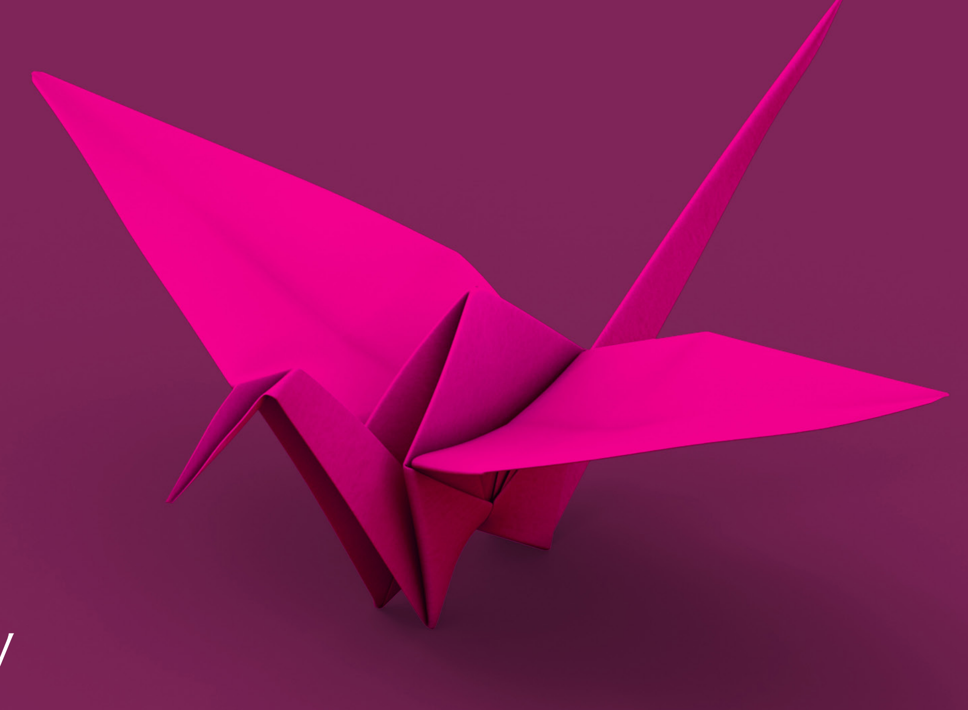
Your Quarterly Pensions Update

Dalriada Trustees – Industry Changes

Quarter Four 2022



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Introduction

The purpose of this report is to provide an update for pension scheme sponsors and trustees on recent industry changes in the quarter

For your convenience, we have summarised the key developments and highlighted the necessary actions sponsors and trustees may need to take.

We also include links to further relevant information and any deadlines you should be aware of.

We trust you will find the update useful and informative. If you require further information about how any of the topics covered might impact on your scheme specifically, please get in touch with Adrian Kennett, adrian_kennett@dalriadatrustees.co.uk or your usual Dalriada contact.

NOTES

This document is aimed at providing you with generic information about recent developments in the pensions industry.

You should not take any action as a result of information included in this document without seeking specific advice in relation to the impact these matters might have on your scheme or company. Dalriada Trustees Limited accepts no liability for actions taken or not taken as a result of this document.

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1 Dashboard Update

Pensions Dashboards - A bit like buses?

You wait ages for a bus and three arrive at once!

The same might be said about pensions dashboards.

In the past few months, there has been no less than three important developments (see below) and, as things stand, it does look as though the proposed go-live date of October 2023 will be achieved. Trustees, even if their scheme does not 'stage' until 2024 or beyond, should now be thinking about the quality of their data – '*is it dashboard proof?*'; how they will connect to the eco system and whether they have sufficient resource to comply with their prospective duties, which will be enforced by The Pensions Regulator.

Response to further consultation on pensions dashboards

The DWP has published the government response to the second consultation on the creation of pensions dashboards. The consultation concerned the formal notice period provided before the dashboard services would be made available to the public referred to as the Dashboards Available Point (DAP) and the disclosure of information between the Money and Pensions Service and the Pensions Regulator.

Guidance on deferred dashboard connection

The DWP has also published guidance for trustees and their advisers regarding the issues trustees consider if they are applying for a deferral of their staging deadline (the deadline for the scheme to be connected to a dashboard of digital architecture) set out in schedule 2 of the draft Pensions Dashboards Regulations 2022.

Pensions Dashboards Regulations 2022

These regulations, SI 2022/1220, set out requirements that need to be in place to enable pensions dashboard services to operate effectively. They come into force on 12 December 2022.

Helpful Links

Pensions dashboards: further consultation - GOV.UK (www.gov.uk)

Pensions Dashboards: guidance on deferred connection - GOV.UK (www.gov.uk)

The Pensions Dashboards Regulations 2022 (legislation.gov.uk)

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2 Funding code update

DRAFT DEFINED BENEFIT FUNDING CODE ARRIVED JUST IN TIME FOR CHRISTMAS

The Pensions Regulator ('tPR') issued its draft defined benefit (DB) funding code of practice on 16 December 2022. This was issued alongside a consultation document, a separate consultation on the 'twin track' (fast-track and bespoke) approach and a response to the Regulator's first funding code consultation in 2020. Collectively, the documents run to over 200 pages.

We anticipate that the consultation will proceed largely as written. Accordingly, this would represent the most significant change in the funding of DB pension schemes since the Statutory Funding Objective first came into force in 2005.

In summary, the overarching theme is one of more detailed requirements in a move towards reducing risk (or, perhaps more charitably, raising the bar for evidencing supportable risk taking) as schemes mature.

THE FUNDING AND INVESTMENT STRATEGY STATEMENT ('FISS')

A new Trustee requirement under the Code is to draft a FISS, which has two parts:

- A record of the funding and investment strategy ('FISS'), and
- A record of various supplementary matters (including matters related to the journey plan, strategy implementation and risk management)

The FISS must be submitted to tPR with every valuation submission; and signed on behalf of the trustees by the chair of trustees (i.e. all DB schemes must ensure that the trustee board has a formally appointed chair).

