as it requires consideration of the management of risks. An early start on documenting key risks and how they are managed is advocated as schemes will need to complete their first ORA within the next 3 year valuation cycle.

The Regulator's approach is outlined. It will engage with schemes where corporate stress is identified to ensure that regulatory guidance is being followed, risk assess valuations (trustees will need to be prepared to justify and evidence the approach taken) and may also investigate or intervene in a valuation where no agreement has been reached or the assumptions or recovery plan fall short of required standards, potentially using new powers granted in the Pension Schemes Act 2021. TPR's expectations are set out in tables stratified by funding strength, covenant and scheme maturity. Key risks and funding plan features are noted. Trustees should consider whether their covenant has been impacted by COVID-19 or Brexit, how mature they are and what their funding position is. This will enable them to identify the most appropriate table setting out TPR expectations and suggestions for preparing recovery plans.

TPR's Annual Funding Statement was followed on 24 June by their Annual Funding Statement Analysis 2021. This considers Tranche 16 valuations – those dated between 22 September 20 and 21 September 21. Key highlights noted are the increase in asset returns and a general reduction in gilt yields over the period. Changes in the calculation parameters have meant technical provisions are likely to have grown over the three year period. Experience between schemes varied depending on a number of factors including investment strategy.

TPR analysis suggests that if all schemes in the Tranche had a valuation at 31 March 21 and generally maintained their recovery plan period, many would need to increase deficit repair contributions, though the limited affordability of this to employers due to the COVID-19 crisis is noted. The Analysis highlights that changes in the employer covenant are a key consideration in considering funding and risk management and that schemes may need to rethink their technical provisions and recovery plans in light of changes to covenant strength post COVID-19, scheme funding levels and affordability.

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DC update: Summary of requirements for the annual chair's statement August 2021

With the draft Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021 having now been made, there are a number of changes ahead for trustees of defined contribution schemes.

Net investment returns

— Trustees of all 'relevant schemes' regardless of asset size, are required to calculate and state in the chair's statement the net investment returns for their default(s) and for each fund which scheme members are, or have been able to, select, and which scheme members are invested during the scheme year. (Net investment returns refers to the return on funds minus all transaction costs and charges.)

— The first chair's statement to include this information should be for the **first scheme year that ends after 1 October 2021.**

New detailed Value for Members assessment

— Trustees of DC schemes with total assets of less than £100 million and that have been operating for at least three years ("**specified schemes**") are required to assess key elements of the value achieved by their scheme on behalf of members.

— When carrying out the value for members assessment, trustees must consider 3 factors:

1. Costs and charges
2. Net investment returns against three other schemes
3. Administration and governance.

— A specified scheme must compare itself with three comparison schemes, where each scheme used as the basis for the comparison should be:
  - an occupational pension scheme which on the relevant date (the date on which the trustees obtained audited accounts for the scheme year that ended most recently) held total assets equal to or greater than £100 million; or
  - a personal pension scheme, which is not an investment-regulated pension scheme within the meaning of paragraph 1 of Schedule 29A to the Finance Act 2004.

— When selecting the three comparator schemes the 2021 Regulations also require that trustees of specified schemes must 'have had discussions' with at least one of the comparator schemes about a transfer of the member's rights if the specified scheme is wound up.

— The outcome of the value for member assessment must be reported in the annual chair's statement and published on a publicly accessible website. The outcome must also be reported to the Pension Regulator (TPR) via the annual scheme return.. This includes outlining next steps, where trustees conclude that their scheme does not provide good value for members, either immediate improvement or consolidation/wind-up.

— The new assessment is required for **the first scheme year ending after 31 December 2021.**

— Schemes with assets of £100million or more are to continue to comply with the current requirements for assessing value for members by reviewing the extent to which member-borne costs and charges represent good value for members, although they will be able to choose to voluntarily adopt the new form of assessment.

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DC update: Summary of requirements for the annual chair's statement August 2021 (cont.)

Revised Statutory Guidance

The DWP has published Statutory Guidance for trustees of relevant schemes on completing the annual value for members assessment and reporting of net investment returns. The DWP has also published updated Statutory Guidance on reporting costs, charges and other information.

The two sets of guidance are effective from **1 October 2021.**

Trustees are advised to read the Guidance alongside the Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021.

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The Pension Schemes Act 2021

On 11 February, a date described by Guy Opperman, Parliamentary Under-Secretary of State for Pensions and Financial Inclusion, as "a historic day", the Pension Schemes Bill received Royal Assent, becoming the Pension Schemes Act 2021.

The Act, whose original aim was stated as being to "…To help people plan for the future, …..to provide simpler oversight of pensions savings. To protect people's savings for later life, new laws will provide greater powers to tackle irresponsible management of private pension schemes", provides a framework with much of the detail following in Regulations. The first of these, looking at climate change disclosures, is already out for consultation but it will be some months yet before all provisions of the Act are in force.

Key themes include new powers for TPR, scheme funding and climate change disclosures, anti-scam provisions and new frameworks allowing the development of pensions dashboards and Collective Defined Contribution ("CDC") Schemes.

TPR

TPR have been given significant new powers.

Contribution Notices ("CN")

Two new tests have been introduced allowing TPR to issue CN:

- Employer insolvency test – may be used if TPR is of the opinion that the value of the assets of the scheme is less than liabilities of the scheme and an act or failure would have materially reduced the amount of s75 debt due. Several defences are noted: taking due consideration of the extent to which an act or failure would reduce the amount recovered, taking all reasonable steps to minimise the effects, a reasonable conclusion that debt would not be reduced and the valuation of assets equalling or exceeding liabilities.
- Employer resources test - may be used if TPR is of the opinion that an act or failure reduced the value of resources of the employer and the reduction was material relative to s75 debts in relation to the scheme. Defences noted in this situation: due consideration given, taking all reasonable steps, a reasonable conclusion that act or failure would not bring about a reduction in value of the resources of the employer.

Clarification is given as to dates for determining CN amounts.

A new criminal offence of failing to comply with a CN is introduced with financial penalties up to £1 million.

New Powers

More controversial new powers are the introduction of criminal sanctions for avoidance of employer debt and for conduct risking accrued scheme benefits. The offence of avoiding employer debt is committed if conduct prevents recovery of whole or part of a debt under s75, prevents such debt becoming due, compromises or settles a debt, or reduces the amount of the debt, with intent and without reasonable excuse. In the case of the offence of conduct risking accrued benefits, an offence is committed if conduct has a material detrimental effect on the likelihood of accrued benefits being received, the person knew or ought to have known conduct would have that effect and had no reasonable excuse. Both new criminal offences attract maximum of a 7 year prison sentence or a fine, or both.

The new offences are very widely drawn. Concern has been expressed by commentators that these provisions may inhibit normal business transactions. On 11 March, TPR published a draft policy for consultation (which closed on 22 April) on how it will use these new powers. The policy is intended to evolve as case law clarifies the primary legislation.

