

Current Pensions Issues

TO DO LIST



This edition of Current Pensions Issues includes several actions for trustees. You can review the non-exhaustive checklist below with your advisers, following the links for background information:

- Issues following 'Brexit' vote:
 - review employer covenant and the value of contingent assets
 - consider impact on scheme funding level
 - consider whether transfer value reduction remains appropriate
 - consider whether and how to communicate with members

2016 Funding Statement: Consider The Pensions Regulator's (TPR) guidance, especially if an actuarial valuation in progress

- Protecting pensions from tax charges:
 - consider whether your staff are affected
 - participate in our research
- Defined contribution (DC) governance: review of DC provision (including Additional Voluntary Contribution arrangements (AVC)) against TPR's Code of Practice
- Notify the Pensions Protection Fund (PPF) by 1 September if scheme is potentially eligible for the Financial Assistance Scheme
- Obtain Legal Entity Identifier (LEI) Code if assets are managed under a segregated mandate

Brexit: the impact on pension schemes



On 23 June, the UK voted 52:48 in favour of the country exiting the European Union (EU).

In the weeks that followed, we have seen the resignation of the Prime Minister and the selection by the Conservative party of Theresa May as replacement. A heated and prolonged battle for leadership of the opposition is still underway. Furthermore:

- Ros Altmann resigned from her post as Minister of State for Pensions and was [replaced](#) by Richard Harrington in the role of Parliamentary Undersecretary of State at the Department for Work and Pensions (DWP)
- Equity markets dropped by around 4-5% in the days immediately following the referendum, but rebounded to recover most of these losses (in Sterling terms) by the end of July*
- Sterling fell in value, for example by 11% relative to the US dollar*
- Bond yields at longer durations fell by over 0.5% pa, potentially increasing pension scheme liabilities (where measured relative to bond yields) by more than 10 percent*

At the time of going to press, no date has been set for the triggering of Article 50 – the formal start of the process of the UK exiting the EU.

Some pension scheme members may have concerns about the impact of 'Brexit' on the security and funding of their pensions. Trustees may therefore wish to include a note about this in their next member communication in order to provide reassurance. For many pension schemes, a significant impact of Brexit will be the financial effect it has on sponsoring employers' business. Trustees should therefore consider whether and how companies' covenants might now change. We summarise the key impact for pension schemes on the following pages.

* Sources: FTSE All-Share Total Return Index – 23 June to 28 June and 29 July 2016
GBP/USD Exchange rate - 23 June to 25 June 2016
Gross Redemption yield on FTSE FI Over 15 Year Gilts - 23 June to 29 July 2016



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Brexit: the impact on pension schemes



Market volatility

The immediate impact of the EU referendum result, as far as pension schemes are concerned, has been in relation to investment markets. The impact on pension scheme funding will vary depending on the scheme's funding and investment strategies, whether there is any currency hedging in place, and the extent to which the assets and liabilities are mismatched.

Some schemes will see very little change in their funding level, while for others, the position at the end of June will look significantly worse than a few weeks before.

In the main, however, trustees should avoid being too concerned by short-term volatility and take a long-term view of funding. Where schemes are reducing transfer values, trustees may wish to review the level of reduction to ensure that members are being treated fairly, whether leaving the scheme or remaining in it.

TPR statement

Following the referendum, TPR issued a [statement](#) guiding pension trustees to:

- understand risks and opportunities of their employer's business and the industry sector they operate in;
- consider investment and funding volatility with their advisers, without being overly focused on short-term market movements;
- consider scenario-testing and review contingency plans, especially if a funding valuation is underway;
- monitor developments and be prepared to explain investment approaches to members with DC benefits; and
- remain vigilant to their schemes' circumstances, maintaining a focus on the longer term.

TPR also noted that it will continue to monitor the markets and other economic developments, and provide further guidance to trustees of defined benefit (DB) and DC schemes as required.

Funding issues

As part of an integrated approach to risk management (see [our spring 2016 newsletter](#)), TPR expects trustees to regularly review their employer covenant. Trustees should liaise with sponsors to consider whether there are any longer-term implications of Brexit on the company's financial outlook.

With gilt and corporate bond yields having fallen significantly in recent weeks, the value placed on many schemes' liabilities will have risen sharply and could remain volatile for some time. Scheme Funding valuations at dates in mid-2016 could therefore paint a materially worse picture than earlier in the year, and therefore early engagement with employers and advisers could help to avoid surprises.

