INSIGHT

DEVELOPMENTS IN OCCUPATIONAL PENSIONS

JANUARY 2024

hughespricewalker

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YOUR NEW YEARS REMINDERS!

31 January 2024 - Deadline for schemes to submit event reports and scheme returns to HMRC (2022/23 tax year)

31 January 2024 – The Pensions Regulator's (TPR) DB & hybrid scheme return notifications expected

27 March 2024 – TPR's General Code of Practice, previously known as the Single Code, expected to come into force

31 March 2024 (midnight) - Pension Protection Fund (PPF) levy deadline for submission of scheme returns, contingent asset and asset-backed contribution certificates and special category employer applications

31 March 2024 – Deadline to submit DB & hybrid TPR scheme return

2 April 2024 (5pm) - PPF levy deadline for submission of supporting contingent asset documents

6 April 2024 - Abolition of lifetime allowance comes into force*

6 April 2024 - New DB statutory funding regime expected to come into force

30 April 2024 (5pm) - PPF levy deadline for submission of deficit reduction contribution certificates and exempt transfer applications

30 June 2024 (5pm) - PPF levy deadline for submission of full block transfer certificates

***Lifetime allowance guidance** (see the updated HMRC guidance issued in December 2023: here).

It covers:

- New rules on Pension Commencement Lump Sums
- Payroll reporting of taxable lump sums and PAYE
- Deadlines for applying for lifetime allowance protections
- Overseas transfer allowance (OTA) and overseas transfer charge (OTC) arrangements – updated guidance on the tax treatment of these transfers
- Lump sum death benefits – confirmation that from an administration perspective there is no change to the current position, whereby a member's legal personal representative should report any chargeable amount after payment of a defined benefits lump sum death benefit or uncrystallised funds lump sum death benefit to HMRC
- New 'Event 24' will be added to the Event Reporting list - this applies where a member has had a relevant benefit crystallisation event (RBCE) that exceeds their available allowance when the payment of a lump sum or lump sum death benefit is paid
- Six events are no longer required and are being removed from the Event Reporting list

Managing Pension Schemes (MPS) service migration update

- HMRC's 'Protection Look up service' to check members' lifetime allowance protections will be moving to Managing Pension Schemes (MPS) service in 2025
- Reporting overseas transfers using APSS262 form will be done via MPS from April 2025
- The functionality to submit event reports is being migrated to MPS
- HMRC pension scheme returns for the tax year ending 5 April 2024, and subsequent tax years, must be submitted on the MPS service, instead of using the pensions scheme online service

HMRC will be asking for more information than they have done in the past in scheme returns completed on the new MPS service. HMRC also plans to ask more schemes to submit returns than before. Even those who have never previously received a notice to file a pension scheme return might need to in the future.

Note: It is more important than ever that Scheme Administrator logins are up to date, and that where possible HPW has practitioner access to MPS service, to avoid any potential fines for failure to make any necessary submissions at the beginning of 2025.

If you would like any further information, including details on HPW can help you, please speak to your usual HPW contact.

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DB FUNDING CODE

A new Defined Benefit Funding Code is expected to be introduced by the Pensions Regular (TPR) on 27 March 2024, delayed from an original target of October 2023, and impacting schemes with valuations from Autumn 2024. It was laid in parliament on 10 January 2024.

Long term planning

The new code focuses on long term planning for schemes. In addition to actuarial valuations showing the current position, trustees must set a plan for the long-term funding of their schemes.

This should comprise a long-term funding target (including how benefits are to be provided and the funding level to be attained by the "relevant date") and a journey plan of how to reach this from the current funding position.

The "relevant date" is set by the trustees and must not be later than the scheme year that the scheme reaches significant maturity, as estimated by the scheme actuary.

The target level must be at least 100% on a "low dependency" basis (i.e. a basis whereby if the scheme was fully funded it would be expected that no further employer contributions would be required).

Methods of providing benefits include:

- continuing to pay them from scheme assets as they fall due;
- taking the scheme to buyout with an insurer; and
- transferring the assets and liabilities to a consolidated fund.

The funding target should be consistent with the selected method of paying benefits, e.g. if looking to buy out with an insurer then a higher funding target would be appropriate.