Click here for more info on the draft policy.

However, any indications TPR may give will only be in the form of guidance and will not have the authority of legislation. TPRs draft policy highlights that there is no clearance process for the new offences as exists for Contribution Notices.

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Legislation

The Pension Schemes Act 2021 (cont.)

Notifiable Events

The 2021 Act also builds on the content of the 2004 Act in relation to notifiable events, adding detail of when notice is required to be given and by whom. An accompanying statement is required on notifications describing the event, its effects, mitigations and communications with the trustees about the event. Financial penalties apply for failure to comply.

Information gathering

Interview powers are clarified and greater detail is given around TPR's powers of inspection. TPR may issue a fixed penalty notice including escalating penalties for failure to comply with an interview request.

David Fairs of TPR commented that "Enhanced information-gathering powers will significantly aid our investigations by giving us more tools to progress them effectively and efficiently, including by being able to compel people to attend interviews and giving us broader powers to conduct inspections."

Financial penalties are also introduced for providing false or misleading information to TPR or to trustees / managers of schemes.

Financial penalties

A new financial penalty regime is set out with a maximum penalty of £1 million. Notice of any penalty must stipulate periods for payment and reasons for its imposition.

Relevant dates for recovery of the debt by TPR are clarified.

Pensions Dashboards

The new Act introduces provisions facilitating the introduction of Pensions Dashboards. Guy Opperman has stated that the passing of the 2021 Act will speed up the creation of dashboards and allow required secondary legislation to progress.

A dashboard service is defined as 'an electronic communications service by means of which information about pensions may be requested by, and provided to, an individual or a person authorised by the individual.' Requirements will prescribe what information is to be provided (to include state pensions, additional pensions and information relating to individuals), circumstances in which it is to be provided and how a service is to be established, maintained and operated. Providers will need to be approved, satisfy certain conditions and provide specified information, facilities or services. Providers will also be expected to cooperate and coordinate activities with Money & Pensions Service ("MaPS") and enable MaPS to monitor compliance. Personal data processing should not breach data processing legislation. Regulations are to follow setting out provision, and facilitating provision, of information by schemes by means of a dashboard service with information to be made available including the constitution, administration and finances of the scheme and information relating to benefits.

Regulations will follow giving more detailed requirements and compliance arrangements. TPR will have powers to issue compliance and penalty notices.

The Act also includes a requirement for MaPS to provide a dashboard service which may provide information about state pensions, basic and additional retirement pensions and state pension information relating to an individual.

Funding

A separate schedule to the Act covers amendments to Part 3 of the Pensions Act 2004, looking at scheme funding. Trustees will be required to determine and, if needed, revise a strategy (a 'Funding and Investment Strategy') for ensuring that pensions and other benefits can be provided over the longer term.

The Strategy must specify the funding level the trustees intend the scheme to have and the investments they intend the scheme to hold on relevant dates. Regulations will follow setting out prescribed matters which may include actuarial methods, the level of detail to be included, the period in which the strategy must be determined and providing for review and revision. Civil penalties apply for failure to comply. The trustees must also prepare a Statement of Strategy as soon as practicable after

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Legislation

The Pension Schemes Act 2021 (cont.)

determining the scheme's Funding and Investment Strategy. This will comprise the Funding and Investment Strategy and supplementary matters (the extent to which the Funding and Investment strategy is being successfully implemented and, where it is not, the steps proposed to remedy the position), the main risks faced in implementation and any reflections on any significant decisions taken in the past which are relevant. Trustees must consult the employer in preparing or revising the supplementary matters.

The Statement of Strategy must be signed by the Chair of the trustees. Again, more regulations are expected to add greater detail. The Act also provides that a scheme's technical provisions shall be calculated in a way which is consistent with the scheme's Funding and Investment Strategy and that trustees must send copies of actuarial valuations and the Statement of Strategy to the Regulator. Regulations will also set out requirements for appropriate recovery plans.

Climate change

Wealth invested in UK private pension schemes is now estimated to be in excess of £6 trillion with many investors having a keen interest in seeing their money invested sustainably. David Fairs of TPR has noted that "trustees are expected to step up and put climate change at the heart of scheme governance".

The Act provides for the issue of regulations (published, see article) ensuring trustees implement effective governance of a scheme in respect of the effects of climate change and risks and opportunities arising, including review of exposure of the scheme to risks, assessing assets as to their contribution to climate change and determining, reviewing and revising a strategy for managing the scheme's exposure to risks and targets. Trustees must measure performance against these targets. Trustees will be required to take into account different ways in which the climate might change and different steps that might be taken, adopting prescribed assumptions including steps towards, and achievement of, the Paris Agreement (holding the global average temperature increase to below 2°C above pre-industrial levels). Regulations will require publication of information relating to the effects of climate change, free of charge and in a prescribed form. Regulations will also ensure compliance, giving TPR authority to issue compliance notices and penalty notices.

Transfer values

Further provisions in the Act focus on rights to cash equivalent transfer values. Trustees may be unable to make transfers if certain conditions are not met concerning for example, the member's employment, residence or the member obtaining information or guidance.

CDC

A framework for the development of CDC schemes is set out in the Act. This includes authorisation conditions and requirements for actuarial valuations to be obtained. TPR will authorise schemes, maintain a listing, and require supervisory returns. Significant events will be notifiable with published Regulations setting out the detail. TPR may also issue risk notices, requiring trustees to submit a resolution plan, where there is an issue of concern or TPR consider that the scheme will breach authorisation criteria. Authorisation may be withdrawn on the occurrence of a triggering event. Once a triggering event occurs, the scheme will need to pursue one of 3 stated continuity options – to wind up, to resolve the triggering event or to convert into a closed scheme. Regulations contain a lot of the detail but trustees will need to produce an 'implementation strategy' within a set timeframe if a triggering event occurs setting out how the interests of members are to be protected including information about administration costs, the relevant continuity option and how it will operate.

Conclusions

As already noted much of the detail is to follow in Regulations which may take time to produce. The thinking behind the Act was first developed pre COVID-19 – it remains to be seen whether the current economic conditions impact the Government's timeframe for action.

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The Pension Schemes Act 2021: draft policy for consultation

TPR's draft policy acknowledges that the introduction of the new offences was not intended to change commercial behaviour, but to give TPR additional powers to deal with more serious intentional or reckless conduct. TPR do not expect to fundamentally change the activity they investigate but will have new powers in dealing with those cases. The new powers will be used to further TPR's statutory objectives, to protect savers and as a deterrent in cases of serious poor behaviour. Criminal liability extends to anyone who helps and encourages another in committing the offence, unless they have reasonable excuse (which is likely to apply to professionals acting in accordance with their professional duty). TPR's draft policy gives a series of examples illustrating behaviours which can expect to be prosecuted.