The UK's exit from the EU is unlikely, however, to directly result in material changes to funding regulations in the immediate future.

IORP Directive

The agreed text of the revised [Institutions for Occupational Retirement Provision \(IORP\) Directive](#) has now been published. Final sign-off of the directive is expected in September 2016 and member states will have [two years](#) to transpose the Directive into national law.

It is likely that the UK will not have left the EU by 2018, and so will still be required to comply with the revised Directive. The details of implementation will be established by the government and TPR.

The UK may well leave the EU before it is required to enshrine these provisions in national law. However, depending on the exit negotiations, the UK may still be required to comply. As part of exit negotiations, the UK might also have to agree to implement any future changes to the pensions directive – without being able to influence its drafting. UK opposition was key to the 'Solvency II' funding proposals being dropped from the directive.

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UK votes Leave: how pension schemes can cope with uncertainty

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Key provisions from the recast IORP Directive

- Schemes will have to produce a risk assessment, including possible remedial actions and a qualitative assessment of the employer covenant
- Schemes will be required to produce a standardised pension benefit statement for members
- Deficits may occur in cross-border schemes, although the requirement to be fully-funded at all times remains
- No changes to funding requirements - in particular, solvency provisions will be off the table for the next review of the directive
- Collectively, those involved in running a pension scheme must be 'fit and proper'
- Schemes should disclose whether and how environmental, social and governance issues are addressed
- Schemes must aim to have an equitable spread of risks and benefits between generation
- Schemes with 15 members or fewer are exempt from the Directive. Schemes fewer than 100 members only need to comply with some basic governance requirements

Brexit: the impact on pension schemes



Pensions legislation / regulation

- **Accounting standards:** We do not expect Brexit to lead to changes in pension cost disclosures in company accounts – particularly as international convergence is considered desirable by standard-setting bodies. However, many employers will see balance sheet deficits increase significantly because of recent falls in corporate bond yields.
- **Financial services industry:** The UK's competitiveness in international markets could be threatened by the UK leaving the EU. Some providers could choose to move outside of the UK, or set up UK-based subsidiaries – in which case additional costs could feed through to annuity pricing.

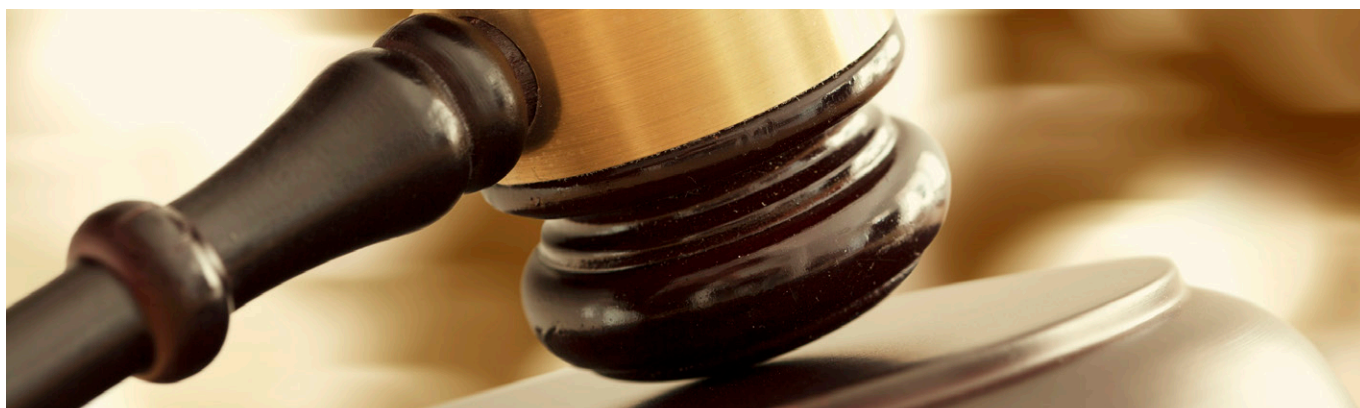
In practice, the financial services industry is likely to continue to comply with most EU regulation to facilitate continued participation in this significant market.