Trustees must set a "journey plan" setting out how they intend to reach their long-term funding target from the current position.

The plan should take into account the employer covenant (with more risk being acceptable if the employer covenant is strong) and the maturity of the scheme, whilst maintaining sufficient liquidity.

After the "relevant date" the trustees should assume a "low dependency" asset allocation, with cashflows broadly matched between assets and liabilities and a funding level resilient to short term adverse changes in the market. The strategy must be set with prudent assumptions and sufficient liquidity to ensure no further contributions are expected from the employer once the scheme is fully funded. Scheme liabilities must be calculated on a basis consistent with a low dependency strategy.

Employer covenant

The new code has a strong focus on the employer covenant, i.e. the ability and willingness of the employer to fund the pension scheme. Previously, considerations of employer covenant have often been backwards looking, focused on past performance, when it is the future cashflows of the company that will determine its ability to contribute to the pension scheme. The new code aims to encourage trustees to engage in more detailed, reliable and forward-looking covenant assessments of employer insolvency risk.

The new code emphasises consideration of the following in respect of the employer:

- covenant visibility, the period for which reliable forecasts are available;
- covenant reliability, the period for which the trustees have reasonable certainty over the employer's levels of available cash; and
- the longevity of the covenant, the maximum period where the trustees can reasonably assume the employer will be able to support the scheme.

The length of these periods should inform choices around the level of risk to take and the length of journey plan. Note that the code also states that the overriding principle that funding deficits should be recovered as quickly as the employer can reasonably afford still applies.

Statement of strategy

Trustees must prepare a statement of strategy setting out the decisions, with a level of detail dependent on the amount of risk being taken. Trustees must agree some parts of the statement with the employer (the general funding and investment strategy) and consult with them on others (the supplementary details). The strategies must be set or reviewed within 15 months of an actuarial valuation falling after the code's effective date (expected to be Autumn 2024).

It should be noted that trustees are not required to invest in line with the low dependency asset allocation. Immature schemes with a strong funding position and strong employer covenant can be justified in taking more risk in seeking growth.

However, given that smaller timeframes will mean less time for any losses to be recouped, TPR expects trustees to move towards a strategy consistent with low dependency after the "relevant date". It does however state that this does not mean no investment allocation to growth assets.

In oral evidence to the House of Commons, Louise Davey of TPR stated:

"the objective is not to remove all risk from the DB system and we are very clear that there are a good number of schemes that have the capacity to take on a significant amount of risk in their investment strategy if that is what they chose to do because they are immature, because they are open to new members and future accrual and because they have a strong employer covenant that can support the scheme should the investment returns not play out as hoped. That is the key. Even with mature schemes, there is still significant scope for them to be investing in growth assets, and that is also made clear in the code of practice."

TPR emphasises that the code is consistent with the government's "mansion house reforms", which aim to increase investment productivity for schemes.

Twin-track regulatory approach

Alongside the new code, TPR will be updating its regulatory approach and introducing a new twin-track method – "fast-track" and "bespoke". For schemes that qualify for "fast-track", the submission will be subject to less scrutiny and TPR is unlikely to query the scheme trustees.

Qualification for the "fast-track" approach is generally based upon the funding basis used and the length of recovery plan agreed relative to the scheme duration, with stipulations specified by TPR. If the scheme does not qualify for "fast-track" it will fall under "bespoke".

This will allow more flexibility in agreeing an approach between trustees and employers to suit the scheme but will require more thorough information in the valuation submission and face greater scrutiny from TPR.

TPO CASE - AMBER FLAG AND OVERSEAS INVESTMENTS

The Pensions Ombudsman (TPO) recently issued its first ruling on the "amber flag" related to overseas investments within the pension transfer value regulations.

Facts:
Mr. W initiated a pension transfer in February 2022, leading to an amber flag due to perceived overseas investments. The Trustee insisted on MoneyHelper consultation, causing a dispute with Mr. W's adviser and resulting in a delay. The transfer was eventually completed in May 2022, with a reduced value.

Background:
The Transfer Regulations, effective from 30 November 2021, govern transfers initiated on or after that date. These regulations impose conditions, including assessing the presence of red or amber flags. Under this framework, a red flag halts the statutory transfer, while an amber flag temporarily suspends it until the member seeks guidance from MoneyHelper.

