Barnett Waddingham
a true partnership approach

News on Pensions

JULY/AUGUST 2016

Work and Pensions Committee – new inquiry

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 The Pensions Regulator (TPR) - for example for agreeing to a 23-year scheme funding recovery plan.

The committee has now launched another inquiry to follow-up the first, and is inviting submissions on a wider range of defined benefit (DB) funding issues, which include:

- regulatory powers in relation to scheme funding recovery plans
- the adequacy of other DB pension scheme regulation, including TPR's powers in relation to 'anti-avoidance'
- the 'clearance' system in relation to corporate activity, 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
- whether the Pension Protection Fund (PPF) is sustainable, and the 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 economic environment warrants an exceptional approach, and whether the existing regulatory framework is resulting in fair inter-generational outcomes. Responses should be sent to the Work and Pensions Committee by 23 September 2016.

Latest from The Pensions Regulator

21st Century Trusteeship and Governance

TPR has launched a consultation on '21st Century Trusteeship and Governance' which runs until 9 September 2016. TPR is intending to use the feedback received to "better support trustees through a more targeted communication and education strategy".

In advance of publishing the paper, TPR researched and engaged with a number of trustee boards about governance, and the key themes from their research are reflected in the paper, focussing on:

- how TPR can encourage diversity of backgrounds, skills and experience in lay trustee boards
- what can be done to recognise the increased 'professionalisation' of trustees, and whether the lack of a recognised 'minimum standard' for professional trustees is an issue
- recognising the important work of chairs of trustees in supporting other trustees and upholding governance standards
- ensuring the appropriate standards of trustee knowledge and understanding (TKU) are being met
- what assistance TPR can give trustees to help them manage conflicts of interest, especially regarding their sponsoring employers
- increasing trustee engagement with 'key governance activities' such as regular formal trustee meetings and holding third-party advisors to account
- how governance for small schemes with limited resources can be improved

TPR hints that it may be looking at introducing stricter knowledge and understanding requirements for both professional and lay trustees, and is exploring the possibility of a CPD framework.

Other discussion questions focus on whether more could be done to help trustees engage effectively with administration and investment governance, as well as whether governance of third party providers and advisers is carried out to an appropriate level.

TPR is also seeking views on how it can deal with small schemes that are unwilling or unable to deliver good governance and member outcomes.

Scheme funding statistics

TPR has published the 2016 edition of its annual funding statistics for DB and hybrid schemes. The analysis is based on scheme funding valuations with effective dates between 22 September 2013 and 21 September 2014 (Tranche 9).

TPR's analysis shows that these schemes had an average funding level of 89% on their scheme funding basis - compared with 88% at their last scheme funding valuation (usually three years ago).

The assets of Tranche 9 schemes have grown over the three-year period due to strong investment returns and deficit reduction contributions having been paid by employers. The value of the liabilities has also increased by a similar amount during that period – in part due to lower expectations of future investment returns (a consequence of falling government bond yields).

Other findings set out in the report include:

- the average Recovery Plan length for Tranche 9 schemes has increased slightly to eight years (Tranche 6: 7.8 years) with just over one third of schemes extending their recovery plan by more than three years
- the average (median) increase in annual deficit contributions was 7.4%
- 19% of schemes used some kind of contingent asset to support the funding of the scheme
- the median assumed life expectancy at 65 was 87.7/89.9 years for males/females currently aged 65, very similar to three years before

DC Code of Practice

TPR has overhauled its defined contribution (DC) Code of Practice (Number 13) – publishing the final version on 28 July 2016.

Changes from the previous version of the Code reflect:

- clearer language, setting out the link between legal requirements and TPR's expectations
- recent legislative changes in relation to governance standards, charge controls and pension freedoms
- the six updated key DC principles – with separate guides produced for each
- an updated assessment framework – which was previously based on TPR's 31 'quality features'

The Code sets out the standards of conduct and practice that TPR expects trustees to meet in providing DC benefits.

TPR expects trustees to use the DC Code to check the quality of any DC pension arrangements they operate on an ongoing basis – taking a 'proportionate' stance regarding Additional Voluntary Contribution (AVC) benefits provided in DB schemes for example.