- **VAT:** As a result of Brexit, it has been argued that the UK could have more flexibility on charging and recovery of VAT on pension scheme costs. However, it remains to be seen whether HMRC will change its stance and, at the time of writing, we are still awaiting updated guidance originally promised for July.
 - **Equalisation of GMPs:** Brexit could potentially result in the requirement to equalise GMPs being dropped from the Government's agenda. Previous governments had maintained that schemes are required (under UK law) to equalise GMPs. It is not likely that the government would seek to reappraise equal treatment legislation already enshrined in UK law, such as equal normal retirement ages and gender-neutral annuity rates. However, it is possible that the issue of equalising GMPs may become less pressing – and the planned regulations could sit on the government's 'too difficult' pile for a while longer.
- Nevertheless, a legal challenge by the Lloyds Trade Union has now been launched in an attempt to clarify whether and how GMPs should be equalised.
- **Age discrimination:** There are unlikely to be material changes to age discrimination rules, although some aspects may be reviewed again in future years.
 - **Actuarial factors:** Again, Brexit is unlikely to have a direct impact on setting actuarial factors. Pension schemes that have gender-based factors should be able to continue.
 - **Transfer values:** Trustees should ensure that their basis for calculating transfer values remains reasonable, in particular following the recent falls in gilt yields. Where transfer values are reduced to reflect underfunding in the scheme, the level of reduction should be considered.
 - **PPF levies:** It is unlikely to be politically acceptable to reduce PPF compensation levels. Potentially, however, there may be upward pressure on PPF levies if insolvencies rise following Brexit.

The Court of Appeal has recently referred [a case](#) (related to the Turner & Newall Limited pension arrangements) to the High Court to consider whether PPF compensation is compatible with EU rules (in particular that some members' compensation may be less than 50% of their scheme benefits). Whether the Brexit decision might ultimately change the direction of this case remains to be seen.

An illustration on a teal background showing a person in a business suit climbing a tall stack of gold coins. An upward-pointing arrow is visible in the background, symbolizing growth or financial success.

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Brexit: has the result affected the bulk annuity market?
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Protecting pensions from tax charges

Following the reduction in the standard lifetime allowance (LTA) from £1.25 million to £1 million on 6 April 2016, HM Revenue & Customs (HMRC) has introduced two new LTA protection regimes:

- **Individual Protection 2016 (IP16)** – If pension savings were more than £1 million (HMRC value) on 5 April 2016, IP16 gives individuals a protected LTA, equal to the value of their pension savings at that date, up to a maximum of £1.25 million. Individuals with IP16 can continue to make pension savings, but savings above their protected LTA will be subject to a LTA charge.
- **Fixed Protection 2016 (FP16)** – FP16 enables individuals to retain a £1.25 million LTA, but they are not permitted to earn any further benefit from, or contribute to, any pension savings after 5 April 2016. For example, they need to have opted out of their pension scheme(s) on or before that date.

There is no specific cut-off date for IP16 or FP16 applications, which must be made via [HMRC's website](#). However, it is essential that individuals wishing to register for these protections do so before accessing any pension benefits.

HMRC is also [still accepting applications](#) for the existing Individual Protection 2014 (IP14) which was introduced on 6 April 2014 when the standard LTA was reduced from £1.5 million to £1.25 million. The deadline for IP14 applications is 5 April 2017.

For further information, please contact our [Executive Pensions team](#).

British Steel Pension Scheme

The Department for Work and Pensions (DWP) has been [consulting](#) on options for intervening in the British Steel Pension Scheme (BSPS). Tata Steel UK, the BSPS's sponsoring employer, is being sold by its parent company and the scheme's large deficit has proved an obstacle to it being sold as a going concern.

The DWP is considering four key options:

- Using existing rules to implement a [Regulated Apportionment Arrangement](#) (RAA), separating the BSPS from Tata Steel UK, with the company having no further liability. The scheme would then enter the PPF or, if well enough funded, benefits above PPF compensation would be secured outside of the scheme.
- Tata Steel UK could end their relationship with the BSPS, triggering a debt on Tata, who would then work with the BSPS trustees and TPR to secure member benefits at above PPF compensation levels but below full benefits. Tata have indicated, however, that this option would be unaffordable.
- The BSPS trustees could amend scheme rules, cutting pension increases to the minimum required by law. This would require government legislation specifically for the BSPS as it would be a detriment to members' benefits – and the first time such a rule amendment did not need informed member consent.
- The BSPS trustees could transfer the scheme liabilities to a new arrangement offering reduced revaluation and pension increases, but with benefits above the level of PPF compensation. The Government would also need to legislate to allow this, as the trustees would be unable to obtain consent to the change from every member of the BSPS.