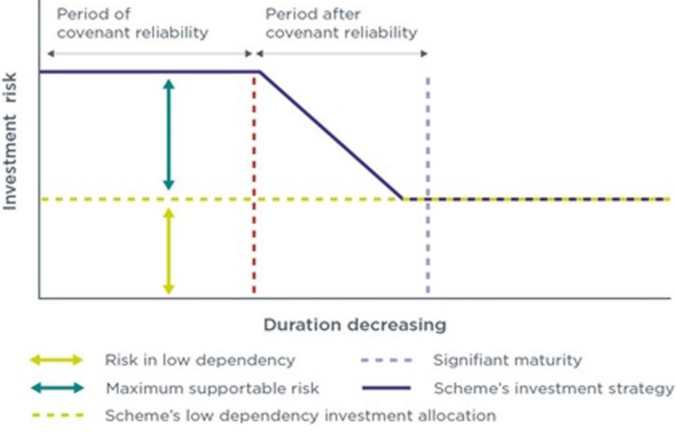
FUNDING AND INVESTMENT STRATEGY

For the purposes of the FISS and determining their 'end game', Trustees must agree, in conjunction with the employers, their long-term objective ('LTO'), a long term funding target ('LTFT') and the investments they intend to hold, when the Scheme reaches significant maturity (the 'relevant date').

For the purposes of the funding and investment strategy, trustees must assume that scheme assets will be invested in accordance with a 'low dependency investment allocation' ('LDIA') on and after the relevant date. The LDIA should broadly match liability cashflows and be resilient to short term market movements.

The LTFT must be at least full funding on a low dependency funding basis ('LDFB'), where the LDFB must use actuarial assumptions which are set such that if one was to presume that the scheme was fully funded on that basis, and the scheme's assets were invested in accordance with the LDIA, then no further employer contributions would be expected to be required.

Trustees must plan how they intend the scheme to reach its LTFT; referred to as the 'journey plan'. When determining the journey, trustees must consider how they intend to transition from their current investment strategy to the LDIA and must ensure that this transition is dependent on the strength of the 'employer covenant' and on the maturity of the scheme.



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COVENANT

Assessing the covenant will be a key underpin for the level of risk supportable, despite there being no covenant metric to satisfy the "Fast Track" (see below) requirement.

When assessing the employer's financial ability to support the scheme, trustees must consider the employer's cash flow, the likelihood of an employer insolvency event occurring and other factors that are likely to affect the performance and development of the employer(s) business. The nature of the assessment will depend on the circumstances of the scheme and employer. There will be a further consultation on detailed covenant guidance during 2023.

VALUATIONS – FAST TRACK AND BESPOKE

Trustees may elect to use a Fast Track or a Bespoke route to demonstrating compliance with the legislative requirements, both being equally valid.

The Fast Track assumptions were derived based on analysis as at 31 March 2021 and at that date tPR estimates that around 50% of schemes would have met all requirements. However, Fast Track is not a route to "minimum compliance". Rather, it is, in essence, a filter for tPR to enable them to focus their attention where they deem it is most likely to be required.

If the Fast Track route is followed then trustees can expect minimum regulatory involvement, if any, on DB funding. For schemes that meet most, but not all, of the Fast Track requirements, tPR still expects them to be Bespoke submissions. However, they should expect a lighter touch assessment.

tPR has not set benchmarks for RPs under Code, but six years is used for Fast Track falling to three years after the relevant date.

TIMETABLE

The consultation on the draft Code lasts until 24 March 2023. tPR has stated that the earliest that the Code will come into place will be 1 October 2023, and will only apply to new valuations due after it comes into force.

Action
Trustees should seek to review their current funding and investment strategies and consider, in the context of the employer covenant, to what extent changes are required and whether fast track or bespoke may be the way to proceed. Trustees with valuations scheduled prior to the Code coming into force might be wise to apply the principles of the draft Code. Both need to plan for additional advisory costs in the short term.

Helpful Links
Draft defined benefit (DB) funding code of practice and regulatory approach consultation | The Pensions Regulator

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3 Investment Update

In the UK, unfunded tax cuts and an uncertain political landscape led to a volatile start to the quarter. The emergency budget announced by Kwasi Kwarteng, the then Chancellor, caused UK gilt yields to soar with the value of sterling collapsing to historic lows of $1.07. However, intervention from the Bank of England allowed markets to stabilise to some degree. The new Chancellor, Jeremy Hunt, followed in the footsteps of the newly appointed Prime Minster, Rishi Sunak, and adopted a more conversative approach, switching focus to a more fiscally aware stance. A revised policy of increased taxes and a reduction in government spending was adopted. During the period, the Bank of England mirrored the US Federal Reserve's decision to reduce the quantum of base rate increases over the period, and whilst raising base rates twice over the quarter in November and December, the latter was by 0.5% (reduced from the previous increases by 0.25%). Overall, the year finished with base rates peaking at 3.5% from just 0.25% twelve months earlier.

Global Stock markets bounced back from a difficult year with gains in Q4 across all regions. The UK posted returns of 8.9% in local currency over the quarter (and 0.3% for the year). US equities rose 7.6%* (-18.1% over 2022), whilst Japanese stocks rose during October and November and despite a decrease in December, the region returned 3.3%*over the period (-2.5% for the year). Emerging markets rebounded with a strong return of 9.8% over the period (-19.7% for the year) in USD, after China succumbed to pressures and relaxed their zero-tolerance policy on COVID-19, which surprised markets and boosted Asian shares late in the quarter. The Eurozone equities outperformed most other regions over Q4, returning 11.1%* (-12.2% over 2022) . Whilst these gains were supported with hopes that inflation had peaked, the European Central Bank (ECB) like many others, followed the US Federal Reserve in reducing their latest interest rate increase, however the ECB warned there was little likelihood of rate increases coming to an end. The US Federal Reserve increased rates twice over the quarter, ending the year with rates at 4.25%. Sustained inflation remains a risk globally.

As at the end of the quarter, the over 15 year UK gilt yields increased by 0.16% to 3.90% as Fiscal uncertainty continued. However the increase in yield was lower than that observed over the third quarter which saw an increase of 1.18% over the period. All else being equal, the move in gilt yields will act to decrease the value placed on pension schemes' liabilities. Long-term inflation rates decreased by 0.51% driven by the BoE's sustained period of interest rate increases which appears to have begun curbing the increasing rate of inflation. All else being equal, sustained periods of heighted inflation will increase the value placed on pension schemes' liabilities.