The statutory exception of reasonable excuse is also discussed. TPR will expect those investigated to highlight any evidence supporting a reasonable excuse and recognise that this will be fact-specific. There are three factors to be taken into account, i) whether the detrimental impact was incidental to the main purpose of the action, ii) whether adequate and fair mitigation was provided and iii) whether there was a viable alternative which could have lessened the impact. Illustrative examples are given for each of these factors. Other factors may be influential in TPRs decision on whether to investigate, for example the extent of openness and timeliness of communication with TPR.

The new offences are similar to TPRs existing power to issue Contribution Notices. However, there are differences including the burden of proof in prosecuting for the new offences lying with the prosecution (in establishing a reasonable excuse, TPR will expect documented explanations for actions taken), the new offences can be committed by anyone (not just the employer) and the new offences can only be committed where a s75 debt is due (whereas a CN can be issued regarding a debt which might become due).

TPR indicate features which they will consider in selecting cases for investigation. These are noted as:

- The primary purpose being the abandonment of the scheme without appropriate mitigation
- Significant financial gains have been made to the detriment of the scheme
- Unfairness in the treatment of the scheme
- The trustees, TPR/PPF have been misled or not appropriately informed.

In investigating and prosecuting, TPR's policy will be to engage early, adopting a 'fair, balanced and impartial' approach.

D Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice, commented on TPR's approach in a speech delivered on 30 March:

"Our goal is to work with Department for Work and Pensions, the regulated community and wider industry and stakeholders to ensure the new measures are introduced in an effective way. We will we only use these powers where it is appropriate and reasonable to do so."

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Legislation

Pensions Scams: Empowering Trustees and Protecting Members - consultation

On May 14 the DWP issued a consultation on draft regulations (The Occupational and Personal Pension Schemes (Conditions for Transfers) Regulations 2021). The Ministerial Foreword reiterates that the Government is committed to working to protect people from pension scams. The new measures aim to strike a balance giving savers flexibility in their choices and at the same time protecting against scam activity. The proposed provisions empower trustees and 'put them in the driving seat' in relation to pension transfers by enabling them to prevent a transfer where there are risks to the member's savings, although it is intended that little intervention will be needed in cases which trustees consider low risk.

These regulations flow from s125 of the Pension Schemes Act 2021 and set out provisions for trustees to allow a member to transfer out of their scheme into another personal or occupational scheme. The proposed measures include 4 conditions, one of which will need to be met before a transfer can go ahead.

The first condition allowing the transfer to proceed will be for trustees to identify if the transfer is to one of a set of scheme types, namely:

- Public Service Pension Schemes,
- authorised Master Trusts,
- authorised Collective Money Purchase Schemes, or
- personal Pension providers, authorised and regulated by the Financial Conduct Authority ("FCA") which are, or are within the same group as, an insurer authorised by the Prudential Regulation Authority ("PRA").

If the first condition is not satisfied, then the transfer can only occur if evidence set out in regulations is provided by the member as noted below.

In the case of transfer to a UK occupational scheme, evidence of an employment link between the scheme, the member and the employer is required – this is the second condition. The nature of the evidence required is set out in the regulations and comprises evidence of the member making a transfer to the same scheme in the last 12 months or a letter from the employer, payslips, a schedule of payments to the scheme and bank statements.

In the case of an overseas scheme ("QROPS"), if an employment link cannot be evidenced, then a residency link (demonstrating residence in the same financial jurisdiction as the QROPS for at least 6 months) must be established – the third condition. Evidence will be required of the member making a transfer to the same scheme in the last 12 months or formal residency documentation (which will vary between jurisdictions). TPR will provide guidance on the requirements.

If conditions 1 – 3 do not apply, then it will only be able to proceed if the fourth condition is satisfied. Trustees will need to determine whether 'red' or 'amber' flags are present. In the presence of a 'red' flag, trustees would be able to prevent a transfer. If 'amber' flags are present, a transfer can go ahead if the member seeks advice and gains evidence of that advice from MaPS or they have made a transfer to the same scheme in the last 12 months and taken advice in that period. Where flags are evident, trustees can request further information to assess the transfer. Standard questions to use in information gathering, aiming to provide clarity on the detail required, have been drafted by the DWP and others and are included as part of the consultation document. Should a member not provide information or evidence of taking MaPS guidance when requested, this will be a 'red' flag.

Red flags are identified as situations where:

- financial advice has been provided by those without appropriate regulatory permissions (or taken recommendations from such people)
- the member has been contacted unsolicited
- the member was offered incentives to transfer, including free pension reviews and cashback
- the member was under pressure to completer the transfer quickly.

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Legislation

Pensions Scams: Empowering Trustees and Protecting Members - consultation (cont.)

Amber flags are defined as situations where:

- high risk or unregulated investment are included in the receiving scheme
- fees are being charged by the receiving scheme which are unclear or high
- the proposed investment structures are complicated or unorthodox,
- the receiving scheme includes overseas investment or any of the advisers are based overseas, and
- there has been a high volume of transfers to a single receiving scheme or involving a single adviser or firm.

Within one month of requesting a transfer or a statement of the value of their transferable rights, trustees must inform members about the conditions for transfer set out in the Regulations and the need for one of the conditions to be met before a transfer can be actioned.

The draft Regulations have received mixed reactions from the industry although commentators have welcomed further protection from scammers. Industry guidance will be welcomed, given the complexity of the proposals. The consultation ran until 10 June 2021, with the intention that the Regulations will be in force from Autumn 2021.

June also saw the Government's response to the Work and Pensions Committee's report 'Protecting pension savers – five years on from the pension freedoms' confirming broad support for the proposals commenting that work is already being progressed and noting that further action may be considered. The Government response gives an overview of the steps already taken to combat pension scams, including the establishment of Project Bloom (a multi-agency co-ordinated response to scam activity), a ban on pensions cold calling, the formation of the Money and Pensions Service (MaPS) and the above mentioned consultation on proposals for a new transfer approval regime, whilst recognizing that a joined-up response provides the best defence against a sophisticated and evolving threat.

Government agree that reporting of scams needs to improve within industry, noting the Ministers letter to122 schemes in March urging them to work with the Pensions Industry Scams Group ("PSIG") to share data with Project Bloom partners. The success of TPRs 'Pledge to Combat Pensions Scams', urging reporting to Action Fraud (the UK's national reporting centre for fraud and cybercrime) is referred to with 285 organisations signed up by June 2021.

Prevention is also a key theme. An April Ministerial roundtable chaired by the Home Office and the Department for Digital, Culture, Media and Sport ("DCMS") and including representatives from the tech and banking industries considered responses to threats from online fraud with participants agreeing to develop a tech sector charter tackling fraud, an idea already being progressed by the Joint Fraud Taskforce in relation to other sectors.