SURVEY: Are your staff affected by the tapered annual allowance?

In the light of recent further changes to pensions taxation, our clients are interested to find out how other companies are managing the impact on staff affected by the tapered Annual Allowance.

We have compiled a [short survey](#) in order to gain some insight into the varying approaches employers are taking, both by size of the Company and type of pension scheme. The results will provide a valuable overview of how businesses are managing this change for their high earners. We welcome and value your opinion, and would be grateful if you could complete this short survey which will take no more than five minutes. We will share a summary of the results in a future Current Pensions Issues and we will send a full report to all those that take part.

[TAKE THE SURVEY >](#)

TPR update

2016 funding statement

TPR has issued its 2016 funding statement for trustees of DB schemes, intended as a guide for schemes undertaking a valuation with an effective date between 22 September 2015 and 21 September 2016. The funding statement was issued before TPR's Brexit follow-up (see above).

The [2016 funding statement](#) emphasises the importance of [Integrated Risk Management](#) (IRM), and how trustees 'should take a proportionate approach to understanding the scheme's exposure to risk across covenant, investment and funding.' Based on [their analysis](#), TPR concluded that:

- In light of recent 'significant financial market volatility' trustees must take a long-term view of investments, as well as understanding the impact on assets and liabilities of changing market conditions
- TPR expects many funding strategies to be based on lower expected investment returns than at the last valuation, and encourages trustees to 'reconsider their assumptions in light

of market developments' if they had previously assumed gilt yields would revert to higher levels. Such a review should consider whether it would be more appropriate to assume reversion 'over a longer time period and to lower levels than before', and whether it would be appropriate to implement any related contingency plans put in place at the last valuation

- TPR expects 'most schemes' will find themselves with a larger deficit than previously expected. Such schemes are encouraged to seek higher contributions where there is sufficient affordability for the sponsor. Where higher contributions may not be affordable, TPR expects trustees and employers to discuss the issue openly and to consider their options

- Trustees who seek to adjust assumptions in light of 'pensions freedoms' should ensure these are evidence-based. TPR says that most schemes, however, will not yet be expected to have enough evidence to support such adjustments.
- TPR is comfortable with trustees using the updated (2015) version of the Continuous Mortality Investigation's model of future longevity improvements, even though it results in lower life expectancies at many ages than the 2014 model. However, TPR advises that trustees should understand the funding implications if it transpires this reduction in life expectancies is temporary and not the start of a longer-term trend.

DC code of practice

Following an earlier consultation (see [Current Pensions Issues Spring 2016](#)), TPR's revised code of practice for trust-based DC schemes is now in force. Using an 'educate and enable' approach, TPR hopes to drive up standards for DC scheme governance.

Based on responses to the consultation, TPR made a number of minor changes to the code, including renaming the code to make it clear that it applies to all trust-based schemes which offer DC benefits.

TPR has also issued a range of 'how to' guides designed to help trustees implement the new DC code and, using best-practice examples, explain how trustees can demonstrate compliance with the law.

For more information about how our Workplace Health and Wealth team can perform a value-for-money (VFM) assessment of your DC scheme, please see our [website](#).

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Everything you need to know about TPR's updated DC Code

[READ MORE >](#)

Scheme funding statistics

TPR has published its [analysis of valuations](#) with effective dates from 22 September 2013 to 21 September 2014. This summarises the recovery plans submitted to TPR and the assumptions underlying those valuations.

The analysis highlighted that the mean recovery plan period was eight years and that just over one third of schemes had extended their recovery period by more than three years between valuations.

21st Century Trusteeship

TPR has published a [discussion paper](#) on '21st Century Trusteeship and Governance', and is consulting on the contents. The regulator researched and engaged with a number of trustee boards about governance in advance of publishing the paper, which focuses on:

- encouraging diversity of backgrounds, skills and experience in lay trustee boards;
- recognising increased 'professionalisation' of trustees and the lack of minimum standards for professional trustees;
- recognising the important work of chairs of trustees in upholding governance standards;
- ensuring the appropriate standards of trustee knowledge and understanding are being met;

- helping trustees manage conflicts of interest, especially regarding their sponsoring employers;
- increasing trustee engagement with key governance activities; and
- improving governance for small schemes with limited resources.