Decision:
TPO ruled in favour of the Trustee, stating they acted reasonably. The decision emphasised the Trustee's right to interpret regulations and concluded that the delay was not unreasonable, considering the perceived overseas investments.

Our comment:
This case provides vital support for pension trustees, administrators, and providers grappling with the increasing complexity of pension transfers. TPO's ruling offers valuable guidance on the proper application of the "amber flag" concerning overseas investments, providing clearer insights into navigating the regulatory landscape surrounding transfers and associated member safeguard requirements.

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CONSOLIDATION INSTEAD OF BUY-OUT – WHAT ARE THE OPTIONS?

According to the 2023 Purple Book, 68% of the 1,875 schemes with fewer than 100 members have buy-out funding ratios over 100%, up from 18% the year before. This means 1,275 small schemes could be ready for end-game, an increase of nearly 1,000 highlighting intense competition in the de-risking market.

As the buy-out market has become increasingly busy, commercial consolidators designed to accept pension scheme liabilities for less than the cost of buy-out, providing additional capital to improve members' benefit security, with the added advantage of removing the sponsor's obligation to support the scheme, have gradually emerged. As trustees you may be wondering what the current options are and which options are potentially in the pipeline?

Option 1 - Superfunds

In the March 2028 Government White Paper outlining the future of commercial consolidation, two superfund options were highlighted:

- Clara Pensions (Clara) – which aims to buy-out schemes it takes on in the medium term.
- The Pensions SuperFund (PSF) – which plans to run-off liabilities it takes on indefinitely.

Whilst the Department for Work and Pensions is developing an authorisation framework, an interim regulatory regime in which The Pensions Regulator (TPR) assesses superfunds is in place. Once an approved superfund is selected, to obtain clearance from TPR, three "gateway principles" must be met, which are:

- The scheme cannot access buy-out now.
- There is no realistic prospect of buy-out "in the foreseeable future" given potential employer contributions and the employer's insolvency risk.
- The transfer improves the likelihood of members receiving full benefits.

Superfund Features

- Ring fenced funding – improved financial member security
- Economies of scale - reduced costs, broader investment options, robust integrated risk management, improved governance
- Funding available from capital providers
- Current administrator can potentially remain in place – continuity
- Support with buy-out for schemes who would otherwise struggle to afford to move straight to buy-out with an insurance company

- Allows employers to focus on their core business – a 'statutory' employer takes responsibility
- Under Clara trustees remain in control of the decision to run on or transfer members out
- Alternatively, with PSF, trustees transfer responsibilities to their independent, professional trustee board
- PSF may offer members a bonus if a surplus in the Buffer Fund exists
- PSF members receive their agreed contractual benefits in full in perpetuity

Currently Clara is the only superfund to pass TPR's assessment process and able to transact. In November 2023, clearance was received from The Pensions Regulator for Clara Pensions to receive the transfer of around 9,600 members of the Sears Retail Pension Scheme in the UK's first defined benefit (DB) superfund transaction. Further details of this transaction are on page 13.

Option 2 - A new statutory vehicle run by the Pension Protection Fund (PPF)

In his Autumn Statement on 22 November 2023, the Chancellor signposted fundamental changes to the way in which the PPF operates in his Mansion House speech. The government has announced a consultation on how to consolidate smaller final salary schemes considered to be "unattractive to commercial providers" into a new statutory vehicle to be established by 2026, to be run by the PPF.

Consolidation will be voluntary on the part of trustees and will not be mandated.

What form might this take? Possibly:

- A pooled investment vehicle for smaller DB schemes operated by the PPF
- A DB master trust run by the PPF, to which small DB schemes could transfer their assets and liabilities, services could be aggregated and investments pooled
- A 'superfund' for smaller DB schemes run by the PPF

Under the first two options, a scheme's employer would remain responsible for any funding shortfall and benefits could still be bought out or transferred to a superfund, whereas under a PPF 'superfund' the link to a scheme's employer would be broken.

Other items on the horizon – DC small pots possible option

There are also plans for a multiple default consolidator model to be introduced, enabling a small number of authorised schemes to act as a consolidator for eligible defined contribution pension pots under £1,000.