The response also noted that while the Online Safety Bill will include measures to combat fraud, fraud facilitated through paid-for advertising will not be covered, going against the FCA's stance on this issue. This will instead be reviewed as part of the DCMS's Online Advertising Programme and a consultation will emerge later this year.

A Fraud Action Plan is being developed by the Economic Crime Strategic Board (chaired by the Chancellor and Home Secretary) to encourage further action against fraud. The Government response notes that Project Bloom has progressed well as has Scamsmart (led by the FCA) which has reached 80% of savers in the most 'at risk' 45 – 64 year age group.

Enforcement activity is also having an impact, for example the collaborative efforts of law enforcement and the private sector in the Joint Fraud Taskforce and TPR activity (including trustee appointments to schemes potentially used by scammers and working with law enforcement and the Insolvency Service). FCA activity has also produced results with thousands of reports of unauthorised activity assessed and many alerts issued. The FCA has committed to publishing further information on its activities.

Support is offered to fraud and cybercrime victims through the National Economic Crime Victim Care Unit ("ECVCU") to aid recovery and prevent people becoming victims in the future. MaPS also support scam victims through the development a Pension loss tool and offering victims Pension Loss appointments.

As pensions fraud continues to evolve responses from Government and industry are likely to develop further.

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Legislation

Consultation: Collective Money Purchase Schemes Regulations 2021

As referenced in the article on the Pension Schemes Act 2021 (see article), in July the Dept for Work and Pensions issued a consultation on draft regulations setting out how Collective Money Purchase Schemes (or Collective Defined Contribution – ("CDC")) schemes will operate. Although referencing the Royal Mail scheme, the proposed regs will enable the launch of CDC schemes more generally. The PSA 21 sets out a framework for CDC provision with the proposed new regulations adding more flesh to the bones. The Pensions Regulator will authorise and supervise CDC schemes and produce further guidance in a Code of Practice (which will be issued after a further separate consultation).

Authorisation is intended to build confidence in the new regime. Guy Opperman (Minister for Pensions and Financial Inclusion) notes that "CDC schemes can only succeed if there is confidence in this new type of provision. These regulations will help ensure that CDC schemes are set up and run well by providing clear criteria…"

The proposed regulations cover various aspects of a scheme's operation with further detail given in a series of appended schedules.

The proposed regs set out the information to be supplied on application for authorisation including analysis of financial sustainability, details of systems and processes used for communicating with members and relevant persons and in the running of the scheme and note that a fee is payable. Schedules provide more detail – schedule 1 in relation to matters that the Regulator must take into account in assessing the 'fit and proper persons' requirement and schedule 2 around the 'scheme design' requirement. Schedule 2 covers the contents of the viability report, annual certification and matters for the regulator to take into account.

Regulations set out two 'gateway tests' to be applied when seeking authorisation. The first assesses inflation proofing, ie whether expected increases in benefits keep pace with the expected consumer prices index. The second looks at whether the scheme is 'value for money' and is applied at authorisation and annual re-certification of viability by comparing value of expected benefits to contributions paid into the scheme.

Schedule 3 covers the financial sustainability requirement considering the information to be provided including costs of setting up and running the scheme, sources of scheme income, strategy for meeting any shortfall and matters for the regulator to take into account. Where an employer has agreed to meet costs relating to the scheme, information must also be provided in respect of that employer.

Matters for the regulator to take into account regarding communication are set out in Schedule 4 and include IT systems, resource planning, quality assurance and member engagement. Schedule 5 sets out matters in relation to systems and processes, to enable the regulator to decide whether the scheme can ensure it is run effectively. This covers IT systems and processes, member records, trustee governance and TKU, contracting and monitoring of service providers, wider governance, risk management, security, resource planning, investment management and monitoring, valuation and benefit adjustment and member engagement.

The proposed regulations also require a lot of detailed information to be disclosed around the selection of a continuity strategy including the steps they would take to decide which option to pursue and the timescales of those steps, decisions and actions to be taken and communication strategies. In relation to certain information, the regulator is also required to consider how robust any assumptions are. Continuity strategies must be made in writing and in compliance with a Code.

Regulations also cover detailed provisions relating to the calculation of benefits. And make clear that trustees of CDC schemes must determine, after actuarial advice, which assumptions are to be used for determining the adjustment of benefits provided under the scheme. An initial valuation must be obtained within one year of the operation of the scheme and annually thereafter to be received by the trustees within 10 months of its effective date and passed to the Regulator within 10 days of the date of the trustees' receipt. Reporting requirements in relation to benefit adjustments are set out where adjustments have not been applied in accordance with the scheme rules.

Part 5 of the proposed regulations covers ongoing supervision including supervisory returns, and details of 'significant events' to be notified to the Regulator. These include significant changes to the scheme's investment strategy and certain changes to the scheme's design. The contents of and time frames for the issuing of, or responding to, risk notices and giving progress reports are also given.

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Legislation

Consultation: Collective Money Purchase Schemes Regs 2021 (cont.)

Notification requirements around triggering events and deadlines are included in Part 6 of the proposed regs, together with information to be included in an implementation strategy about the levels of admin charges and other items, the format of the strategy and timeframes for availability. A separate schedule covers requirements for those following continuity option 1 (winding up). Timeframes are given for those following options 2 and 3. Detail around the content and timeframes for periodic reporting are given. More detail is also given around the prohibition on increases in charges during a triggering event period.

The annual recertification by the actuary must consider two ‘backstop’ tests in assessing whether schemes should close to future accumulations. These look at value for money and limiting cross-subsidies across time periods. The consultation sought views on these tests and the ‘gateway tests’ mentioned earlier. Detail in schedule 6, covering continuity option 1), discusses, inter alia, alternative ways of discharging the scheme’s liability, the requirements of scheme rules, the date of commencement of winding up, quantification of the value of beneficiaries accrued rights to benefits, restrictions during the winding-up period, the payment of ‘periodic income’ (rather than scheme benefits), required notifications and correspondence and trustees powers and duties.

A number of proposed consequential amendments to existing Regulations are proposed, including provisions requiring CDC schemes to publish various documents. The consultation period ran from 19 July to 31 August. Once established it is hoped that, as Guy Opperman states, ‘collective provision can benefit millions of pension scheme members when its full potential is realised’.

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ESG

ESG Essentials

As ESG and Climate Change is constantly evolving and invariably in the news, "ESG Essentials" gathers together the developments in the ESG world over the month and pulls out key points for occupational pension schemes.

Igniting an investment Big Bang: a challenge from the Prime Minister and Chancellor to the UK's institutional investors

The 4 August 2021 saw the Prime Minister and Chancellor challenge the UK's institutional investors to invest a greater proportion of capital in long-term UK assets

The open letter says, "Currently global investors, including pension funds from Canada and Australia, are benefitting from the opportunities that UK long term investments afford, while UK institutional investors are under-represented in owning UK assets. For example, over eighty per cent of UK defined contribution pension funds' investments are in mostly listed securities, which represent only twenty percent of the UK's assets. While we are glad that international investors prize UK assets, and are working hard to attract even more inward investment, we also want to see UK pension savers benefitting from the fruits of UK ingenuity and enterprise, being given the opportunity to back British success stories, and secure higher returns and better retirements."