The paper suggests TPR may be exploring a formal professional training and development framework for trustees.

TPR has asked whether more could be done to help trustees engage effectively with administration and investment governance. TPR also asks whether governance of third party providers and advisers is being carried out to an appropriate level.

Work and Pensions Committee inquiries: BHS, TPR and the PPF

The Work and Pensions Select Committee and the Business, Innovation and Skills Committee have published their [report](#) on the role of the pension scheme in the collapse of BHS.

The report criticised the actions of the previous and new owners of the BHS business, and to a lesser extent TPR (for example, for agreeing to a 23-year scheme funding recovery plan).

Following the initial inquiry, the committee has [now launched](#) a further investigation and is inviting submissions (by 23 September 2016) on a wider range of DB funding issues, including:

- The adequacy of DB pension scheme regulation, including TPR's powers in relation to 'anti-avoidance' and the 'clearance' system, specifically focussing on complex and multi-national companies
- Whether TPR's regulatory approach has an impact on company behaviour or 'incentivises moral hazard'. The inquiry will investigate resourcing and prioritisation of TPR's supervisory work
- Regulatory powers in relation to scheme funding recovery plans
- Whether the PPF is sustainable, and whether the PPF levy system is fair for employers and members
- The powers of pension scheme trustees and relationships between TPR, PPF, trustees and employers

The inquiry will also consider whether the current environment warrants an exceptional approach, and whether the current regulatory framework is resulting in fair inter-generational outcomes.



News in brief

HMRC: LTA survey

HMRC is collating feedback on the new pension lifetime allowance online service, from both [pension scheme administrators](#) and [scheme members](#). Feedback will help HMRC to 'build the best possible service'.

The survey was originally open only until end May but has since been extended.

Those completing the survey can opt-in to participate in further research.



Creating a secondary annuity market

Three consultations, all now closed, set out further detail ahead of the start of a secondary market for pension annuities in 2017 (see [Current Pensions Issues Spring 2016](#)).

The first by HMRC, sets out how tax rules will be amended so that individuals will be able to take the proceeds of annuity sale as a cash lump sum, have them paid into a flexi-access drawdown fund or purchase a flexible annuity policy (an annuity where regular payments may increase or decrease).

HM Treasury's consultation is on draft legislation to help regulate firms or individuals acting as the buyer or intermediary of a secondary annuity. Only buyers authorised by the Financial Conduct Authority (FCA) will be able to participate in the market

The Financial Conduct Authority is consulting on changes to its Handbook which will set out rules for conducting sales of annuity income. The rules will make sure individuals have the information they need and adequate protection when selling their annuities

Inquiry into Lifetime ISA

The Work and Pensions Committee has [re-opened its inquiry](#) into auto-enrolment amidst fears that opt-out rates could be influenced by the introduction of the [Lifetime ISA](#) (LISA).

The LISA is due to be launched in April 2017 and will reward savers under age 40 with a 25% government bonus on savings of up to £4,000 each year. LISA savings may be used to buy a first home or to fund retirement from age 60. The government bonus may be lost if drawn earlier, or used for other purposes.



BLOG Has Osborne given saving a new LISA life?

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Financial Assistance Scheme to close

The PPF is to [close the Financial Assistance Scheme \(FAS\)](#) to new applications from 1 September 2016. Eligible schemes which have not yet notified the PPF should do so as soon as possible. The closure will not affect members currently receiving compensation or those with a deferred entitlement in the scheme.

The FAS was established to offer help to members who have lost out on their pension because they were a member of an under-funded DB scheme that started to wind-up and/or the employer went insolvent between 1 January 1997 and 5 April 2005.

PPF: common misconceptions

The PPF has published a [short document](#) intending to correct several 'common misconceptions about the PPF'. The document is intended for use by journalists and others in the media, but may be of interest to those dealing with the PPF for the first time.

LEI codes

TPR [has asked](#) all UK occupational pension schemes with two or more members to obtain a Legal Entity Identifier (LEI) code by 30 June 2016. The LEI code is a legal requirement for schemes with segregated investment mandates including derivatives.

DB to DC transfers: FRC review

The Financial Reporting Council (FRC) has published the results of a [review of transfers](#) from DB to DC schemes, which show that since the introduction of the pension freedoms there has been a small increase in the number of DB to DC transfers being processed (although numbers remain low overall).

