Essential UK Pensions News

November 2021

Introduction

Essential UK Pensions News covers the key pensions developments each month.

A stronger Pensions Regulator

Revised code of practice on contribution notices clarifies tests relevant to dividends

The Pensions Regulator's revised Code of Practice 12 came into force on November 25, 2021. This sets out the circumstances in which the Regulator expects to issue a contribution notice where it believes that the "material detriment" test, the "employer insolvency" test or the "employer resources" test has been met.

Interestingly, the finalised Code states that only the "material detriment" or "employer insolvency" tests would be relevant to dividend payments. The consultation draft had suggested that the "employer resources" test could also be a trigger and this previously seemed the more natural route for the Regulator to take if minded to consider a contribution notice in relation to a dividend.

This revision is helpful in that companies considering dividend payments can now focus their analysis on the two tests called out in the Code.

Governance

Top-up payments to be introduced for net pay arrangements

The main point of interest for the pensions industry in the Chancellor's autumn budget was that low earners saving in pension schemes using a net pay arrangement will receive top-up payments in respect of contributions made from 2024-25 onwards.

This is the Government's response to a known disparity of tax treatment between employees saving in a pension scheme using a net pay arrangement and those saving in a scheme using relief at source. The changes won't come in for another three years which is unlikely to satisfy those low paid individuals who have lost out in the past.

DC charges: decision on flat fees but more to come on charge caps

The Department for Work and Pensions (DWP) has decided to press ahead with a ban on charging flat fees on DC pots worth £100 or less held within a default arrangement. This restriction will come into force from April 2022.

It appears to have parked for now a decision on moving to a "universal charging structure" for default funds, noting that a majority who responded to the consultation were against this.

Separately the Chancellor committed in the autumn budget to consulting on further changes to the charge cap for DC schemes. The aim is to ensure that the cap can better accommodate well-designed performance fees to ensure savers can benefit from higher return investments, while unlocking institutional investment to support some of the UK's most innovative businesses. The Government will continue wider policy work to understand and remove various barriers to illiquid investment.

The Government is determined to get DC schemes investing in long-term projects where the returns will be slow and the performance fees high. It recently finalised the framework for a "Long Term Asset Fund" for this purpose. We may now see more innovation in illiquid fund packaging for the DC market but the reality is that long-term projects and erratic, high performance fees don't fit well with a pension model requiring instant valuations and instant access.

Unexpected change to rules for rise in normal minimum pension age

The normal minimum pension age is set to rise from 55 to 57 from April 2028. Members of pension schemes which give them an unconditional right to draw their benefits from age 55 will have that right preserved as a "protected pension age".

As reported in our July edition of Essential UK Pensions News, the Government had originally proposed having a "joining window" until April 2023, to give members a chance to transfer their benefits to a scheme that would give them a protected pension age.

However, following concerns that fraudsters could use this opportunity to pressure members into transferring unwisely, the Treasury unexpectedly announced on November 4, 2021 that it had decided to close the joining window with effect from 23.59 the previous day – before that window was even formally confirmed to exist. Members who had already requested a transfer before that time will still be able to get their protected pension age but anyone who had not has missed their chance. This U-turn was deliberately not publicised in advance so as to avoid a rush of last-minute transfers.

Trustees should work out whether their scheme will give members a protected pension age and consider updating transfer communications to make clear that members cannot change things by taking a transfer.

For more information and suggested action points, please see our recent article for *Pensions Expert* and our blogpost.

Transfers and scams

New trustee duties to block pension scams

The DWP has finalised its new rules about statutory pensions transfers which will give trustees significantly greater scope to say no to a member request to transfer their pension to another scheme. This is intended to help protect members from scams.

The revised regulations, which have been significantly updated since the version that was consulted on in the summer, will apply to any statutory transfers which are initiated from November 30, 2021, onwards.

Under the new regime, trustees will only be able to agree to a transfer if it is either to a "safe" type of scheme (namely a public sector scheme, an authorised master trust or an authorised collective money purchase scheme) or if they are satisfied the transfer does not show certain warning signs of a scam. They will have to refuse transfers showing any "red flags" (the clearest signs of a scam). If they spot amber flags (possible scam indicators) members can still choose to transfer but not until they have taken scams guidance from MoneyHelper.