Yields on global credit fell over the quarter with credit spreads also narrowing. Following the actions taken by central banks (rates of increases reducing) and the potential for inflation to begin to fall back, investors have begun to view the market more optimistically. UK Long-dated credit spreads decreased 0.5% which was mainly driven by calm being restored to markets from 1.34% to 0.84%.

* All regional returns are shown in local currency terms unless otherwise defined.

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Pension Scheme Health Check 2022

- Administration
- Automatic Enrolment
- Defined Benefit
- Defined Contribution
- Guaranteed Minimum Pensions and GMP equalisation
- Indexation of pensions
- Investment
- Pension Protection Fund
- Tax
- The Pensions Regulator

ADMINISTRATION

Pensions Dashboards Regulations 2022

These regulations, SI 2022/1220, set out requirements that need to be in place to enable pensions dashboard services to operate effectively. They come into force on 12 December 2022 and include the staging timetable for pension schemes to connect to dashboards.

Action
Consider steps to get 'dashboards ready', including quality of scheme data, connection and the resource required to ensure timely compliance. The Pensions Regulator will be able to impose penalties for non-compliance.

AUTOMATIC ENROLMENT

Earnings trigger and qualifying earnings band

The automatic enrolment earnings trigger and qualifying earnings band for 2022/23 are shown in the table below -

	Trigger	Qualifying earnings band, lower limit	Qualifying earnings band, upper limit
2022/23	£10,000	£6,240	£50,270

Action
Ensure correct assessment of all relevant workers and payment of minimum automatic enrolment contributions. The Pensions Regulator has been targeting employers who fail to fulfil their workplace pension duties.

DEFINED BENEFIT

Consultation on DB funding draft regulations and new funding code

The DWP has published a consultation seeking views on the draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023. These set out the detail of the new requirements in the Pensions Act 2004, inserted by the Pension Schemes Act 2021, for DB pension schemes to have a funding and investment strategy and submit a statement of strategy to The Pensions Regulator. The consultation also invites comments on proposals to amend the Occupational Pension Schemes (Scheme Funding) Regulations 2005 and details of the new requirement for DB schemes to appoint a Chair where they do not already have one.

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The Pensions Regulator (TPR) has published its draft funding code of practice for defined benefit (DB) pensions schemes and a consultation document. The consultation sets out that schemes will be expected to set a long-term objective and a journey plan to get there. It is expected that schemes will reduce reliance on their sponsoring employer as they reach maturity. It will require trustees to improve risk management and raise the bar for evidencing supportable risk taking. A new twin track regulatory approach will help TPR filter out schemes that require minimal engagement (estimated to be around half of schemes, as at March 2021), and identify and intervene when there are concerns schemes are not complying with regulations.

The final regulations and code are currently planned to come into force in October 2023.

Action
The changes will apply only to valuations with an effective date after the new requirements come into force. Nevertheless, employers and trustees should consider the potential impact of the new regime at an early stage.

DEFINED CONTRIBUTION

'VfM' assessments and reporting of net investment returns

For DC schemes with assets of less than £100 million, a new value for members (VfM) assessment requirement applies for the first scheme year which ends on or after 1 December 2022. For all schemes, the requirement to publish net investment returns applies in relation to the first scheme year which ends after 1 October 2021.

Simpler annual benefit statements

A requirement is placed on trustees of occupational pension schemes, which offer money purchase benefits and are used for automatic enrolment, to provide that a statement given to members informing them of their pension savings must not exceed one double-sided sheet of A4-sized paper when printed, and the equivalent if printed from an online statement. These Regulations came into force on 1 October 2022. The DWP has published new statutory guidance to assist pension scheme trustees in complying with the new requirements.

'Stronger nudge' to pensions guidance and final regulations

The DWP published its response to the July 2021 consultation on draft regulations for delivering a 'stronger nudge' to pensions guidance when individuals seek to access, or transfer for the purpose of accessing, flexible (DC) benefits, including additional voluntary contributions (AVCs), in occupational pension schemes.

The Occupational and Personal Pension Schemes (Disclosure of Information) (Requirements to Refer Members to Guidance etc) (Amendment) Regulations 2022, SI 2022/30, have been published and are now in force. These make amendments to regulations governing the disclosure requirements for occupational and personal pension schemes. They place new requirements on trustees of schemes with DC benefits to ensure relevant beneficiaries are referred to appropriate pensions guidance, provided by the Money and Pensions Service.

The Occupational Pension Schemes (Collective Money Purchase Schemes) Regulations 2022

These regulations, SI 2022/255, implement the new authorisation and supervisory regime for collective money purchase schemes. They will enable single or connected employer collective money purchase schemes to apply for authorisation to operate in Great Britain.

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Action
For scheme year ends after 31 December 2021, ensure compliance with the new VfM requirements and build this into processes for Chair Statements. Trustees should also ensure that, where applicable, their schemes comply with the new requirements for simpler annual benefits statements and 'nudging' members to pensions guidance. For noting, a consultation is expected, by the end of 2022, on collective money purchase schemes for non-associated employers.

GUARANTEED MINIMUM PENSIONS (GMPS) AND GMP EQUALISATION

Pension Schemes (Conversion of Guaranteed Minimum Pensions) Act 2022

Parliament has published the Pension Schemes (Conversion of Guaranteed Minimum Pensions) Act 2022, following its Royal Assent on 28 April 2022. The Act amends provisions in the Pension Schemes Act 1993 and the Pensions Act 2007 in order to help occupational pension schemes to convert Guaranteed Minimum Pension (GMP) benefits into other scheme benefits. It does this by clarifying that the legislation applies to the survivors of those who earned the GMP and by removing the requirement to notify HMRC of every individual whose benefits are being converted. Some provisions are though subject to regulations, which have not yet been published.

HMRC publishes third GMP equalisation newsletter

HMRC has published a Guaranteed Minimum Pension (GMP) equalisation newsletter, which contains information on corrective action in relation to past transfer payments and also conversion of GMPs.