Continuing with "To seize this moment, we need an **Investment Big Bang** to unlock the hundreds of billions of pounds sitting in UK institutional investors and use it to drive the UK's recovery. It's time we recognised the quality that other countries see in the UK, and back ourselves by investing more money into the companies and infrastructure that will drive growth and prosperity across our country."

The letter goes on to say "Whether you are a trustee or manager of a DC or DB pension fund, running an insurance company or advising investors on their investment strategy, we are challenging you this summer to begin to invest more in long-term UK assets, giving pension savers access to better returns and enabling them to see their funds support an innovative, healthier, greener future for their country. We know that this will require a change in mindset for many investors that won't happen overnight, but that is why this change needs to start now."

The Pensions Regulator lifts proposed 20% restriction in private markets

The Pensions Regulator confirmed to the Financial Times on 6 August 2021 that it will not proceed with its proposal to cap investment in unquoted assets to no more than a fifth of a portfolio.

"TPR is committed to protecting and enhancing savers' retirement outcomes, so welcomes calls for trustees to consider the full range of investments available to meet that aim," said David Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice.

"Trustees of pension schemes have an obligation to invest in the best financial interest of their members. Pension schemes generally have a longer-term investment horizon which enables them to consider investing in a wider range of assets."

TPR Blog: **Why trustees do have influence in the shift to UK net zero**

On 10 August 2021, the Regulator published a blog by David Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice. In it, he explains how schemes can and must make a difference in the transition to a net zero economy.

Following on from the launch of the consultation on TPR's new climate-related guidance issued last month, Mr Fairs said "We urge all trustees and advisers to take this chance to shape our guidance and join in the consultation, which ends on 31 August."

"Pensions schemes can and must make a difference in the transition to a net zero economy."

Mr Fairs continues, "Even where trustees feel their advisers and asset managers are doing a satisfactory job considering climate-related risks and opportunities, the trustees have a duty to monitor whether their expectations are being met. Trustees should challenge asset managers and advisers to improve their processes where appropriate. Ultimately, if a scheme's advisers do not sufficiently consider the risk and opportunities from climate change trustees can vote with their feet by re-tendering with mandated climate-related criteria or by appointing specialists."

TPR also encourages trustees to sign up to the 2020 UK Stewardship Code.

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Pensions Dashboard Programme - plans for 2021 and data standards

The receipt of Royal Assent on 11 Feb was a significant step in the introduction of Pensions Dashboards. We now expect to see secondary legislation emerging and the Pensions Dashboard Programme ("PDP") continuing to develop at pace. This will build on recent activity.

In April the PDP issued their latest progress update report. The report confirmed that the programme remains on track with procurement of digital architecture underway and the hope of the contract being awarded in the next six months. Procurement of the identity service will also soon begin, with an initial 2 year appointment prior to the adoption of an identity service under the UK Digital Identity and Attributes Trust Framework, once established. Progress continues to be made in developing an onboarding strategy, including looking for volunteers to test the system.

Over the following six month period, procurement exercises will continue and work will include the onboarding strategy, consumer protection, user needs, design standards and collaboration to support secondary legislation emerging from the Pension Schemes Act 2021.

We have already seen some activity. During May the PDP issued a call for input on staging proposals referring to a data providers hub which contains directions for data providers such as schemes in linking up to dashboards. The proposals aim to balance the competing demands of consumers, data providers and the PDP in ensuring the systems work. Staging is proposed in three waves:

- wave one (starting in April 2023 and running for two years): largest schemes (1000+ memberships)
- wave two: medium schemes (100 to 999 memberships)
- wave three: small and micro schemes (99 or less memberships)

Wave one will be further split down into three cohorts; master trusts and FCA regulated providers of personal pensions; defined contribution schemes used for Automatic Enrolment; and all remaining occupational schemes with 1,000+ memberships (in order of size) [the largest defined benefit (DB) schemes to onboard in 2023].

The industry has broadly welcomed the PDP proposals on staging, though with some reservation expressed. Concerns noted include:

- remaining uncertainties and dependencies (e.g. on tech providers);
- the potential for any requirement to provide an Estimated Retirement Income (ERI) to delay the project; several commentators suggesting providing 'match' or 'find' data before full ERI information;
- the need for clear communication so that users understand the data they are able to view will be crucial; in particular the need for inclusion of state pensions is seen as key.
- potential exposure to fraud.

Although compulsory staging will commence in 2023, volunteer data providers will begin to stage long before then, some as early as late this year. In a recent blog, the PDP confirmed that seven pension providers have volunteered for this early (or 'Alpha') testing phase with further volunteers lined up for later testing phases. Lessons learnt from early testing will help frame future plans for onboarding. The blog calls for further providers to volunteer for later testing phases.

The PDP have also issued a response to the earlier call for input on the identity service which revealed some concerns with knowledge of the structure of the core architecture, clarity around the identity proposals and solution and alignment of legislative requirements. It is hoped that the information provided within the data providers hub will alleviate some of these concerns, with more information to follow.

Another significant stage for the PDP came in April with the issue of an ITT for the contract to supply major elements of the digital architecture, including the pension finder service ("PFS"), the consent and authorisation service and the governance register.

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Pensions Dashboard Programme - plans for 2021 and data standards (cont.)

The current timeline outlines that during 2021-2, the PDP will undergo a 'develop and test phase' before moving onto voluntary onboarding and ongoing testing followed by staged onboarding and a 'Dashboards Available' point in 2023.

Member engagement is central to the success of the PDP.

This is recognized in the production of a Rapid Evidence Assessment report, published in June, which discusses barriers to engagement and ways they may be overcome. Barriers are identified as inertia, bias to immediate rewards, friction (inconvenience) costs, choice overload, and lack of knowledge or ability.

Insights can be drawn from behavioural science with key strategies proposed to lessen these barriers including timely prompts to engage, encouraging members to consider their future position, simplifying processes and providing 'rules of thumb' to simplify complex decisions. Demographics are also seen to contribute to the level of member engagement with older members and those more financially literate being more likely to engage. The key information to include is Estimated Retirement Income (ERI), this can be helpfully supported by future and current balances and the inclusion of supporting guidance. The report also notes that it may be helpful to wait until dashboards are almost complete, as users may be deterred from engagement if information is missing. Presentation is also critical to engagement and will require careful consideration. Dashboards should continue to evolve even after their 'go live' date.

In July, the PDP commissioned a qualitative survey of its intended users. The results will inform future developments.

This follows the issue in March of The Pensions Administration Standards Association's ("PASA") issue of the first of their intended series of guides for schemes looking at how to start preparing for pensions Dashboards.