There is no grace period for trustees and administrators to get up to speed, so the pressure is on to get to grips with the new rules and adapt schemes' transfer processes. The Pensions Regulator has published some guidance to help with this.

For further information, please see our recent briefing.

Investment

Members sue pension scheme trustees over ESG issues

Members of the Universities Superannuation Scheme (USS) have brought a claim in the High Court against the scheme's trustee and trustee directors. Amongst other things, the claimants allege that a failure by the trustee directors to divest from fossil fuels has caused, and will continue to cause, significant financial detriment to the scheme beneficiaries.

Trustees typically have a wide discretion over investment matters but it will be interesting to see how this case develops and whether it will encourage other members to bring claims in relation to ESG issues.

Pensions Regulator disappointed with engagement on climate change

The Pensions Regulator has warned that UK pension schemes "still have much work to do" to adapt to the challenges of climate change. It commissioned surveys of schemes last year to assess the level of engagement with climate change and has published the results in a climate adaptation report. The results showed that in 2020:

- only 43% of DC schemes took account of climate change in their investment strategies; and

- 51% of DB schemes had not allocated time or resources to assessing any risks and opportunities associated with climate change

This new report is part of a UK-wide "adaptation" programme where government and public sector organisations explain what they will be doing to be ready for the challenges of climate change. The Regulator recognises the "scale of the challenge" and that there is a lack of data, but notes that "practices are rapidly evolving" and data should improve as the financial system as a whole moves to mandatory climate reporting requirements.

According to the Regulator, trustees should:

- be considering climate change in their scheme's investment strategies;
- allocate sufficient time and resources to assessing climate-related risks and opportunities; and
- ensure processes used to manage those risks and opportunities are robust.

This message is not just for the largest schemes or those already legally obliged to undertake climate-related governance and reporting. As the Regulator comes under pressure to demonstrate progress, it may start to push smaller schemes to comply voluntarily. Smaller schemes may want to factor this into their planning.

The report also recommends that trustees sign up to the 2020 UK Stewardship Code. It notes that only 9% of schemes have so far done so.

Climate change reporting to be extended to UK's largest companies

The Department for Business, Energy, and Industrial Strategy (BEIS) has confirmed that the largest UK-registered companies and financial institutions will have to report on climate-related risks and opportunities, in line with recommendations from the Task Force on Climate-Related Financial Disclosures (TCFD).

This will come into force from April 6, 2022 and will include many of the UK's largest traded companies, banks and insurers, as well as private companies with over 500 employees and £500 million in turnover. (For more information on these requirements, please see our briefing.)

This is the latest step in the Government's roadmap to make TCFD-aligned disclosures mandatory across the economy by 2025. UK premium-listed companies and the largest occupational pension schemes and master trusts are already required to comply. Requirements for asset managers, life insurers, FCA-regulated pension providers and issuers of standard listed shares are expected to take effect early next year.

These additional disclosures may further help pension schemes with their own climate-related reporting as it should lead to improvements in the infrastructure around TCFD reporting and make TCFD-compliant data more accessible.

Proposed new requirements for stewardship and implementation statements

The DWP is consulting on draft guidance designed to improve scheme voting and engagement. It mostly focusses on points that need to be covered in the scheme's implementation statement and these parts take the form of statutory guidance, meaning they will be mandatory.

The guidance increases the level of detail that is required for implementation statements. If the guidance comes into force in its current form, we expect most schemes will have to update their statements significantly in the future and will need to request more information from their asset managers. Some may find they have to enhance their engagement and voting practices.

For example, when reporting on voting behaviour, trustees will need to include details such as:

- relevant statistics on voting behaviour;
- a rationale for some or all voting decisions and how this links to the scheme's stewardship priorities, and
- where someone exercises votes on behalf of the trustees, whether that person has agreed to follow the trustees' voting policy.

In addition, trustees will need to explain in their implementation statement how their stewardship activities are in scheme members' best interests.

The consultation closes on January 6, 2022 so we expect the new guidance will come into force next year.

FCA confirms rates for legacy use of synthetic LIBOR rates

The FCA has confirmed that it will allow the temporary use of 'synthetic' sterling and yen LIBOR rates in all legacy LIBOR contracts, other than cleared derivatives, that have not been changed by the end of 2021.

