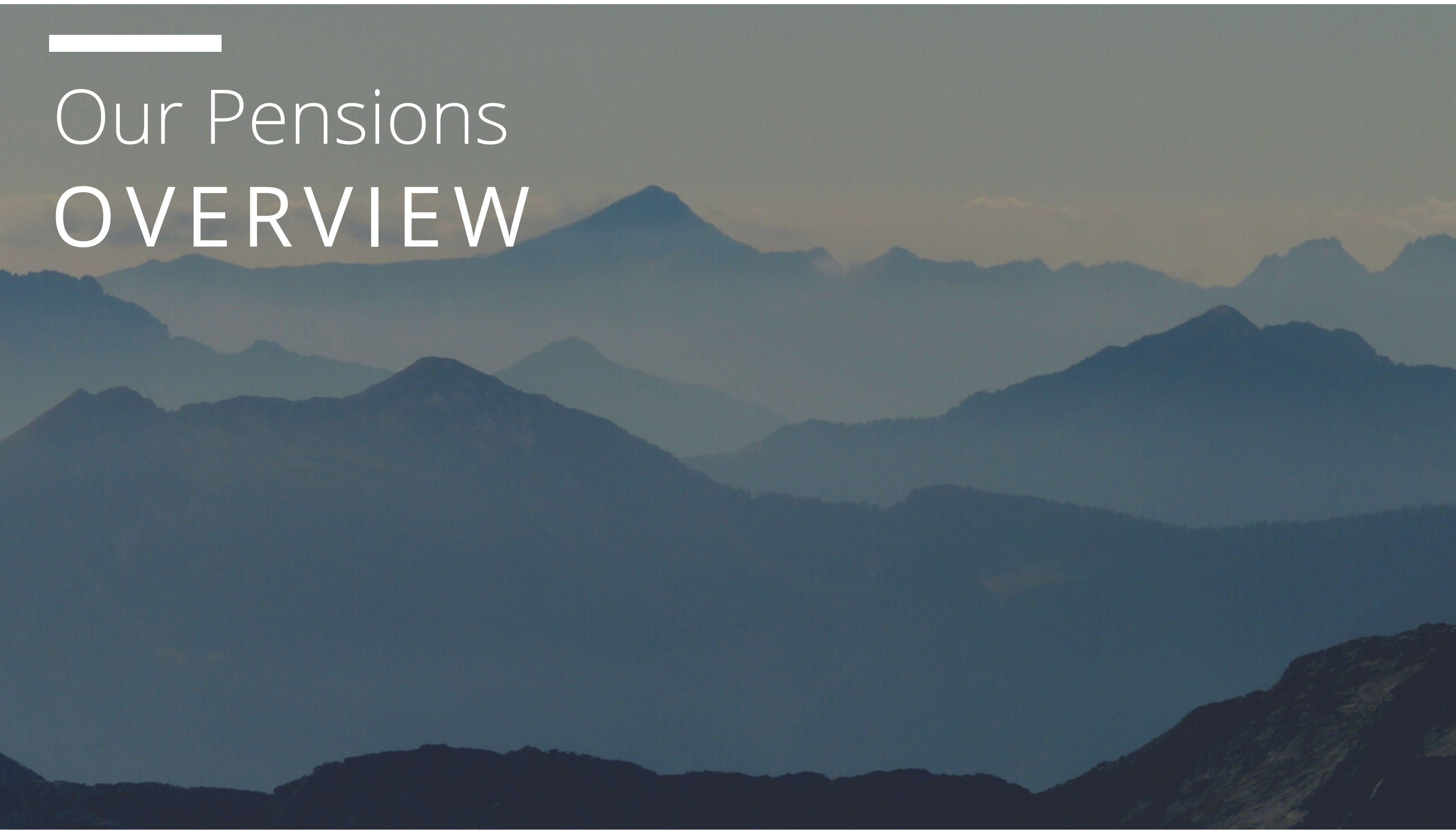
INSIGHT

DEVELOPMENTS IN OCCUPATIONAL PENSIONS

JULY 2022

hughespricewalker

CONTENT



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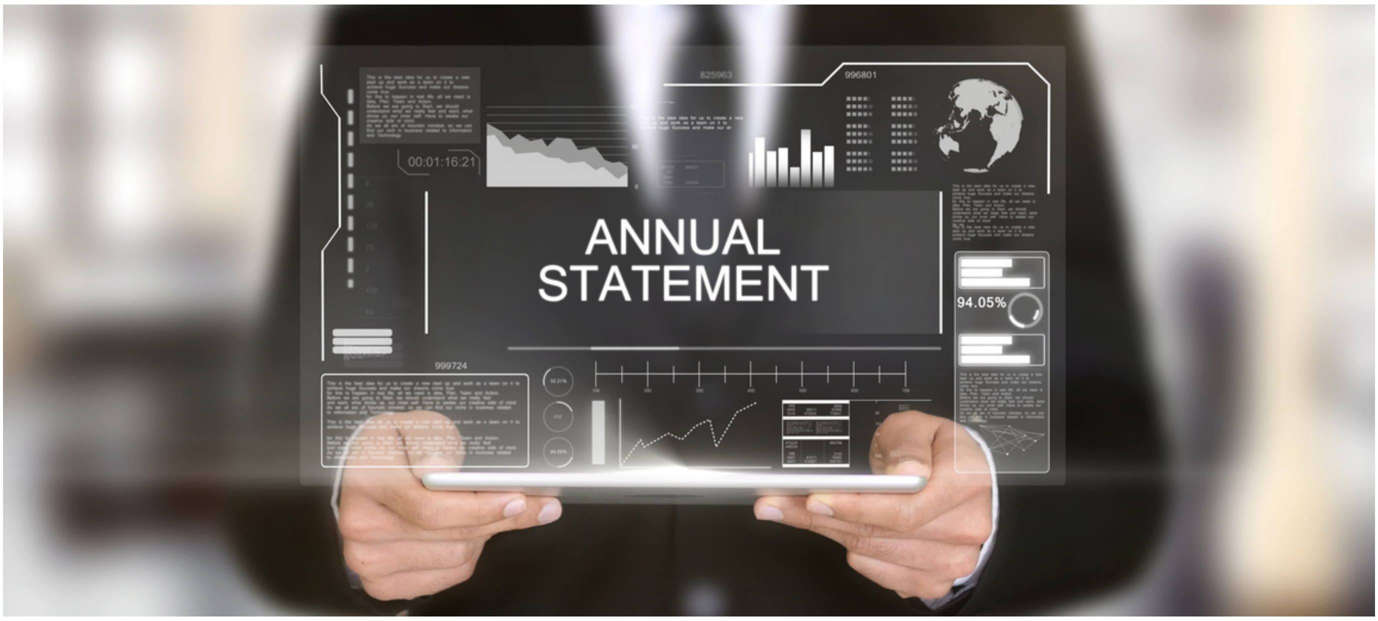
ANNUAL FUNDING STATEMENT (AFS) 2022



The Regulator publishes a statement each year on how it expects trustees to approach current actuarial valuations.

The latest statement was published in April 2022 and can be found at the following link.
https://www.thepensionsregulator.gov.uk/en/document-library/statements

Key points include:

Valuation assumptions

- The UK Statistics Authority plans to align the Retail Prices Index (RPI) with the Consumer Prices Index including owner-occupier housing costs (CPIH) from 2030. Trustees should carefully consider the impacts of this change on assumed inflation before and after 2030.

Covenant considerations

- Trustees should consider the impact of market events on the employer's business and separate them into:
  a. events which have had a limited impact on the business;
  b. events which have had a material impact on the business but trading has recovered; and
  c. events for which the impact continues to be material. They should then consider how the impact of these events should be allowed for in the valuation.
- Trustees should be vigilant over all forms of covenant leakage, not only dividends.
- Where adverse changes in the covenant occur, trustees should have contingency plans in place with agreed trigger points for specified actions.

Recovery plans

- Trustees should consider the impact market events have had on the employer’s covenant:
  a. Where market events have had a limited impact on the employer’s business, there should be no change to the manner in which contributions are set and trustees should try to reduce the length of recovery plans.
  b. Where employers are experiencing short-term affordability constraints, trustees should carefully consider any requests from the employer to temporarily reduce contributions. The Regulator expects any deferred deficit repair contributions to be paid before any dividends recommence.
  c. Where employers continue to ask for a deferral of deficit repair contributions and/or lower ongoing contributions, trustees are expected to obtain suitable mitigations.