GMP revaluation

The DWP has published the Government's response to its consultation on the Guaranteed Minimum Pension (GMP) fixed rate revaluation. The response confirms that the fixed rate of revaluation of GMP for early leavers is reduced from 3.5% to 3.25% per annum from 6 April 2022.

The Occupational Pension Schemes (Schemes that were Contracted-out) (No 2) (Amendment) Regulations 2022 were laid in Parliament following this review.

Action
Schemes with GMPs accrued between 1990 and 1997 should now be making progress to address inequalities arising from those GMPs. The Pensions Regulator has GMP equalisation on its radar. At some point, it may even ask schemes for updates through the pension scheme return.

INDEXATION

Consultation outcome on government reform of RPI updated

HM Treasury has updated the consultation outcome for the consultation on reform to the Retail Prices Index (RPI) methodology. The update reflects a High Court judgment on 1 September 2022, which rejected a judicial review claim over plans to replace RPI with a version of the Consumer Prices Index (CPIH) from 2030. The judicial review claim was brought by the trustees of BT, Ford and Marks and Spencer pension schemes who claimed that the change was unlawful and would leave millions of pensioners worse off. As things stand, the reform will go ahead as planned.

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Action

The impact of this change on defined benefit pension scheme sponsors, trustees and members will depend, and scheme specific advice should be sought.

INVESTMENT

Climate Change and Governance requirements

New trustee climate change risk governance and reporting duties introduced under the Pension Schemes Act 2021 started to apply to the trustees of schemes with assets of £5 billion or more and of master trusts from 1 October 2021. From 1 October 2022, they also apply to the trustees of schemes with assets of £1 billion or more.

Paris Alignment and new guidance on SIPs and Implementation Statements

From 1 October 2022, pension schemes within scope are required to measure and publish how their investments support the Paris Agreement climate goal of limiting global warming to 1.5 degrees Celsius above pre-industrial levels. The Government suggests that the new measures will mean that from October more than 80% of UK pension scheme members will be invested in pension schemes subject to these new rules. Regulations amend the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021, from 1 October 2022 and apply to trustees of trust schemes with relevant assets of £1billion or more on their first scheme year end date to fall on or after 1st March 2021.

DWP has also finalised its statutory and non-statutory guidance for trustees of all schemes to help them understand and consider financially material Environmental, Social and Governance (ESG) factors and stewardship approaches in their investment decision making. The statutory guidance applies to Implementation Statements for any scheme year ending on or after 1 October 2022. The non-statutory guidance focusses on stewardship reporting in Statements of Investment Principles (SIPs) and applies from 17 June 2022. Interestingly, the final guidance confirms that The Pensions Regulator (as opposed to pension scheme members) is the primary audience for the SIP and IS, but member facing summaries of these documents are encouraged.

CMA Order transposed into regulations with Pensions Regulator oversight

The Occupational Pension Schemes (Governance and Registration) (Amendment) Regulations 2022, SI 2022/825, have been made in order to transpose, into pensions legislation, Parts 3 and 7, and related provisions of Parts 9-11, of the Investment Consultancy and Fiduciary Management Market Investigation Order 2019 made by the Competition and Markets Authority (CMA) on 10 June 2019 ('the CMA Order'). The new regulations came into force on 1 October 2022. (See, further, 'The Pensions Regulator', below.)

Action

Schemes in scope should ensure compliance with the CMA Order changes and new climate change governance and reporting requirements. Also, a watching brief should be kept on environment, social and governance (ESG) developments. Trustees of schemes that need to produce a Statement of Investment Principles (SIP) or Implementation Statement (IS) should take into consideration the best practice guidance when reviewing or revising their SIPs and ISs.

PENSION PROTECTION FUND

2023/24 levy rules

The PPF has published its final levy rules for 2023/24 following its consultation in September. In a Policy Statement, the PPF confirmed that its levy estimate will be £200m for 2023/24 which is around half of last year's estimate. The PPF also confirmed that its levy methodology changes will go ahead; the increments between the levy bands will be halved and there will be a reduction in both the levy scaling

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factor by 23% and the scheme-based levy multiplier by 10%.

Government pushes ahead with proposal to increase FCF levy

The DWP has published its response to the consultation on the review of the fraud compensation levy (FCL) ceiling, announcing that it will push ahead with its proposal to more than double the levy on retirement savings plans as it seeks to cover the rising cost of compensating victims of fraud following the High Court's decision in Board of the Pension Protection Fund v Dalriada Trustees [2020] EWHC 2960 (Ch). In that case, the High Court held that, in principle, members of pension schemes that were set up fraudulently should be able to receive pay-outs from the Fraud Compensation Fund (FCF). The Occupational Pension Schemes (Fraud Compensation Levy) (Amendment) Regulations 2022, SI 2022/259 were subsequently laid before Parliament on 10 March 2022 to implement this FCL increase with effect from 1 April 2022.

The FCL is currently fixed at a maximum charge of 75 pence per member per year, which pension plans must pay. This cap will increase to £1.80 per member from 1 April 2022 in an attempt to cover the increased costs of paying compensation to victims of fraud. The DWP's decision could add £5m to the bill for the country's largest retirement savings plans.

The FCF is administered by the PPF.

Action
Changes to levies should be considered and budgeted for. Where appropriate, steps to reduce the PPF risk-based levy should be implemented by relevant deadline(s).

TAX

Autumn Statement 2022: Pensions-related announcements

The triple lock on the State Pension will be retained; so, the State Pension will increase by 10.1% in April 2023. The Secretary of State for Work and Pensions will publish the Government's latest Review of the State Pension age early in 2023.

No changes have been proposed to the annual and lifetime allowances, but there are some changes to income tax which will have indirect implications for pensions tax relief: the personal allowance was already frozen until April 2026 and this will now be extended until April 2028; and the threshold for the 45% tax band will be lowered from £150,000 to £125,140 from 6 April 2023.

The Employers NICs threshold will be frozen until April 2028.

HM Treasury also published the outcome of its consultation on its review of Solvency II, setting out the government's final reform package for a new Solvency UK regime following Brexit. The package includes cutting the risk margin significantly, maintaining the existing methodology and calibration of the fundamental spread while allowing for the use of notched ratings, and reforming eligibility rules for the matching adjustments.