The FCA notes that many contracts that use or previously used LIBOR have already been switched to new risk-free overnight interest rate benchmarks or will do so at the end of 2021. However, it also acknowledges that there is a risk of disruption to markets if interest payments in contracts that have not switched by the end of 2021 cannot be calculated. The FCA is therefore requiring the publication of 1-, 3-, and 6-month LIBOR rates for sterling and Japanese yen on a synthetic basis until the end of 2022, to allow more time for impacted firms to complete a smooth transition.

Schemes should discuss the impact of this development, for example on hedging, de-risking triggers and investment agreements, with their investment advisers.

For more information on the new benchmarks, please see our financial services blogpost.

GMP Equalisation

New Bill seeks to clarify GMP conversion rules

Margaret Ferrier MP's private member's Bill on GMP conversion has been published. The Pension Schemes (Conversion of Guaranteed Minimum Pensions) Bill would amend existing laws governing GMP conversion with the aim of making conversion easier by addressing known technical issues.

The proposals include:

- allowing regulations to set out minimum requirements for post-conversion survivors' benefits;
- clarifying employer consent requirements; and
- removing the need to notify HMRC.

The DWP appears to be supporting the Bill which makes it more likely to succeed than most private member's Bills.

This development will be welcomed by the many schemes interested in taking the conversion route to GMP equalisation.

Restructuring

Fraud Compensation Fund levy set to rise

The DWP is consulting about increasing the ceiling for the levy which funds the Fraud Compensation Fund managed by the PPF.

This is not unexpected in the wake of a High Court decision *(The Board of the PPF v Dalriada Trustees Ltd)*, which has enabled victims of some pension liberation scams to recoup their losses from the Fraud Compensation Fund. For now the DWP has agreed to make a loan of approximately £250M over the period 2021-2025 to the Fraud Compensation fund to cover the expected further claims.

The DWP proposes that the ceiling for the levy would more than double, rising from 30p to 65p for master trusts and from 75p to £1.80 per member for all other occupational pension schemes.

Schemes can expect their Fraud Compensation Fund levy to rise in the future. The actual amount of the rise has not yet been confirmed.

Industry trends

Controversy over state pension triple lock

The House of Lords took issue with the Government's plan to suspend for one year the earnings element of the state pension triple lock, proposing that earnings growth should be adjusted for the impact of the pandemic rather than disregarded. As expected, the House of Commons has rejected this proposed amendment but this episode has reignited the debate about adequacy of state pensions and intergenerational fairness.

Pensions issues in the pipeline

Development	Expected timing	Suggested action*
Requirement for trustees of smaller DC schemes (assets of less than £100m) annually to assess the value provided to their members and, where they conclude value not provided, to consider winding up	From October 1, 2021 (for scheme years ending after December 31, 2021)	Trustees to consider whether their DC scheme is in scope for the new requirements. Prepare for value assessment (if relevant) and for reporting in chair's statement and scheme return to the Pensions Regulator. If value assessment unlikely to be met, consider options for DC members.
Trustees of all DC schemes to report on net investment returns in the chair's statement	From October 1, 2021 (for scheme years ending after October 1, 2021)	Gather relevant information and prepare for reporting.
Statutory transfers: additional requirements November 30, 2021	November 30, 2021	Identify which transfers fall under the new rules. Review and update transfer processes and communications.
PPF 2022 / 23 Levy	December 2021	Keep an eye out for the final rules following the closure of the consultation on November 9, 2021 and consider the impact of any change in the levy.
Climate change risk governance and disclosure requirements start to apply for: • Asset managers, life insurers, FCA-regulated pension schemes. • Standard listed companies.	From January 1, 2022 Consultations published June 22, 2021; final rules expected Q4 2021.	For noting only. Information from asset managers and investee companies may become more readily available which would help trustees with their own disclosures.
Compliance report for Competition and Markets Authority (CMA) regarding objective-setting for investment consultants and tendering of fiduciary manager appointments	January 7, 2022	Prepare the necessary documentation in good time and ensure it is submitted to the CMA before the deadline. In future, compliance may need to be confirmed to the Pensions Regulator, instead of to the CMA, through the annual scheme return. However, the regulations required to make this change have been delayed, probably to the first half of 2022.
Climate change risk governance and disclosure requirements start to apply for the UK's largest traded companies, banks, insurers and private companies with over 500 employees and £500 million in turnover	April 6, 2022	For noting only. Increased transparency may help trustees with their own disclosures.