Conclusion

Only when the outcome of the consultation on the PPF proposals is announced, will it be possible to obtain a view on the potential implications for our clients. Although 2026 is not too far away, we are also mindful that a general election next year may change things in the meantime.

The superfund option may be of interest where the scheme's covenant is weak, or scheme size makes it less attractive to insurance companies who may prioritise larger transactions.

If you would like more information on your specific needs, please feel free to discuss with your usual HPW consultant.

THE IMPLICATIONS OF THE CMG CASE ON RECTIFYING ERRORS IN PENSION MATTERS

In a recent ruling (The Pensions Ombudsman v CMG Pension Trustees), the Court of Appeal has confirmed that obtaining a court order is necessary for the recoupment of overpaid pensions from members. The court made it clear that relying solely on a decision by the Pensions Ombudsman (TPO) is insufficient for reclaiming a disputed sum.

Breakdown:
In 2022, the High Court, in the case Pensions Ombudsman v CMG Pension Trustees, examined trustees' authority to recoup overpaid benefits, particularly through future pension payment reductions. Section 91 of the Pensions Act 1995 (PA95) governs set-off against pension benefits, allowing trustees to recoup overpayments under specific conditions. These conditions include (i) ensuring that deductions don't exceed the monetary obligation, (ii) providing the individual with a certificate detailing the owed amount and its impact on benefits, and (iii) in case of a dispute, waiting until the obligation is enforceable under a court order.

Summary:
The court clarified that for recouping through future benefit reductions, a court declaration is sufficient, eliminating the need for a payment order. The Court of Appeal specified that TPO isn't a competent court in this context. To enforce TPO's decision, trustees should present a certified copy to the County Court, which will then administratively enforce it, avoiding a rehearing of the case.

Additionally, the court addressed the interpretation of a "competent court," rejecting the idea that TPO qualifies. It emphasised that TPO's role is distinct from a court and his jurisdiction is one-sided, requiring a member to initiate the process.

Conclusion:
The court upheld the requirement for a court order from a competent court, such as the County Court and not TPO, to enforce recoupment after a dispute has been considered and determined by TPO.

TPO issued a factsheet outlining guidance on handling disputed overpayments. The factsheet, along with the first determination post-CMG in Mr Y v AECOM, clarifies the process for trustees. If overpayment recovery is disputed, trustees acting without a County Court order may be considered unlawful and constitute maladministration.

The factsheet provides guidance on managing overpayment disputes, emphasising the need for a County Court order to enforce TPO’s determinations. The document outlines the internal dispute resolution process, pre-determination considerations, and the County Court process, specifying that the County Court's role is not to re-hear the case but to authorise recoupment according to the designated schedule in the TPO determination.

2024 NEW YEARS RESOLUTION - PROTECT AGAINST CYBER SECURITY

Taking steps to protect members' personal data and pension scheme assets from cyber risk should be a priority for all trustees. In December, The Pensions Regulator (TPR) outlined its expectations for trustees and scheme managers.

In summary, overall responsibility for the security of pension schemes sits with trustees and scheme managers. In many cases responsibility will be delegated. Where this is the case, to fulfil their governance obligations trustees need to understand the potential risks relevant to the scheme, ensure relevant controls exist, and be able to manage any incidents that may occur.

To achieve this, trustees should:

- Carry out regular assessments working together with all who deal with the scheme
- Seek assurances or evidence of the controls that exist
- Think about what isn't included but should be (possibly consider using an independent specialist)
- Set up a process where regular jargon free reports are received to monitor the frequency, type and impact of any systems compromises or data breaches

The purpose of the assessments is to understand who has data, where scheme data is being transmitted, the type and severity of both intentional and accidental incidents that might take place and the impact of these on members, the scheme and possibly the employer.

Trustees should also:

- Consider operational and financial issues but also potential reputational damage.
- Understand which functions are critical and why a criminal would benefit from interrupting them as well as what they might do if they stole your data.
- Remember all risks need to be included on the scheme's risk register.

As cyber security affects everyone, trustees need to think about their own activities too – how safe are personal email addresses and reading emails on mobile phones and tablets? Do not delay software updates! Installing software updates promptly can reduce cyber risk.