Corporate transactions

- Trustees are expected to take a rigorous approach to assessing the impact of any corporate transactions and to negotiate mitigation (where relevant) to protect the interests of members and ensure fair treatment with other creditors.
- If trustees are working through a valuation process at the same time as a corporate event, trustees are expected to obtain mitigation for detriment caused by that event independently of the valuation. Then, separately, they should make appropriate changes to funding elements of the scheme's valuation, taking account of the change in covenant and mitigation received.

Managing risks

- The Pension Schemes Act 2021 requires trustees to set a Long Term Funding Target (LTFT) consistent with how the trustees and employers expect to deliver the scheme’s benefits.
- When setting the LTFT, trustees should consider the extent of their reliance on the employer’s covenant over time and discuss with the employer to understand the short-term and long-term risks that could impact the scheme’s journey plan to its LTFT.
- Where funding positions are below target, trustees and employers should consider strategies to put the scheme back on course.
- Where schemes are fully funded, or are expected to be in the near future, trustees should consider how their liquidity needs will change due to no longer receiving deficit repair contributions from the employer.

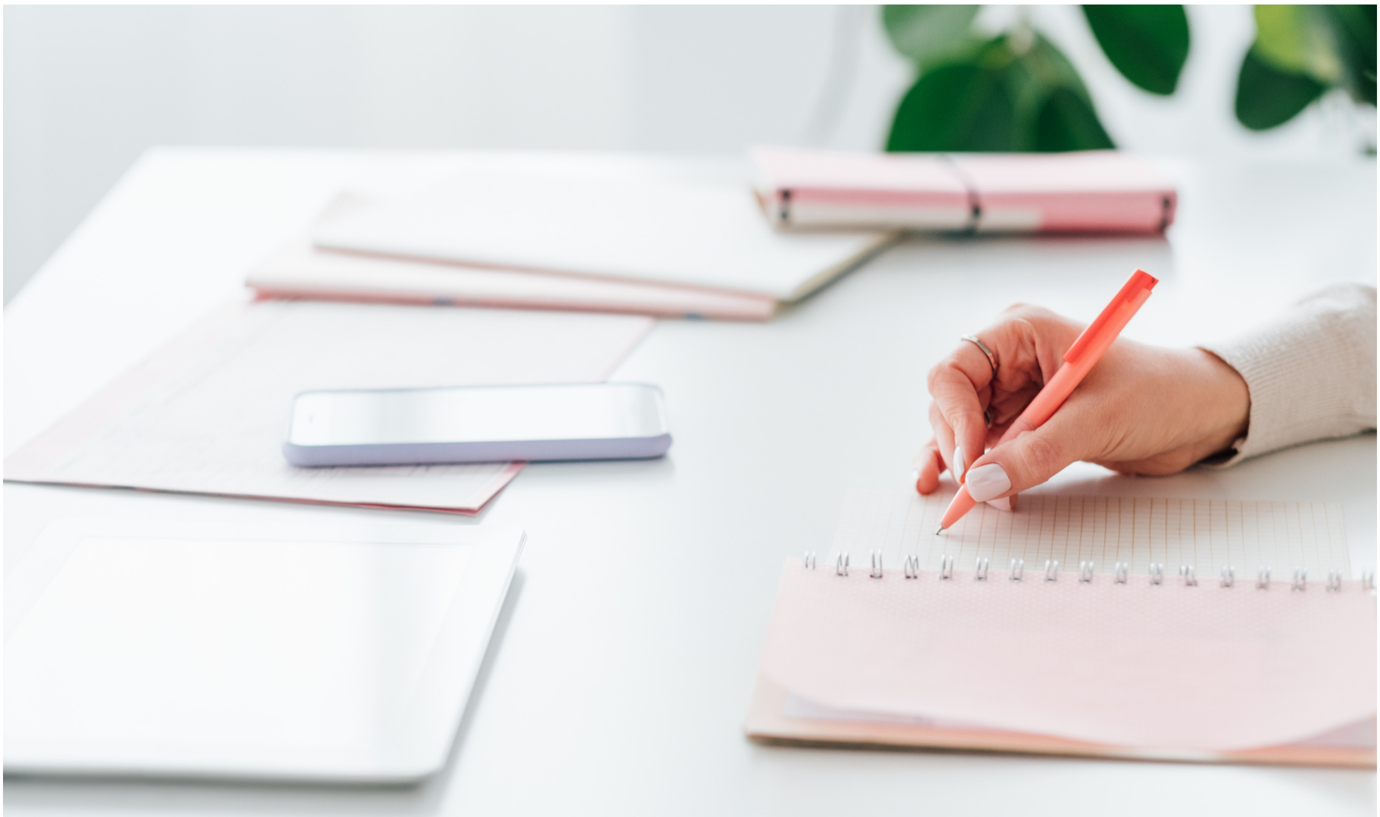
PASA GUIDANCE - GMP EQUALISATION (GMPE) IMPLICATIONS OF PAST TRANSFERS OUT

PASA has published a checklist of generic questions and administrative implications to help trustees hold informative discussions, capture the decisions made and provide an audit trail when implementing the equalisation of past transfers out for the effects of GMP in their scheme. The guidance can be found here.

A summary of the typical issues facing trustees, which the guidance addresses, include but are not limited to:

1. **Bulk transfers** - Transferring schemes which have paid bulk transfer values, perhaps as part of a company disposal, should take specific advice on how the Lloyds judgment impacts on those transfer exercises.
2. **Interest on top ups** - Interest will need to be added to any top up payment. In the Lloyds 2020 judgment, interest on top up payments was set at 1% simple over bank base rates (from time to time). Consideration could be given to using this approach, although some trustees may, having taken advice, choose to use an alternative basis based on scheme rules or previous precedents.