The FRC found many trustees reluctant to actively promote transfers and the review suggests the value members place on their benefits may explain the low take-up of transfer options.

FCA: Retirement Outcomes Review

The FCA has published [Terms of Reference](#) for its Retirement Outcomes Review (ROR), a follow-up to the [Retirement Income Market Study \(RIMS\)](#), which will assess how competition is developing in the retirement income market following the changes that were introduced in April 2016. Results of the review will be published in the summer of 2017.

Alongside this, the FCA issued an [update](#) on their work regarding pensions and retirement income, including results of their recent review into how FCA-regulated firms are signposting the availability of [Pension Wise](#).

Following the RIMS, the FCA published [research](#) into the implementation of an 'annuity comparator' tool, concluding that a comparator could increase the proportions of members 'shopping around' from 13% to 40%.



As one of the UK's largest independent providers of actuarial, administration and consultancy services, Barnett Waddingham offers:

- Advice relating to DC pension schemes – trust, master trust and contract
- Scheme Actuary and associated services to DB pension schemes – in the Public and Private Sectors
- Accounting for UK and international companies
- Consultancy and administration services to companies on all wellbeing policies
- Consultancy to the Higher Education sector, across a top-tier client list spanning the UK
- Business insights through practical, risk-based solutions
- Administration services including pensioner payroll, preparation of annual accounts, secretarial services and administration consultancy
- Investment strategy reviews and advice on investment managers
- Employer support regarding insurance arrangements (group life insurance and PHI)
- Employer support in relation to pension arrangements for senior executives
- Guidance for senior executives regarding retirement options
- Analysis and modelling of mortality and longevity risk for insurance companies, reinsurance companies, investment banks and pension schemes.

Barnett Waddingham is also a leader in the provision of self-invested personal pensions, small self-administered pension schemes and other retirement arrangements.

Forthcoming events

DC Training

London, 7 September 2016 [REGISTER >](#)

DC trustees are legally required to have a minimum standard of knowledge and understanding. Our course in London is aimed at both trustees of DC schemes and those involved with the governance and management of DC schemes.

Trustee Training

London, 8 September 2016 [REGISTER >](#)

Barnett Waddingham's one day course in London is designed to give trustees a thorough grounding in pensions matters and the confidence to complete The Pensions Regulator's trustee toolkit.

Please contact us for further information.

DC Conference

London, 6 October 2016 [REGISTER >](#)

Barnett Waddingham's third DC conference will take place in the iconic surroundings of [London's Barbican](#) and, this year; will provide a unique opportunity for delegates to explore complex issues through the structure, flow and creativity of music.

Investment Conference

Birmingham, 12 January 2017 [REGISTER >](#)

London, 26 January 2017 [REGISTER >](#)

We are delighted to announce the dates and locations of our 2017 Investment Conferences. These conferences – at the [Belfry](#) in Birmingham (12 January 2017) and [Etc Venues, Bishopsgate](#) in London (26 January 2017) - will provide delegates with the opportunity to hear from industry experts and stay up to date with key issues in an ever-evolving industry.

Further information

You may also find the following Barnett Waddingham briefing notes and blog posts interesting:

Blogs

[The evolving role of the pension management consultant](#)

[Pension freedoms – a potential trigger for mass financial mis-selling?](#)

[Changes to widows' pension rights - not just a 'Thai Bride' problem](#)

[Walk the line: between GMP rectification and benefit audit](#)

Briefings and research

[FTSE350 report - impact of pension schemes on UK business](#)

[Current Issues in Pensions Financial Reporting - June 2016](#)

[Buy-outs and buy-ins – Summer 2016](#)

Webinars

Barnett Waddingham hosts a number of online seminars throughout the year. Recordings of previous webinars (including one on the impact of the pensions flexibilities on DB schemes) are available on our BrightTalk channel, along with details of upcoming live events.

[VIEW OUR WEBINARS >](#)



This newsletter is intended as a summary of recent pensions-related events. Whilst we have taken care to ensure all information is correct at the time of going to press, the content of this newsletter should not be relied on as advice to act, or refrain from acting, in relation to any of the subjects contained herein. Before taking any such action (or deciding not to act) you should seek appropriate professional advice.

Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail.

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