Have an incident response plan – prioritise core services (for instance a main aim might be that payroll is reinstated within 24 hours)

Individuals should be selected to make up an incident response team. The plan should clearly define the roles and responsibilities along with the scheme's priorities. It must set out detailed processes for escalating and responding during an incident. This should include how internal and external communications might be managed via alternative means if the usual systems infrastructure is not available.

Test the plan! – test a range of different situations. No one can protect themselves from everything, but you will be better equipped to react if you have practiced the drill.

CLARA PENSIONS ANNOUNCES UK'S FIRST PENSION SUPERFUND

On 6 November 2023, Clara-Pensions (Clara) and the Trustees of the Sears Retail Pension Scheme (Sears) reached an agreement for the UK's first superfund transaction. Sears has around 9,600 members who will enter the superfund, with Clara providing £30m of new capital to increase the security of these members' benefits. Clearance for the transfer was received from the Pensions Regulator and the formal transfer of members took place at the end of November.

The Trustees of Sears said: *"Clara is committed to putting members' needs first, which will ensure members continue to receive the excellent quality of support we have committed to as trustees. We are delighted to have reached this agreement with Clara and are confident that the proposed transfer is firmly in our members' best interests".*

Clara was established in 2017 and operates a "bridge to buyout" model. Simon True, CEO of Clara, said: *"Clara was created to provide a safe bridge that brings the insurance market into reach for more schemes and their members".*

In the Autumn Statement published on 22 November 2023 the government confirmed itwill consult this winter on how the Pension Protection Fund (PPF) can act as a consolidator for defined benefit schemes unattractive to commercial providers. Oliver Morley, CEO of the PPF, has said: *"Running a Public Sector Consolidator would be a natural evolution of the PPF's existing capabilities. Through our investment approach the PPF already provides a blueprint for how the government's objectives can be delivered at scale".*

Further details of the superfund transaction between Clara and Sears can be found here.

DASHBOARD UPDATE!

The Pensions Administration Standards Association (PASA) has released new 'Connection Ready Guidance' on dashboards along with a 'Call to Action' reminding trustees and scheme managers to:

- consider the Pensions Reglator's checklist
- talk to administrators about what they are doing
- review PASA's guidance
- check to see if anything extra needs to be done
- develop a plan!

Trustees should read the guidance which can be found here.

What does 'Connection Ready' look like? PASA's guidance sets out 5 key readiness pillars and suggests some of the ways these can be met might be as follows:

'Governance readiness'

- A documented governance structure with evidence of regular meetings to oversee delivery of the project plan and a record of decisions made.

'Matching readiness'

- A data assessment report to help establish a process for matching.
- A statement confirming the initial matching approach chosen (with any legal advice obtained attached).
- An ongoing data management statement & possibly a data improvement/cleanse report.
- A matching readiness statement to sign off the final choice for matching.

‘Pensions Values readiness’

- A report outlining data coverage rates and improvement plans.
- Documented processes for maintaining good data, refreshing data, meeting deadlines and dealing with queries.
- Documenting any differences between calculations and having a process to communicate these to members.
- An implementation statement.