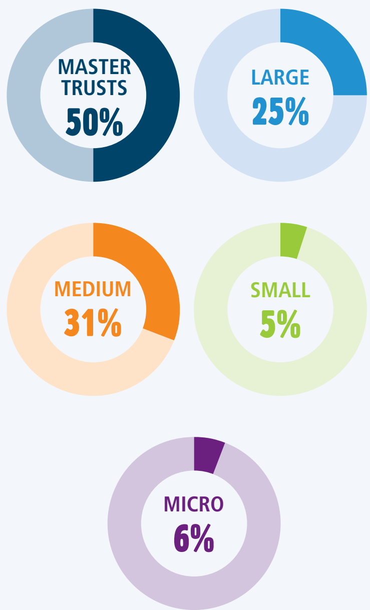
In view of the substantial changes to the Code, trustees may wish to bring forward the next quality review of their DC arrangements.

Meanwhile, research by TPR shows that larger DC schemes consistently out-perform small schemes on all aspects of governance and administration.

The research shows a strong correlation between scheme size and the number of standards being met. Half of master trusts met at least three quarters of the standards set by TPR, compared to 25% of large, 31% of medium, 5% of small and 6% of micro DC schemes.

TPR is urging pension trustees to focus on driving up standards of governance and administration in their schemes, in order to increase the likelihood that members receive a good outcome from their retirement savings.

Proportion of schemes complying with at least 75% of the governance standards



source: OMB research

Halcrow

A deal has been agreed between TPR and the engineering consultancy Halcrow in order to keep its pension scheme out of the PPF and avoid the firm's insolvency.

Members will be offered the option to transfer to a new scheme with reduced benefits. The new scheme will receive an £80 million contribution, which is more than the existing scheme would have received on insolvency. An equity stake of between 25% and 45% in the employer will be split between the new scheme and the PPF, depending on the number of members who choose to transfer.

The Halcrow Pensioners' Association launched a legal challenge to the deal, which has since been withdrawn.

2015/16 annual report

TPR reports that it is performing well in its key areas of responsibility despite the pace of change in the pensions sector, and says it has met or narrowly missed the majority of its performance goals, but has fallen short on more challenging targets for integrated risk management and sustainable growth of employers.

Prosecution policy

TPR has publically set out its prosecution policy, detailing how it will use its powers in the case of criminal offences connected with workplace pensions. In the document TPR states that:

- it will apply a risk-based approach to prosecution decisions;
- when prosecuting, TPR puts considerable weight on the public interest; and
- for cases that are not serious enough to prosecute they may refer it to the police, recommending they issue a formal caution.

EU referendum: 'Brexit'

The referendum on the UK's continued membership of the European Union resulted in a win for the 'leave' campaign, and caused considerable volatility in investment markets.

The long-term impact of leaving the EU - for pension schemes and for the wider economy - is still very much an unknown and will depend on the negotiated terms of the UK's exit. Pension scheme trustees may want to pay particular attention to concerned about the expected longer-term effect on sponsoring employers' businesses.

Changes to pensions legislation, if they happen at all, are more likely to be realised in the medium to long term. In the meantime, there are a number of pensions-related matters which could be affected by the referendum result, which trustees may wish to monitor closely.

Our 'Brexit-special' edition of Current Pensions Issues (Summer 2016) considers these actions in more detail, including:

- trustees will need to consider how changes in **employer covenant** will affect the security of members' benefits and the funding plans already in place
- pension scheme **funding levels** are likely to have reduced in many cases when measured in the period immediately after the referendum and are expected to be more volatile in the near future
- members may be concerned about the implications of Brexit on the security and funding of their pensions. Trustees may want to consider a **communication to members**
- it will be important to keep **transfer value** assumptions under review given recent falls in gilt yields

You may also wish to read more on this subject in our blog post: UK votes Leave: how pension schemes can cope with uncertainty.