The PDP data providers hub includes a timeline and steps needed for connection to the dashboards ecosystem. It sets out what data providers need to do at each stage of the programme.

During phase one (programme set up and planning) providers will need a data audit to identify gaps in both 'find' and 'view' data and plan how to fill them. An assessment will need to be made to how much of this data is non-digital and how this can be included. Data cleansing for dashboard should complement other data cleanse activity. Providers need to understand who they will need to communicate with to prepare; this may include software providers in considering connection to the dashboard ecosystem.

Phase two (develop and test) will see early testing and volunteer data providers. Data providers will need to decide on their approach to matching data, i.e. which fields of data to use and conduct an audit to determine any gaps in this data. Partial matches will also need consideration. Providers will need to continue to ensure that 'find' data is complete and accurate. The approach to 'view' data provision (ie 'on demand' or stored) will need to be considered. Change may be needed to the basis for providing Estimated Retirement Income (ERI) as a result of PDP and industry working group findings. Dependencies on third parties should be understood and data providers will need to consider connection in more detail. The impact of high volumes of traffic from the dashboard ecosystem should also be considered – it is estimated that 6-9 million users will access the system each year – and whether any additional software solution would be advantageous to manage this.

On 29 July, PASA announced that it will be working with the PLSA and ABI to develop conventions for matching data. An industry standard, in agreement with regulator's thinking, for data matching is seen as key to facilitate efficient adoption by schemes across all sectors. It is hoped that the initial output from the project will be ready for Alpha phase testing in early 2022.

By phase three (voluntary onboarding and ongoing testing), data providers should be progressing data cleansing and ensuring completeness of information. On an ongoing basis prior to connecting, providers should be validating and auditing data. An approach to data matching and ERI reporting should be in place. Plans for working with dependencies should be in place as should connection plans, including

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Pensions Dashboard Programme - plans for 2021 and data standards (cont.)

implementation and testing to tie into compulsory onboarding dates. Providers may wish to consider any advantages of voluntary onboarding. If data mapping to allow for additional software is being undertaken, this should be progressing.

Once phase four (staged onboarding) is reached, providers should be confident in the availability of digital data. The matching basis and delivery of estimated retirement income ("ERI") should have been tested and assessed before the staging date. Dependency plans should be validated and plans for connection with the ecosystem be in progress to tie into the staging date. This should include testing of find and view functions. Providers should be familiar with the onboarding process and be in a position to start onboarding. Workload will have been considered together with processes for handling queries.

The recent activity follows the December release of the PDP data standards guide setting out expectations in relation to the type of data which needs to be verified and made available to facilitate the new dashboard system. The publication of the PDP's data standards document in December was a significant step. Standards outlined are intended as a starting point and will evolve.

It is suggested that a final set of data standards will be made available once the supplier of the digital architecture is in place. The standards are applicable to all pension providers (a term encompassing occupational pension schemes).

It is noted that lack of comparability in the way estimated retirement income is supplied will present issues. PDP suggest that ERI is initially reported in the 'best possible way', although this may not be optimal. A Working Group will test responses to varying data presentations. PDP will progress with the elements of data used to 'find' pension pots while coming up with a solution to the ERI issue.

The December data standards publication outlines data element definitions (categorized as mandatory, conditional or optional) allowing pension providers to assess their own data for quality and availability. The document includes a process flow chart clearly showing the chain of events leading to the release of data to a member via a dashboard.

What trustees need to do

Trustees should seek advice as to next steps appropriate to their scheme. With onboarding commencing from 2023, time is of the essence for pension providers to review their data to ensure that standards are met. However, the benefits to savers will be significant - a PLSA blog published on 29 June highlighted the benefits of the creation of pensions dashboards, noting that they are likely to be available to savers from 2024 or 2025. The blog anticipates that 'pensions dashboards will propel retirement saving into the 21st century!'

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Small Pots Working Group Report

On 24 May the DWP released a consultation on proposals to limit the charging of flat fees on small pots (the threshold is proposed at £100) to come into force in April 2022. The aim is to prevent any undermining of auto enrolment by protecting members from erosion of their pots. The proposals aim to strike a balance between member protection and financial sustainability of providers. The consultation also seeks views on proposals for a universal charging structure allowing a single percentage annual management charge, based on the value of the member's pot within the default fund with the aim of increased comparability between products. Views are also sought on whether the move to a single charging structure would impact employer choices.

This follows after the Small Pots Working Group, set up to consider issues surrounding the existence and consolidation of small deferred pension pots, published a report In December outlining their findings and conclusions. The Group was set up by Guy Opperman to inform the approach to small pot consolidation while protecting members and controlling charges.

Their findings highlighted the large numbers of small pensions savings pots. It is suggested that the average number of jobs a person might have in their lifetime is in excess of ten. If each of these provides a pension pot (as is required under auto-enrolment legislation), many inefficient small pots will result which may be susceptible to loss through members losing track of them and erosion due to charges. They will not necessarily provide their owners with an incentive to save towards good quality pension provision (damaging the reputation of auto-enrolment policy) and pension providers could suffer if the management of such pots is uneconomical. There are currently estimated to be 8 million deferred pension pots held in Master Trusts with an average value of approx. £1,000. Data collected by the DWP over large DC schemes suggests that three quarters of deferred pots are smaller than £1,000, and a quarter smaller than £100, giving an idea of the scale of the problem. However, the Working Group notes that more analysis is needed. Even smaller 'micro' pots typically resulting from employment changes and in the range £25 to £250 are discussed but no proposals are made in this area.

Some current policy initiatives are already working to alleviate the issue, i.e. proposals for a minimum pot size before flat charges can be made, enhanced pensions planning made available through the advent of Pensions Dashboards and the simplification of benefit statements to improve member understanding.

Consolidation may make the market more efficient and achieve better member outcomes. Fewer pots would result in reduction of charges and administration effort. The report suggests that consolidation should comprise a mix of member-initiated and automatic solutions (such as default small pot consolidation and automatic pot follow member models).

Recommendations

The Working Group suggest that member- initiated solutions should continue to be explored and may be effective if members are engaged with their savings. This fits in with developments in technology, such as dashboards. However, there is also a need for automatic and automated consolidation solutions.

Solutions recommended are:

— Same provider / scheme consolidation of multiple pots for the same member or, as an initial step, a single consumer facing view of pots held.

— Member exchange should be a concept trialed as part of the investigation into administration challenges to be overcome in delivering mass transfer and consolidation systems. Such trials, which should involve a range of stakeholders, would allow investigation of matching capability (to verify identification), data standards, costs, member experiences and safeguards.

— The report also recommends cost / benefit analysis of consolidation models such as default small pot consolidation and automatic pot follow member models, together with 'customer journey mapping' to understand the full impacts.

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Small Pots Working Group Report (cont.)