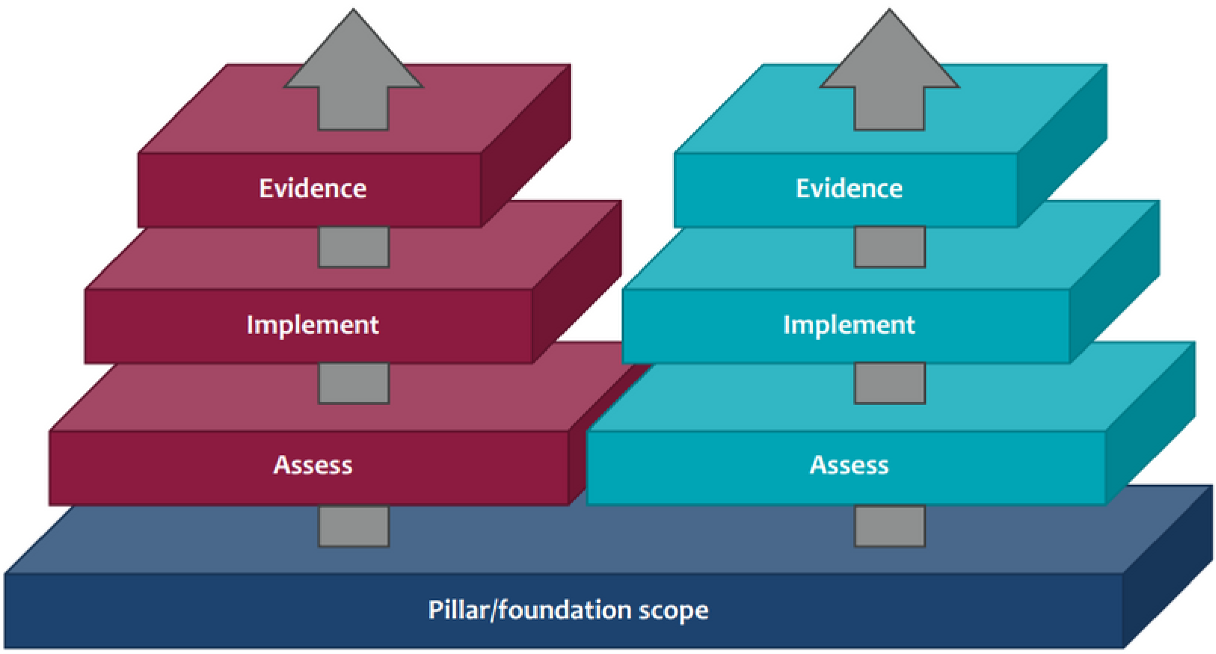
‘Technology readiness’

- Confirmation that the connection solution has been verified by the Pensions Dashboards Programme.
- An acceptance testing statement which should include user access to the exchange or loading of test data.
- An implementation statement evidencing end to end data processing, that matching is working, and all information is ready to launch.

‘Administration readiness’

- Processes established for reviewing, testing and updating documentation and analysing reporting data.
- Documenting assumptions and undertaking an impact assessment on various scenarios.
- A documented communication strategy including a review process.

Further supporting material from PASA is expected to supplement the Values Guidance issued in June 2023 in due course. HPW will keep you updated of developments as they arise.



Picture from PASA’s guidance

TPR - New general code

The Pensions Regulator (TPR) has finally published the general code which is set to come into force on 27 March 2024. This code encourages governing bodies to assess their schemes in accordance with TPR standards, with a focus on cultivating robust governance systems and conducting comprehensive risk assessments. TPR advocates for proactive engagement, encouraging schemes to actively align with the prescribed standards. Those that do not meet the code's expectations should take immediate action to improve their scheme's governance.

HPW will be supporting its clients and their HPW consultants will be in touch with them.

If you need support in enhancing your governance, and you are not already a HPW client, please contact us. We are here to assist you! Click here to read the general code of practice.

PPF publishes final 2024/25 levy rules

In December 2023 the Pension Protection Fund (PPF) published its final rules for the 2024/25 levy year. It has set the levy estimate at £100m, which is a £100m reduction from the levy estimate for 2023/24 and is the lowest levy estimate the PPF has ever set.

The PPF expects to hold the levy estimate at this level for future years, and has confirmed it will keep the amount charges under review in case there are any material changes in the risks it faces. The PPF will continue to consult on its approach each year.

The two main changes from the 2023/24 levy year are an increase in the levy scaling factor from 0.37 to 0.40 and a decrease in the scheme-based levy multiplier from 0.000019 to 0.000015. No other significant changes have been made.

The PPF expects that 99% of schemes will see a decline in their total levy between the 2023/24 and 2024/25 levy years. On average, schemes are expected to see a 25% reduction in the scheme-based levy and a 40% reduction in the risk-based levy. The PPF confirmed that it intends to delay any revision to the asset stress factors, despite the significant volatility in interest rates over the last year. It appears likely that the 2025/26 levy rules will include changes such as increasing the investment stresses by considering worse economic scenarios and introducing an additional factor on the liabilities.

The levy rules and policy statement can be found here.

If you would like any further information, including details on how HPW can help you to monitor your PPF levy, please speak to your usual HPW contact.

hpw

PHONE:
0117 427 8900

EMAIL:
info@hughespricewalker.co.uk

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

WEBSITE:
www.hughespricewalker.co.uk