PPF news

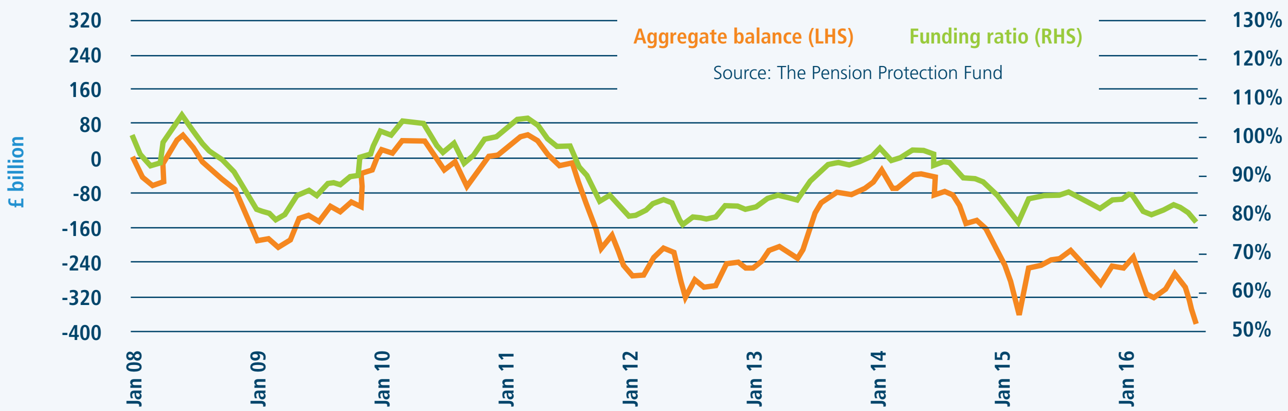
2016 accounts

The PPF has reported a surplus of £4.1 billion in its 2016 accounts. Based on the position at the accounting date, which was before the EU referendum, the likelihood of the PPF meeting its goal of being self-sufficient by 2030 had increased to 93%.

PPF 7800 Index

The latest update of the PPF 7800 Index of schemes' funding (on the s179 basis) shows there was a fall in the s179 funding ratio from 81.5% to 78.0% between May and June 2016. The aggregate deficit of the 5,945 schemes in the index is estimated to have increased over the month by £89 billion.

ESTIMATED AGGREGATED BALANCE (ASSETS LESS S179 LIABILITIES) AND FUNDING RATIO OF SCHEMES IN THE PPF UNIVERSE



IORP Directive

The European Insurance and Occupational Pensions Authority (EIOPA) has published the text of the revised Institutions for Occupational Retirement Provision (IORP) Directive. Final sign-off is expected in September, 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 then, and so will be required to comply with the revised directive (although it is always possible that the UK might repeal the provisions at a later date).

The directive is not expected to be onerous for the UK, and the details of implementation will be decided by the government working with TPR.

- Schemes will be required to produce a risk assessment and disclose this to regulators. The risks themselves are largely covered by TPR's integrated risk management framework and, as such, this risk assessment would not be expected to be an additional burden on schemes.
- The requirement for individual trustees to be 'fit' has been relaxed, and is now to be applied to trustees collectively.
- Annual benefit statement requirements set out in the directive now allow for differences between DB and DC schemes. Some required information (e.g. benefit projections, the funding level of the scheme) is already included in other regularly-issued documents (for example statutory money purchase illustrations or summary funding statements).

As reported in the News on Pensions May 2016 the directive does not include changes to pension scheme funding requirements.

Further information

You may find the following recent blog posts and information sheets interesting:

- What does Brexit mean for UK pensions?
- Open for business: HMRC's online registration for Fixed and Individual Protection
- Everything you need to know about TPR's updated DC Code
- The real impact of pension schemes on UK business
- Evidence-based funding assumptions: TPR's 2016 annual funding statement
- The evolving role of the pension management consultant

Forthcoming Events

Webinars

You can view Barnett Waddingham's back catalogue of webinar recordings on our BrightTALK channel, including:

- How to survive the EU referendum (recorded 19 May 2016);
- Pension flexibilities, the impact on DB schemes (26 April 2016); and
- Pension Tax changes from April 2016 (23 February 2016)

Chair of Trustee forums

Our forums are aimed at Chair of Trustees to provide an informal opportunity to network with peers and enter into open, lively debate on current hot topics.

- Royal Automobile Club, London – 6 September 2016
- Marco Pierre White Steakhouse, Birmingham – 8 September 2016

Save the dates

You may wish to add the following Barnett Waddingham events to your calendar for 2016/17. Further details can be found on our website.

- DC Conference 2016: The Barbican, London – 6 October 2016
- Investment Conference 2017: The Belfry, Birmingham – 12 January 2017
Etc Venues, Bishopsgate, London – 26 January 2017
- Annual Pensions Conference 2017: Etc Venues, Bishopsgate, London – 28 March 2017

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

info@barnett-waddingham.co.uk
0207 776 2200
www.barnett-waddingham.co.uk