3. **Who might be excluded** – Trustees may conclude that, for some groups of former members, a top up payment won't be due based solely on the transferring scheme's benefit structure, knowledge of the basis used to calculate historic transfer values and/or the member's accrual cessation date. Such groups can then be excluded from the exercise.
4. **De-minimis** - Trustees may want to discuss with their advisers the scope for adopting a de-minimis policy to limit the number of past transfers out cases which will be reviewed.
5. **Tax implications** - If a transferring scheme chooses to pay the top up payment to the former member as a cash lump sum the tax treatment would need to be considered. The pension tax rules allow for small lump sum payments and relevant accretions to be paid out to former members as authorised payments, but with conditions. It's not certain these conditions would be met in all cases and trustees of transferring schemes will need to take advice to ensure the payment is authorised for pension tax purposes.
6. **Tracing and mortality screening** - It's likely to be necessary to undertake tracing and mortality screening for some or all of the in-scope population. Trustees should consider at what point in the project tracing should be undertaken and how this relates to the other decisions which are made e.g., if a de minimis is adopted.
7. **Record-keeping** - It's important to keep records which ensure all of the in scope population have been addressed. This will make it easy to identify the decisions taken on a member-by-member basis in the future.

ITEMS FOR YOUR NEXT TRUSTEES' MEETING



We advise trustees and employers to have on their agenda, among the usual and the scheme specific items, the following items to discuss during their next trustees' meeting:

1- Pension Scams
Pension scams are increasingly hard to spot and anyone can be a victim of scammers. To help protect members and to meet the Pension Regulator's expectations, discuss how to complete the new Trustee Toolkit module and how to issue the ScamSmart leaflet to your members.

2- GMP equalisation (GMPE)
Discuss progress of your GMPE's journey and how to optimise time.