Migration from PSO to MPSS

For HMRC information and reporting purposes, registered pension schemes are largely managed online by 'Scheme Administrators' (usually, the statutory Administrators are the scheme trustees but trustees can also authorise their third-party administrators as 'practitioners' to act on their behalf).

There are currently two platforms used by pension schemes – Pension Schemes Online (PSO) and Managing Pension Schemes Service (MPSS), which was introduced in 2018. Pension schemes currently on PSO must be migrated to MPSS so that schemes can continue to report and account for tax charges, and avoid penalties for non or late payment. Scheme Administrators must initiate the migration.

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Action

The Autumn Statement is largely for noting. Action is, however, required on the migration from PSO to MPSS; otherwise, pension schemes will not be able to report and account for any tax due and may, in consequence, incur interest and late payment penalties. Trustees should ensure that their scheme is on the MPSS platform.

THE PENSIONS REGULATOR

Single code of practice

The Pension Regulator's (TPR's) 15 existing codes of practice are set to be transformed into a new online code, which is intended to provide "one up-to-date and consistent source of information on scheme governance and management". The new code, expected to be published by end of 2022 / start of 2023, will consist of 51 shorter, topic-based modules.

The new code will incorporate changes introduced by the Occupational Pension Schemes (Governance) (Amendment) Regulations 2018. These relate to "effective systems of governance" (ESoG) and the "own risk assessment" (ORA).

All trustees of an occupational pension scheme must, under section 249A of the Pensions Act 2004, establish and operate an ESoG, including 'internal controls'. That system should be proportionate to the size, nature, scale and complexity of the activities of the scheme and applies in addition to any other governance obligation under legislation, scheme rules or otherwise. In addition, the trustees of a scheme with 100 members or more must also carry out and document an ORA of their scheme; i.e. carry out and document how well their governance systems are working and the way potential risks are managed.

2022 Annual Funding Statement (AFS)

AFS 2022 is particularly relevant to trustees approaching 'Tranche 17 valuations' and recognises the pressures (e.g. the economic background) and uncertainties (e.g. Ukraine) that trustees are facing, and the potential impact of this on their pension scheme funding and employer covenant. TPR nevertheless expects trustees to "remain alert", to think about their long-term funding target and journey towards it and to consider risks in an integrated way.

Importantly each scheme is expected to "consider its position depending on its own circumstances".

This year's AFS, as with AFS 2021, is accompanied by helpful tables setting out key risks that TPR expects trustees and employers to focus on, and actions to take, depending on the scheme's funding strength, maturity, and strength of the employer covenant.

The tables are the same as last year, except the reference to the length of the recovery plan has been updated to six years (to reflect that recovery plan lengths have decreased over recent years and the average is now less than six years across all valuation tranches).

Revised guidance for fiduciary management (FM) services and investment consultants (CMA Order)

TPR has published updated guidance for the tender process for fiduciary management services and for trustees setting objectives for their investment consultants. Currently, investment consultancy services must abide by the Investment Consultancy and Fiduciary Management Market Investigation Order 2019 (the CMA order).

The updated guidance reflects the requirements of The Occupational Pension Schemes (Governance and Registration) (Amendment) Regulations 2022 (SI 2022/825) which transposes the CMA Order into pensions law with effect from 1 October 2022.

TPR, FCA and MaPS warn against heightened risk of pension scams

TPR, the Financial Conduct Authority (FCA) and the Money and Pensions Service (MaPS) have issued a warning to pension scheme trustees and savers regarding the risk of scammers in light of increased economic hardship.

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The warning was issued as a result of concerns that savers may perceive risks to their retirement pots and make rushed financial decisions, rendering them vulnerable to exploitative malefactors seeking to take advantage of their vulnerability.

Guidance statement on expectations for the use of LDI funds

In response to statements made by the National Competent Authorities (NCAs) on the resilience of Liability-Driven Investments (LDI) funds, the Pensions Regulator (TPR) has issued its own guidance statement calling on scheme trustees who use LDI to maintain an appropriate level of resilience in leveraged arrangements to better withstand a fast and significant rise in bond yields.

If trustees depart from the liquidity buffer set out by the NCAs, TPR expects trustees to:

- work with their advisers to demonstrate the buffer the scheme has in place
- complete a risk assessment of how the scheme will respond to stressed market events so that the scheme remains resilient during these events, including how it will raise liquidity—taking into account that the ability to sell assets in such conditions may be greatly impaired
- detail a step-by-step plan for bringing the scheme to higher levels of resilience in the event of volatility returning to the market, noting any assumptions in respect of market conditions, operational arrangements and timescales that the plan is based on, and
- document these arrangements and review regularly.

The statement also calls on trustees investing in leveraged LDI to improve their scheme's operational governance.

Action
Trustees should discuss with service providers how they will comply with the ESoG and, if applicable, ORA requirements, noting the first ORA must be undertaken with a year of the single code coming into force. Schemes using FM services and investment consultants should ensure compliance with the new regulations and will need to report on it in scheme returns. Consideration should be given to a member communication on pension scams, reminding members to be extra vigilant in uncertain economic times. Trustees of schemes using LDI strategies should be discussing the impact of recent events and subsequent TPR guidance with their investment advisers.

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5 Scheme Returns

It's that time of year again where Trustees of defined benefit / hybrid pension schemes have to submit scheme information to The Pensions Regulator as part of the annual Scheme Return process.

The Scheme Return has been evolving in recent years and 2023 is no different with a number of changes in comparison to previous years.

The relevant deadlines, along with changes to this year's return, are set out below. Information must be provided within prescribed timescales; so, trustees should ensure that they and their advisers are ready to supply this information and that Scheme Returns are completed on time.

WHAT IS REQUIRED?

In line with previous years, Trustees will have to complete the Part 1 and Part 2 return. Both will be emailed to Trustees separately.

WHAT ARE THE DEADLINES?

Trustees can expect to start receiving notices at the beginning of February, with submissions by 31 March 2023.

WHAT ARE THE CHANGES THIS YEAR?

A tiered system for asset information. Schemes with less than £30m in assets are allocated to Tier 1 and can submit simplified asset information. Schemes with assets from £30m up to £1.5m are in Tier 2, labelled the 'standard' tier – this requires more detailed reporting on bond and equity holdings. Schemes with assets greater than £1.5m have more complex reporting requirements including risk factor stresses.