Reporting non-taxable pension death payments to HMRC using Real Time Information	April 6, 2022	Check scheme administrators are aware of and prepared for this new requirement.
Stronger nudge to pensions guidance: Ensure members of occupational pension schemes aged 50+ have taken or opted out of guidance before they flexibly access or transfer DC benefits.	April 6, 2022? Consultation published July 2021 and closed on September 3, 2021.	Look out for final regulations and liaise with administrators to update transfer processes and prepare the necessary communications. Similar obligations will apply to personal pension schemes.
Introduction of the £100 “de minimis” threshold, below which flat fees cannot be charged for DC auto-enrolment schemes	April 2022	Update scheme’s charging structures if necessary.
Notifiable events: changes to current regime	April 6, 2022 Consultation on detailed regulations closed on October 27, 2021.	Update or implement a notifiable events protocol for employers and trustee to minimise risk of breaches. Train key people on the new requirements. Review trustee confidentiality agreements.
Regulator’s new single Code of Practice comes into force, including a requirement for an annual “own risk assessment”	Summer 2022? Interim response to consultation published August 24, 2021	Check scheme and employer are compliant with the Code’s requirements. Consider planning first “own risk assessment”, if relevant.
New simpler annual benefit statements for DC schemes used for auto-enrolment	October 1, 2022	Understand the new requirements and be able to design the new form of statement in time for October 2022 (if applicable).
Requirement to measure and report on alignment with Paris Agreement	October 1, 2022	Keep an eye out for the final regulations following the closure of the consultation on January 6, 2022 and discuss the requirements with asset managers.
Climate change risk governance and disclosure requirements extended to further schemes	From October 1, 2022, for second wave of schemes (assets of £1bn and above) Requirements may be extended to smaller schemes (assets under £1bn) from late 2024 or early 2025 – TBC	Second wave schemes to finalise and follow project plan for implementing governance structures and reporting. Smaller schemes to consider whether to comply on a voluntary basis.
Additional TPR guidance for trustees on investing in illiquid investments	2022	Look out for the industry consultation expected in Q4 2021.
New statutory guidance to improve scheme voting and engagement, and increasing level of detail needed in implementation statement	2022	Consultation closes on January 6, 2022. Look out for final guidance and consider what updates are needed to implementation statement and voting and engagement practices

DB scheme funding: changes to requirements	Late 2022/2023	Consider scheme's long term objective and journey plan and discuss with employers. Look out for second consultation, expected Q1 2022, together with full response to first consultation, and consider implications with advisers.
Legislative framework for superfunds	2022/2023	Look out for draft regulations and a consultation in due course. DWP expects to share its vision for a regulatory regime in autumn/winter 2021.
Statutory framework for Collective DC schemes	2022? 2023?	Consultation took place July 19, 2021 - August 31, 2021. Consultation on a code of practice expected Q4 2021/Q1 2022 with final code likely Q2 2022. Target timing for regulations to come into force TBC.
Pension Dashboards	From April 2023 Compulsory staged on-boarding of schemes, starting with the largest schemes with 1,000+ members.	Look out for consultation, and draft regulations expected late 2021 or early 2022. Develop action plan for getting data ready for dashboard.
Changes to asset class information requirements for DB schemes	2023	Look out for further details and discuss with asset managers and advisers.
Reforms to auto-enrolment – lower minimum age to 18 and remove lower earnings limit.	"Mid 2020s" So far this is only the Government's stated intention but no firm steps taken.	Look out for a consultation and draft regulations.
Rise in normal minimum pension age from 55 to 57	April 6, 2028	Draft legislation published November 4, 2021. Take advice on which members benefit from the new protected pension age (of 55). Update member communications.
RPI reform and switch to CPIH	2030	Take advice on implications for DB schemes and necessary actions.

*** This table sets out some indicative action points that trustees and employers may wish to consider but should not be read as a comprehensive plan of action or client-specific advice. Should you wish to discuss these issues further, please contact the Norton Rose Fulbright LLP pension team who will be happy to assist.**

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