The report notes that work should be done on administration systems to reduce friction and facilitate large scale consolidation, highlighting the minimum necessary processes. Some progress is being made with the development of data standards by the Pensions Dashboards Programme (see article) which can then be developed further for use in consolidation.

Identify verification is critical; the industry will need to define data fields necessary to provide safeguarded matching capability to ensure the correct recipients of pension pots being transferred, even without member consent. Low-cost bulk transfer processes will need investigating, looking first at the current processes though recognising that automated transfers may require new approaches. Appropriate governance arrangements will need to be considered.

A move towards consolidation will require the investigation and addressing of administrative challenges, to facilitate low-cost mass transfers within the auto-enrollment market. The results, together with assessment of the impact on members, will then inform decisions on larger scale solutions: the report presents a roadmap towards achieving this. Analysis of any need for new legal powers may also be necessary.

As Guy Opperman notes in the Ministerial Foreword, more work is still required to overcome administrative challenges involved however recent industry comment indicates that the rewards could be significant.

The recommendations from the Small Pots Working Group will be taken forward by a new industry group convened by The Pensions and Lifetime Savings Association and the Association of British Insurers. The group will focus on administration processes underpinning a long-term future consolidation model, looking at data-match requirements, common data standards and a low-cost transfer process. A progress report is expected in the summer.

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TCFD recommendations: revised draft climate change regulations and Statutory Guidance issued

Following DWP issuing its response to the "Taking action on climate risk: improving governance and reporting by occupational pension schemes" consultation alongside revised draft Regulations and Statutory Guidance on 8 June 2021, regulations were made in July and will come into force on 1 October 2021.

Schemes with relevant assets* of £5bn or more on the first scheme year end date to fall on or after 1 March 2020 must meet the climate change governance requirements for the current scheme year from 1 October 2021 to the end of that scheme year (unless audited accounts have not been obtained in respect of that scheme year, in which case from the date they are obtained.) Trustees must publish a TCFD report within seven months of the end of the scheme year which is underway on 1 October 2021 (unless scheme relevant assets are zero on the scheme year end date).

Relevant assets are (except in the case of earmarked schemes) net assets of the scheme, excluding bulk and individual annuity policies.

If on or after 1 October 2021 the scheme is an authorised master trust or a collective money purchase scheme, then trustees must meet the climate change governance requirements for the current scheme year which is underway to the end of that scheme year and produce a TCFD report within seven months of the end of the scheme year which is underway.

Where-trustees are subject to the requirements for part of a scheme year, their report need only cover that part scheme year.

The trustees must include a link for the TCFD report in the annual report and accounts produced for that scheme year.

Schemes with £1bn or more assets have an additional twelve months to comply.

The Regulations

Governance

Trustees must establish and maintain oversight of the climate-related risks and opportunities which are relevant to the scheme.

Trustees must establish and maintain processes for the purpose of satisfying themselves that:

- any person who undertakes scheme governance activities otherwise than as a trustee, takes adequate steps to identify, assess and manage climate-related risks and opportunities which are relevant to the governance activities they are undertaking; and
- any person who is not a legal adviser of the trustees and who advises or assists the trustees with respect to scheme governance activities, takes adequate steps to identify and assess any climate-related risks and opportunities which are relevant to the matters in respect of which they are advising or assisting.

Strategy and scenario analysis

Trustees must, on an ongoing basis, identify and assess climate-related risks and opportunities which they consider will have an effect over the short term, medium term and long term on the scheme's investment strategy and the funding strategy (the latter where applicable).

The time periods short, medium and long term are as the trustees determine are appropriate taking into account the scheme's liabilities and its obligations to pay benefits.

Trustees must, as far as they are able, undertake scenario analysis in at least two scenarios where there is an increase in the global average temperature and in one of those scenarios the global average temperature increase selected by the trustees must be within the range of 1.5 and 2 degrees Celsius above pre-industrial levels.

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TCFD recommendations: revised draft climate change regulations and Statutory Guidance issued (cont.)

The scenario analysis must be undertaken in the first scheme year in which the requirements apply and thereafter where trustees have determined that it is appropriate to undertake new scenario analysis or the trustees have not undertaken scenario analysis in the previous two years, new scenario analysis must be undertaken.

Trustees must, in each scheme year except for the first scheme year in respect of which the requirements apply, review the most recent scenario analysis to determine whether it is appropriate to undertake scenario analysis to ensure they have an up to date understanding.

Whenever new scenario analysis is undertaken, the three year cycle is automatically reset.

Note, schemes with DB and DC sections will need to do separate scenario analysis. The Statutory Guidance provides more detail on multi-section schemes.

Risk Management

Trustees must establish and maintain processes for the purpose of enabling them to identify, assess and manage effectively climate-related risks which are relevant to the scheme. Trustees must ensure that theses processes integrated into their overall risk management of the scheme.

Metrics and targets

Trustees must select a minimum of one metric which gives the total greenhouse gas emissions of the scheme's assets ("absolute emissions metric"); one metric which gives the total carbon dioxide emissions per unit of currency invested by the scheme ("emissions intensity metric"); and one other climate change metric.

Trustees will not have to collect and report on Scope 3 emissions in the first scheme year that they are subject to the requirements. The DWP have clarified the timing of the requirements to make clear that they must be carried out in each scheme year, and that where metrics are dropped following review, replacement metrics must be selected.

Each scheme year, trustees must, and as far as they are able, obtain the data to calculate their selected metrics, and use the metrics they have calculated to identify and assess the climate-related risks and opportunities which are relevant to the scheme. This metric selection must be reviewed from time to time as appropriate for the scheme.

Where the first year of application is a part scheme year, activities carried out within the same scheme year in advance of the date of application may be relied upon to meet the requirements. The DWP have also made clear that when trustees drop out of scope and then subsequently come into scope again, they must select metrics in the same way as they are required to do in the first scheme year.

In the first year the requirements apply, trustees must set a target for the scheme in relation to at least one of the metrics which they have selected to calculate and in each scheme year measure, as far as they are able, the performance of the scheme against that target. Having reviewed that performance, and determined that a target should be replaced, trustees must set a new target in relation to one of the chosen metrics.

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TCFD recommendations: revised draft climate change regulations and Statutory Guidance issued (cont.)

The DWP have clarified that performance against the target is the only criterion which trustees must consider in determining whether to retain or replace that target, although they are free to choose others.

"As far as they are able"

"As far as they are able" is defined as trustees taking all such steps as are reasonable and proportionate in the particular circumstances taking into account the costs, or likely costs, which will be incurred by the scheme; and the time required to be spent by the trustees, or any person to whom the trustees have delegated responsibility.

The Statutory Guidance provides more support for trustees, recognising the data restrictions and gaps when calculating scenario analysis and metrics. It also acknowledges the challenges trustees may face when quantifying climate risks for some sovereign bonds, relevant contracts of insurance, asset-backed contribution structures and derivatives. Trustees of defined benefit schemes may also experience limitations in relation to liabilities, funding strategy and employer covenant analysis.