A number of asset categories have also been removed in comparison to previous years.

We are also expecting Scheme Returns to ask information about fiduciary management and investment consultancy services used by pension schemes but, so far, the Regulator's website makes no reference to any changes to the Scheme Return in this regard.

WHAT SHOULD TRUSTEES THINK ABOUT?

Completion of the Scheme Return is mandatory, and the information contained in it will be used to calculate the PPF levy. Trustees should ensure that it is accurate and up to date. In particular, the asset breakdown should reflect hedging strategies to ensure that credit is given in the stress calculations for low risk investments.

Trustee should also consider whether it is appropriate to submit a new s179 valuation for calculation of the levy.

https://www.thepensionsregulator.gov.uk/en/trustees/submit-reports-payments-and-requests-to-us/scheme-return/db-and-mixed-benefit-scheme-return

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6 PPF publishes final levy rules for 2023/24

Key Points

- £200 million levy estimate for 2023/24, down from £390m in 2022/23.
- 98% of schemes expected to pay less levy in 2023/24 than this year.
- The majority of schemes that pay a risk-based levy can expect it to fall by more than half.
- Proposals to significantly reduce volatility in levies and to incorporate new asset class information will go ahead as planned.
- Recent market movements will not impact funding strategy or proposed asset stresses, which take a long-term view of risk and are not guided by short term volatility.

Following an earlier consultation, the Pension Protection Fund (PPF) has announced its final levy rules for 2023/24, almost halving the levy estimate for next year, which is expected to result in almost all schemes paying less levy.

The changes will cut the levy to around £200 million for 2023/24, down from £620m in 2020/21 and £390m for this current year.

The PPF confirms that they will go ahead with proposals to reduce the increments between levy bands to significantly reduce volatility in levies, and to cut the risk-based levy scaling factor by 23 per cent and the scheme-based levy multiplier by 10 per cent. The consultation also contained proposals to integrate into the levy the new asset class information being collected by TPR in 2023.

The PPF's consultation also sought views on priorities for developing the levy methodology in the longer term, on the basis the PPF expects the levy to substantially reduce over time. The majority of respondents were supportive of the proposed direction of travel and provided a range of comments that will inform the PPF's future approach. In response, the policy statement emphasises that the PPF remains committed to ensuring the risk-based levy is risk-reflective, so that schemes with weaker sponsors continue to pay more per pound of underfunding.

The headlines, taken from the Policy Statement, are:

Levy estimate
We confirm the levy estimate is £200m.

Levy parameters
The Levy Scaling Factor ('LSF') and Scheme-Based Levy Multiplier are confirmed as 0.37 and 0.000019 respectively, and the risk-based levy cap at 0.25 per cent of scheme liabilities.

Measures introduced in 2021/22 to support schemes through the pandemic with flexibility on payment terms stay in place.

Insolvency risk
We are confirming the proposed change to the levy rates for levy bands 2 to 10, halving the band-to-band increase in the levy rate (as set out in the Insolvency Risk Appendix)

Asset stresses
We are confirming the asset and liability stresses set out in the consultation document.

Dun & Bradstreet scores
For the 2023/24 levy year, we'll be using insolvency risk scores produced by our insolvency risk partner Dun & Bradstreet starting in April 2022.

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KEY DATES FOR 2023/ 24

Item	Key Dates and Times
Scheme returns and electronic contingent asset certificates to TPR	31 March 2023 - Midnight
ABC certificates and special category applications to PPF	31 March 2023 - Midnight
Start of 2023/24 levy year	01 April 2023
Send contingent asset documents to PPF	03 April 2023 - 5.00pm
Defecit-reduction contributions certificates to TPR	28 April 2023 - 5.00pm
Send exempt transfers with TPR	28 April 2023 - 5.00pm
Certify full block transfers with TPR	30 June 2023 - 5.00pm
Publication of Mean Scores	July 2023
Invoicing starts	Autumn 2023

Helpful Links

Determination_Levy_Rules_2324 (ppf.co.uk)

Policy statement - Dec 2022 (ppf.co.uk)

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7 Pensions Ombudsman Determinations

Ombudsman order scheme to reinstate pensions scam victim following poor due diligence

In this case (PO-26616), Mrs G complained that Teachers Pensions (TP) did not conduct sufficient due diligence checks when transferring her pension benefits from the Teachers Pension Scheme (TPS) to the London Quantum Pension Scheme (the LQPS). Mrs G is unable to access her benefits from the LQPS.

The Ombudsman upheld the complaint because TPS failed to put in place proper processes to conduct adequate checks and enquiries in relation to the LQPS and warn Mrs G of the potential consequences of transferring. He determined, on the balance of probability that, but for TP's maladministration, Mrs G would not have proceeded with the transfer. As a result, Mrs G suffered the loss of her benefits within the TPS.

To put matters right he directed that TP reinstate Mrs G's accrued benefits in the TPS accounting for any revaluation that would have taken place since the transfer. He also awarded £1,000 for distress and inconvenience. Specific failings identified by the Pensions Ombudsman included –

TP claiming Mrs G had a statutory right to transfer when she did not (because she did not complete her application form within three months of receiving the statement of entitlement).

Even if TP did believe it was under a statutory duty to affect the transfer, it was still under an obligation to carry out sufficient due diligence but did not do so because:

There was insufficient checks as to Mrs G's status as an 'earner' for the purpose of section 95 of the Pension Schemes Act 1993 (if a member was not employed then they cannot be an earner for the purpose of acquiring transfer credits in the receiving occupational pension scheme)

Based on the evidence, it was not reasonable for TP to conclude that Mrs G was receiving regulated advice about the benefits of transferring from TPS to LQPS

Warnings about scams and fraud were deficient

TP should have engaged with Mrs G to find out more about the transfer.

TP also contended that the transfer request had been dealt with quickly because it had been criticised in the past for delays. In response, the Ombudsman stated that there is a "difference between being dilatory and being diligent" and that "I do not consider that a desire to avoid criticism … excuses TPs actions".