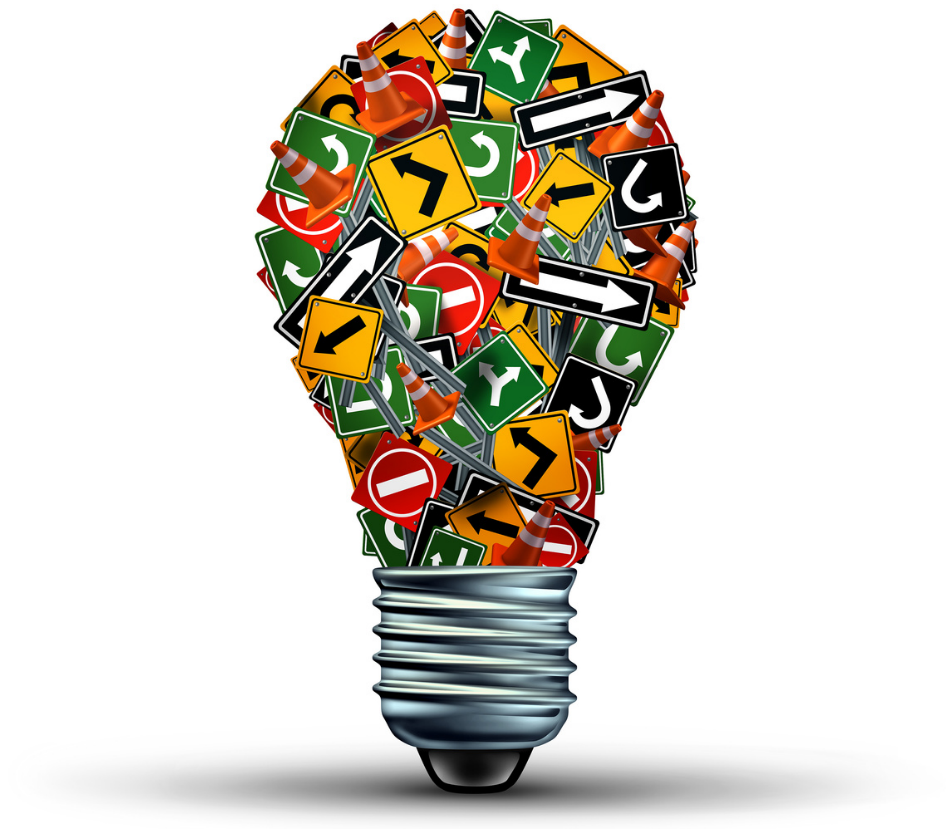
3- Value for Members (VFM)
Consider whether your scheme needs to comply with the VFM assessment and, if so, agree timescales and responsibilities.

4- Effective System of Governance (ESOG)
Check you have an ESOG in place and consider undertaking a gap analysis of your scheme's current policies, practices and procedures to ascertain whether any input is needed.

5- DB transfers
The 2021 Transfer Regulations require additional due diligence checks in some cases. Discuss these regulations with your administrator at your next meeting to make sure you understand your new legal duties and you are satisfied that your administrator's processes have been updated accordingly.

6- Discuss discretionary increases
Given the significant increases in inflation, trustees and employers should check what their scheme rules allow for when it comes to discretionary increases. Even where the power to award discretionary increases might exist, trustees and employers should carefully consider whether it is appropriate to award such increases.

NEW PASA GUIDANCE
SAFER AND BETTER DEFINED BENEFIT TRANSFERS



HPW is pleased to be a member of the PASA DB Transfers Working Group who drafted this new PASA Guidance. The aim of this guidance is to prioritise members and their needs when they decide to transfer their defined benefit (**DB**) benefits out of their schemes.

The Guidance is packed with helpful suggestions for all the parties dealing with DB transfer requests to make sure they know what to do when a transfer request is received.
The objectives of the Guidance are:

1. To improve the overall member experience through faster, safer transfers – the Guidance encourages administrators to look after the member experience during the DB transfer from the beginning to the end and suggests setting realistic response times for third parties to avoid unnecessary delays;
2. To improve communications and transparency in the processing of transfers - the Guidance supports consistency of transfer information through the shared use of the Transfer Template and advises to keep members informed of potential delays, next steps and timescales; and
3. To improve efficiency for administrators – the Guidance shows how using the Transfer Template helps to avoid unnecessary further requests for information and to improve efficiency and save time and resources.

The Guidance sets the principles around the members and underlines that:

1. The member experience is paramount;
2. It’s vital that member communications are timely, fair, clear, unbiased and straightforward;
3. Potential delays and the reason for the delay should be communicated to members and, where appropriate, other third parties;
4. Safety and security should be a priority for administrators when setting internal timescales for each stage of the process. Technology should be used where appropriate to improve efficiency of processes and to enhance the member experience;
5. Working practices should follow the Guidance and administrators should use the Transfer Template when providing information to member advisers; and
6. Administrators should collaboratively work with other third parties to meet the Objectives and Principles of the Guidance.

The Guidance also includes a useful chart that shows a transfer from a member perspective and a settlement process chart that shows the process from when the transfer form is received up to when the payment is made and the member and the IFA is informed.

PHONE:
0117 427 8900

EMAIL:
info@hughespricewalker.co.uk

ADDRESS:
Pembroke House 15 Pembroke Road Clifton Bristol BS8 3BA

WEBSITE:
www.hughespricewalker.co.uk