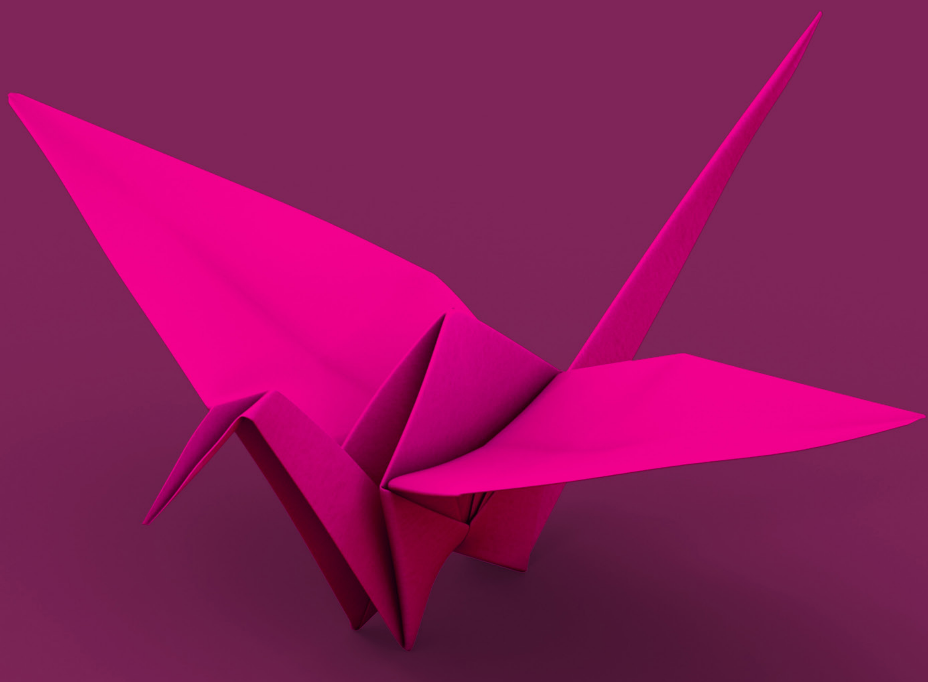
Your Quarterly Pensions Update

Dalriada Trustees – Industry Changes

Quarter Four 2023



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Contents

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.

1 Autumn Statement 2023 – What it means for pensions

Jeremy Hunt, the Chancellor, delivered his Autumn Statement on 22 November. The key measures can be summarised as further consolidation and trustees needing to do more, together with several announcements in connection with the **pensions and growth agenda**, intending to aid the UK economy and reverse the 40% reduction of new companies listing in the UK since 2008.

The **pensions and growth agenda**, including productive finance, is expected to include the prioritising of long-term pension investment performance over low fees, reversing the 23 year Value for Money (VfM) focus on charges when Stakeholder was first introduced in 2001. This is likely to be an important development for DC trustees.

DC trustees also need to note the proposals placing duties on them to offer decumulation services. Until now the vast majority of DC trustees will have focussed on the accumulation only and will have had little involvement in decumulation or the transitional period between the two. If the proposals are carried, DC trustees are likely to have a sizable 'TKU' requirement in this area.

For trustees and sponsors of schemes making contributions via salary sacrifice, the National insurance cut by 2 percentage points from 12% to 10% on 6 January is a good opportunity for member engagement, to nudge members to review their pension savings.

On the DB side, for trustees of "schemes unattractive to commercial providers", it may be advantageous to pro-actively review the consolidators in 2024 as part of your Business Plan. The DWP is to launch a consultation on options for smaller DB schemes, which they say are currently unserved by the market, to consolidate into a new statutory vehicle run by PPF. The direction of travel could therefore be the PPF consolidator or one of your own choice. At this stage it is not clear what part of the market might be considered commercially unattractive (in terms of scheme size/total assets), but important to remember that small schemes are typically considered to be those of less than £100m in assets.

Also, importantly for Trustees, TPR will put into place a **register** to help improve communication and guidance to trustees and to assess whether knowledge requirements are being met and will review its **trustee toolkit** so that it better aligns with the codes of practice and guidance. And with the General Code now having been published, TPR has been clear that schemes not meeting the code's expectations should take action to improve their scheme's governance or consider consolidation. At the very least, trustees need to be aware of where they fall short of TPR's expectations and have clear and realistic plans in place to address those shortcomings.