This very comprehensive (30-page) determination is a salutary reminder of the importance of conducting proper due diligence on transfer requests based on all prevailing regulations and guidance at the time of the request (in this case, the transfer took place in 2015).

The current position with the LQPS is that the independent trustee, Dalriada Trustees Limited, appointed by the Pensions Regulator, is trying to reconcile the remaining assets and establish the funds, if any, that might be able to be returned to scheme members. The Ombudsman therefore also directed that:

Should Dalriada manage to retrieve some or all of Mrs G's pension fund for her benefit and provide TP with satisfactory evidence that has happened, TP shall be entitled to recover that amount from Mrs G.

Should Mrs G make a successful application for compensation from the FSCS, she shall disclose to TP the sum she receives and TP shall be entitled to recover that sum from Mrs G.

https://www.pensions-ombudsman.org.uk/sites/default/files/decisions/PO-26616.pdf

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8 DC Update

BENEFIT STATEMENTS / ILLUSTRATIONS

The Financial Reporting Council (FRC) has announced changes to the Actuarial Standard Technical Memorandum 1 (AS TM1) to support consistent and reliable pension illustrations for defined contribution pension scheme members.

The changes to AS TM1 ('version 5.0') include standardising the accumulation rate assumptions and the form of annuitisation at retirement. According to the FRC, the new standard is a major step change to increase consistency between pension projections once they start to be provided to pensions dashboards from October 2023 (see our separate article on dashboards).

AS TM1 will continue to apply to the Statutory Money Purchase Illustration (SMPI) statements that individuals receive each year. In addition, the DWP intends for AS TM1 to determine the illustrations of defined contribution pensions shown on pensions dashboards, from October 2023.

The current version of AS TM1 ('version 4.2') will remain in force for SMPIs produced between 6 April 2023 and 1 October 2023.

GOVERNMENT UNVEILS 'EDINBURGH REFORMS' OF FINANCIAL SERVICES

The chancellor of the exchequer, Jeremy Hunt, has announced a package of proposed measures for UK financial services, collectively termed the Edinburgh Reforms, which include reforms to the bank ring-fencing regime, the securitisation regime, the Building Societies Act 1986, the prospectus regime, and first steps towards reforming the Short-Selling Regulation and the Consumer Credit Act. The reforms include plans to lay regulations to reform the DC pensions charge cap in early 2023, and plans to increase the pace of DC pension consolidation.

DWP CONSULTATION ON PERFORMANCE FEE EXEMPTION FROM CHARGE CAP AND NEW INVESTMENT DISCLOSURES

The DWP has launched a consultation - 'Broadening the investment opportunities of DC pension schemes' which:

- includes the government's response to Chapter 2 of the March 2022 consultation on Facilitating Investment in illiquid assets, concerning proposals relating to 'disclose and explain' policy proposals
- proposes amendments to requirements relating to the default SIP (Statement of Investment Principles) to ensure that relevant DC schemes disclose and explain their policy on illiquid investments in respect of default arrangements
- proposes to require relevant DC schemes to publicly disclose and explain the percentage of assets in the default funds allocated to different asset classes in their annual chair's statement
- proposes to enable trustees to exempt performance-based fees from their charge cap calculations where they feel this in their members' best interests.

Helpful Links

News I Financial Reporting Council (frc.org.uk)

Financial Services: The Edinburgh Reforms - GOV.UK (www.gov.uk)

Broadening the investment opportunities of defined contribution pension schemes - GOV.UK (www.gov.uk)

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9 Autumn Statement

The triple lock on the State Pension will be retained; so, the State Pension will increase by 10.1% in April 2023. Pension Credit will also increase in line with inflation from April 2023 (rather than in line with average earnings growth). The Secretary of State for Work and Pensions will publish the Government's latest Review of the State Pension age early in 2023. Sadly, for most defined benefit pensioners, they will suffer an effective real cut of ~7% since most pension inflation uplifts are capped significantly below the level of inflation.

No changes have been proposed to the annual and lifetime allowances, but there are some changes to income tax which will have indirect implications for pensions tax relief: the personal allowance was already frozen until April 2026 and this will now be extended until April 2028; and the threshold for the 45% tax band will be lowered from £150,000 to £125,140 from 6 April 2023.

The National Living Wage will increase next year by 9.7% to £10.42 per hour from April for those aged 23 and over.

The Employers NICs threshold will be frozen until April 2028.

HM Treasury published in November the outcome of its consultation on its review of Solvency II, setting out the government's final reform package for a new Solvency UK regime following Brexit. The package includes reducing capital requirements (by cutting the risk margin) and allowing assets into the matching asset portfolio which would not have qualified previously. The capital released is intended to provide funding to "UK Growth plc", although HMG admits that this aim may well not be achieved. That the insurance industry was keen for these changes might suggest that it is not so good for policyholders (aka pensioners). At the same time, the Prudential Regulation Authority has published feedback statement FS1/22 with a summary of responses received to discussion paper DP2/22 on potential reforms to risk margin and matching adjustment within Solvency II.

On a related note, the Office for Budget Responsibility has published the latest Economic and Fiscal Outlook, which sets out a central economic and fiscal forecast to 2027–28, taking account of recent data and Government policies announced since March, up to and including the Autumn Statement. Welfare spending is £19.0bn (6.5%) a year higher on average between 2023–24 and 2026–27 relative to the March forecast. In 2026–27 alone, welfare spending is up £14.0bn (6.5%). £8.4bn of that is due to the effects of higher inflation, which raises spending via uprating. Three-quarters of this upward revision is the result of the 10.1% rise in most pensioner and working-age benefits in 2023–24 thanks to outturn CPI inflation in September 2022 being much higher than the forecast in March.

Helpful Links

Solvency II Review: Consultation - GOV.UK (www.gov.uk)

Autumn Statement 2022 - GOV.UK (www.gov.uk)

Economic and fiscal outlook - November 2022 - Office for Budget Responsibility (obr.uk)

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10 The Purple Book 2022

The Pension Protection Fund (PPF) has published The Purple Book 2022, now in its 17th edition, which details the further improvement in the net funding levels of UK Defined Benefit (DB) schemes.