TKU requirements

Trustees are to have an appropriate level of knowledge and understanding of the principles relating to the identification, assessment and management of climate change risks and opportunities. The DWP have amended the drafting of the Miscellaneous Provisions Regulations in relation to knowledge and understanding of opportunities, to align with the language around risks. In relation to both opportunities and risks, clarification has been added that the intention is for trustees to have sufficient knowledge and understanding to enable them to meet the climate governance requirements in Part 1 of the Schedule to the Climate Change Governance and Reporting Regulations.

The DWP add that Trustees are not required to be experts, but have sufficient expertise so that they properly exercise governance over climate change risks and opportunities.

Disclosure requirements

Trustees are required to publish their TCFD report on a publicly available website, free of charge, within 7 months of the scheme year-end. The chair of trustees must also sign the report. In addition, a link to the report must be included in the Annual Report and Accounts (accompanied by a short summary if trustees wish to do so). Members must be notified of the report either in their annual benefit statements, or via the scheme funding statement depending on the scheme.

Trustees must provide the web address where the TCFD is published to TPR, together with the website location for the Statement of Investment Principles, Implementation Statement and excerpts from the Annual Chair's Statement in the annual scheme return form. Trustees who have not yet produced their first TCFD report to inform TPR whether the period for doing so has ended.

Audit implications

At this point, there is no specific requirement for the TCFD report to be audited, but as there would be reference to it in the scheme Annual Report and Accounts, (see article on TPR consultation on the Climate Change Report) the auditor would need to fulfil its responsibilities under ISA (UK) 720 on "Other information" – similar to the Annual Chair's Statement and the Implementation Statement.

Review

Review of the effectiveness of the Regulations and Statutory Guidance for schemes in scope, assessing whether the Regulations remain appropriate, and whether or not they should be extended to smaller schemes will take place in the second half of 2023.

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TCFD recommendations: revised draft climate change regulations and Statutory Guidance issued (cont.)

Penalties

TPR will be able to issue discretionary penalties for inadequate reports, but a mandatory penalty will only be issued for the non-production of a report. In the response, the DWP have also amended the wording regarding the mandatory penalty, to make clearer that it only applies where TPR are of the opinion that a person has failed to publish a report on a publicly available website, accessible free of charge.

Concluding comments

Although data sources and best practice will evolve over time, trustees must educate themselves now on the TCFD recommendations and what it means for their scheme. There is much information and guidance already available, now including the Pensions Climate Risk Industry Group's non-Statutory Guidance which was finalised at the same time the Government published its response and draft regulations and Statutory Guidance in January.

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News in brief

Money and Pensions Service ("MaPS") dashboard update

The MaPS is responsible for building a pensions dashboards (see earlier article) which will be available to the public over the coming months. A recent MaPS blog underlines how dashboards tie into the MaPS vision of greater engagement of members with their pensions savings.

MaPS staff are working closely with the PDP to ensure that the dashboard created meets the required design and service standards and programme timing to enable input into the early dashboard testing phases. Recent research conducted by MaPS into the intentions of users regarding the data gained from dashboards will help them frame the ongoing support which may be needed. Users will need guidance and interpretation of the data to make informed decisions and avoid becoming the victims of scams.

In the blog, MaPS summarise that 'we see pensions dashboards as the start of an information gathering process for individuals: one that leads them towards taking control of their savings and preparing effectively for their retirement'.

New Benefits Statements Working Group

In a press release on Aug 16, PASA announced the formation of a new working group looking at the implications of new government proposals for simplification of benefit statements. This follows a consultation on new regulations and guidance looking at simpler annual benefit statements earlier this year.

The group will consider the various issues raised in the proposals and make recommendations regarding the introduction of a 'Statement season', necessary changes (to law, regulation or process) and guidance for involved parties. An initial paper has been prepared for discussion looking at administration issues arising from the introduction of a statement season, and considering the practicalities around the introduction of a single valuation or publication date.

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News in brief

TPR publishes Annual Report and Accounts 2020-2021

TPR published its 2020-2021 Annual Report and Accounts on 21 July 2021, which highlighted a number of successes despite the difficulties experienced by the pensions industry due to COVID-19:

- providing and communicating guidance to help employers, trustees and scheme members through the challenges of the pandemic
- responding to the challenges of COVID-19 by easing burdens on schemes, employers and providers and increasing engagement to provide support
- publishing new guidance for trustees and sponsoring employers of defined benefit (DB) schemes on what they need to consider when proposing to transfer to a superfund
- calling on trustees, administrators and providers to pledge to combat pension scams and meet anti-scam best practice
- publishing a policy on ending enforcement action more quickly if the targets of its action come up with an acceptable proposal and help scheme members achieve a good outcome without the need for legal proceedings
- launching a 15-year corporate strategy that puts actions behind the overarching theme of 'putting the saver at the heart of everything we do'
- the extradition of an alleged fraudster from Spain, securing a confiscation order to force charity boss Patrick McLarry to pay back over £280,000 to the scheme he stole from, and a £35 million settlement on our anti-avoidance case against the owners of bed manufacturer Silentnight.

TPR Chair Sarah Smart said: “This has been an extraordinarily tough year for everyone and I am immensely proud of how TPR has risen to the challenge. Our staff provided essential support to schemes and employers as they battled the impact of the pandemic, and have shown great resilience to plan for new responsibilities given to us under the Pension Schemes Act, push on with significant changes internally and launch a new strategy to protect savers. This strategy brings key priorities such as climate change and value for money sharply into focus.”

“TPR Chief Executive Charles Counsell, said: “In a year in which we have all been tested like never before, I am delighted that we continued to deliver successfully against our statutory objectives to protect savers and make workplace pensions work.

The Annual Report and Accounts can be accessed here.

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News in brief

TPR: Scheme Funding Analysis 2021

On 27 July, the Pensions Regulator issued the 2021 update to its annual funding statistics for UK defined benefit ("DB") schemes. The data is based on tranche 14 valuations (those with valuations between 22 September 2018 and 21 September 2019).

Of the 1660 valuations covered by tranche 14, almost a third were in surplus. Since the previous valuations of this cohort (tranche 11), asset growth has exceeded liability growth giving higher average funding positions. Average annual deficit reduction contributions (DRCs) increased by 8%, with average annual DRCs as a proportion of technical provisions remaining approximately unchanged. Recovery plans were extended, on average, by one year.

For schemes submitting both tranche 11 and 14 valuations, the median increase in asset values was 18% over the period and for liabilities an increase of 12%.

Schemes saw improved asset positions compared to tranche 11, due to the impact of sponsor contributions and positive gains on investments over the three year period. The growth in liabilities was attributable to lower inv return assumptions in turn driven by lower expectations for bond yields.

The update goes on to give further analysis focusing on funding strategies and valuation assumptions.

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