The Purple Book aims to provide the most comprehensive overview of the risk posed by the 5,131 DB schemes which are eligible for PPF compensation. The data for this year's edition includes 9.6 million DB scheme members; down from 9.7 million in the previous year. Of these:

- 43% are pensioner members;
- 47% are deferred members; and
- 10% are active members.

The number of active members has reduced by 5% in comparison to the previous year. On a related point, the proportion of schemes that are closed to new benefit accrual has increased from 48 per cent in 2021 to 51 per cent in 2022. This now means that for the first time we have more schemes that provide no form of accrual of benefits than those that do.

Schemes with more than 5,000 members make up almost 75 per cent of each of total assets, liabilities, and members, while only forming seven per cent of the total number of schemes in The Purple Book 2022 dataset. Conversely, schemes with fewer than 1,000 members make up 80 per cent of the total number of schemes but only around 10 per cent of total assets, liabilities and members.

The overall net funding position of DB schemes improved to a surplus of £193bn in the year to 31 March 2022. The total funding ratio increased to 113.1% from 102.8% in the previous year, which was mainly the result of market movements. The year to 31 March 2022 also witnessed the largest-ever annual fall in liabilities within the universe of DB schemes, with total section 179 liabilities falling by almost 12% and buyout liabilities falling by nearly 10%.

The number of DB schemes in deficit increased from 709 to 746, with the deficit of the schemes in deficit also increasing from £4.7bn at the end of October to £5.8bn at the end of November.

The number of schemes in surplus decreased to 4,385 despite the total surplus of schemes in surplus increasing to £377.3bn.

With more schemes closing to future accrual and therefore accelerating their maturity, total annual recovery plan payments, based upon current recovery plans in place, are indicated to decrease by around 88 per cent over the next 10 years, from around £12.3 billion in 2022 to around £1.4 billion in 2032, as schemes increasingly become fully funded on a Technical Provisions basis.

Despite the wider economic turbulence in recent times, DB schemes are, on the whole, continuing to improve their funding positions, reduce the risk of PPF entry and, most importantly, increase the likelihood of members receiving their full benefits as they fall due.

The Purple Book 2022 | Pension Protection Fund (ppf.co.uk)

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11 Coming Up Next

And… breathe.

Another year has flown by in the blink of an eye. We've witnessed war in Europe. Winced at eye-watering inflation. Waved fair well – and welcome – to prime minister after prime minster. Wilted in record-breaking heatwaves. Withstood record-breaking wintery weather. And, we even have ourselves a new monarch.

Thinking back at the year that was, one could be forgiven for forgetting what else we'd managed to get done. 2022 brought its challenges in the pensions industry too, with unprecedented financial movements shaking the system to its core – not least the LDI crisis. Members. Trustees. Investment managers. Employers. No one had an easy ride in 2022; but we all made it. We got on with it. We rolled with the punches and rolled our sleeves up. If there was one word to sum up 2022, in this writer's mind, it would be… 'resilience'.

The trials of 2022 will stand us in good stead as we race into 2023 and the new challenges that await. Just like the year passed, there will be some challenges that we won't see coming. But we know we are resilient and have the capacity to meet those tasks head on.

Thankfully, we can see the majority of the challenges ahead of us already and can make sure that we are suitably prepared. Planning for the things we can see and can predict, leaves us ready and agile to react to any unforeseen crisis that may pop up along the way.

So, as ever, we end the Quarterly Report by offering up a brief summary of those near-future events that we can see coming and that we think you should prepare for.

NEW DB SCHEME FUNDING CODE

- TPR has published its draft funding code of practice for DB pension schemes and a related consultation, with the primary focus being on schemes setting their long-term objective and a journey plan of how to get there. The new regime expects schemes to reduce reliance on the sponsoring employer as they reach maturity, with assessments of the employer covenant being a key underpin for the risk that can be supported on the journey. Trustees will be expected to manage risk and document risk-taking decisions, while setting their scheme's funding assumptions in line with those risks and the stage of the journey plan.
- In terms of TPR intervention and enforcement of the new funding requirements, a new twin-track regulatory regime will be implemented. TPR intends to filter out schemes that require minimal engagement (estimated to be around 50% of schemes, as at March 2021) and intervene when there are concerns about schemes being non-compliant with the regulations.
- The final Code and regulations should come into force in October 2023, for schemes with triennial valuations effected after that date.

TPR CODES OF PRACTICE

- Whisper this, as we don't want to scare it away, but we expect TPR's long-awaited Single Code of Practice to be laid before Parliament imminently – perhaps by the time you are reading this!
- Eventually combining the 15 current codes of practice into a single, "super-code", this will bring the much discussed effective systems of governance (ESoG) and own-risk assessments (ORA) to the fore, with the latter needing to be completed, for schemes with more than 100 members, within 12 months of the Code coming into force. If trustees haven't started preparing for the Code, now is the time to begin reviewing the requirements and getting the necessary actions on their scheme's project plan for the year.

Building on those selected topics, here are some key dates to keep in your diary as we kick on through 2023:

- **From 2023 onwards** – More information on assets to be collected by TPR in scheme returns for DB pension schemes.
- **January 2023** – The new Revaluation Orders came into force on 1 January 2023.

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- **January 2023** – Consultation due to be published on new proposals for Value for Money assessments for DC schemes.
- **16 January 2023** – Dominic Harris due to take up his role as the new Pensions Ombudsman.
- **February/March 2023** – DB schemes returns will be issued from 1 February, to be completed by 31 March 2023.
- **Q1 of 2023** – an updated Practitioners' Guide for the new Conditions for Transfer Regulations, to help combat pension scams, is expected.
- **Q1 of 2023** – a consultation on Collective Defined Contribution Schemes for non-associated employers to be issued.
- **April 2023** – Revisions to the 'notifiable events' that must be reported to TPR come into force, as well as new Declarations of Intent.
- **Q2 of 2023** – DWP is expected to undertake a review and publish a report into the Conditions for Transfer Regulations (which came into force in November 2021).
- **31 August 2023** – Start of the phased compulsory on-boarding of schemes to the pensions dashboard, beginning with the largest pension schemes and master trusts.
- **1 October 2023** – New 'AS TM1' assumptions for money-purchase illustrations.
- **October 2023** – the new DB scheme funding rules come into force for schemes with effective dates from October 2023.

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