The Autumn Statement in detail: -

- To provide better outcomes for savers the government is:
  - introducing the multiple default consolidator model for defined contribution (DC) schemes, to enable a small number of authorised schemes to act as a consolidator for eligible pension pots under £1,000
  - launching a call for evidence for DC schemes on a lifetime provider model to simplify the pensions market by allowing individuals to move towards having one pension pot for life, and on a potential expanded role for Collective DC (CDC) schemes in future
  - publishing an update that proposes placing duties on DC occupational pensions trustees to offer decumulation services and products at an appropriate quality and price when savers access their pension assets, either themselves or through a partnership arrangement
- To drive a more consolidated pensions market government is:
  - welcoming the current trend of DC pension fund consolidation and expecting to see a market in which the vast majority of savers belong to schemes of £30 billion or larger by 2030
  - welcoming the Financial Conduct Authority (FCA) and the Pensions Regulator (TPR) announcements on next steps towards implementing the Value for Money framework in the DC workplace pensions market
  - publishing a review of the Master Trusts market, 5 years after the 2018 Master Trusts regulations came into force

- consulting this winter on how the Pension Protection Fund can act as a consolidator for defined benefit (DB) schemes unattractive to commercial providers
- confirming a March 2025 deadline for the accelerated consolidation of Local Government Pension Scheme (England and Wales) assets, setting a direction towards fewer pools exceeding £50 billion Assets Under Management, and implementing a 10% allocation ambition for investments in private equity

— To enable pension funds to invest in a diverse portfolio government is:

- consulting this winter on whether changes to rules around when DB scheme surpluses can be repaid, including new mechanisms to protect members, could incentivise investment by well-funded schemes in assets with higher returns
- reducing the authorised surplus payments charge from 35% to 25% from 6 April 2024
- welcoming TPR's announcement that they will implement a register of trustees and update the trustee toolkit
- engaging with industry on proposals to ensure all aspects of the pensions industry are supporting best outcomes for savers, including how to shift employer incentives away from low fees towards long-term pension investment performance
- committing £250 million to 2 successful bidders in the Long-term Investment for Technology and Science (LIFTS) initiative, subject to final agreement
- following positive feedback from industry, confirming its intention to establish a Growth Fund within the British Business Bank (BBB)
- developing a fellowship course targeting mid-career science and technology Venture Capital (VC) investors, similar to the Kauffman Fellowship in the US, to be operational in 2024

In relation to the State pension, this will increase by 8.5% from April 2024 to £221.20 a week; i.e. the government will honour the triple lock "in full".

The Chancellor also announced that employee National insurance will be cut by 2 percentage points from 12% to 10% from 6 January .

Following the Autumn Statement, a number of papers were issued by the DWP and many of the measures could have a material impact on occupational pension schemes. The current state of play is summarised below.

DEFINED CONTRIBUTION (DC) MEASURES

In the context of the long-standing problem of **"small pots"**, a call for evidence is launched on a lifetime provider model that would allow individuals to have contributions paid into their existing pension scheme when they change employer. This is despite the fact that the DWP had previously discounted the 'Lifetime Provider Model'. There is a potential expanded role for collective defined contribution (CDC) schemes in future.

Also, the Government will proceed with plans to introduce the **multiple default consolidator model** to enable a small number of authorised schemes to act as a consolidator for eligible pension pots under £1,000.

There were several announcements in connection with the **pensions and growth agenda**, including the prioritising of long-term pension investment performance over low fees. TPR will provide further information for employers on what factors should be assessed when they are selecting a pension scheme.

The Government has published a review of the Master Trusts market, five years after the 2018 Master Trusts regulations came into force. This looks at market trends and the future of regulation and supervision.

The Government is proposing to place duties on occupational pensions trustees to offer decumulation services and products at an appropriate quality and price when savers access their pension assets, either themselves or through a partnership arrangement.

DEFINED BENEFIT (DB) ISSUES

Despites a mixed reaction from the pensions industry to earlier proposals, the Government will consult on how the Pension Protection Fund (PPF) can act as a consolidator for "schemes unattractive to commercial providers". The DWP will launch a consultation this winter on options for smaller DB schemes, which they say are currently unserved by the market, to consolidate into a new statutory vehicle run by PPF. At this stage it is not clear what part of the market might be considered commercially unattractive (in terms of scheme size/total assets).

Also, there will be a consultation this winter on the appropriate regime under which surpluses can be repaid. This will include new mechanisms to protect members, and whether this could incentivise investment by well-funded schemes in assets with higher returns. The authorised surplus repayment charge will be reduced from 35% to 25% from 6 April 2024. The changes could encourage more schemes to choose run-off as a long-term objective.

Various measures were announced in connection with the Local Government Pension Scheme (see the links, below).

TRUSTEE SKILLS, CAPABILITY AND CULTURE

The DWP published its response to its 'Pension trustee skills, capability and culture: a call for evidence'. TPR will put into place a register to help improve communication and guidance to trustees and to assess whether knowledge requirements are being met. TPR has also strongly encouraged all professional trustees to receive accreditation through the two main accreditors, though have not mandated this.

TPR will review its trustee toolkit so that it better aligns with the codes of practice and guidance. TPR is also planning to release additional guidance (expected by the end of this year) related to trustee investment decision making in alternative assets.

On a different but related note, Laura Trott has left her role as Minister for Pensions, following her appointment as Chief Secretary to the Treasury. Paul Maynard, MP for Blackpool North and Cleveleys, has been named as the new Minister for Pensions, having been appointed as a DWP Parliamentary Under Secretary of State. The Secretary of State for Work and Pensions is Mel Stride, MP.

Helpful Links

Ending the proliferation of deferred small pension pots - GOV.UK (www.gov.uk)

Government response to 'Pension trustee skills, capability and culture: a call for evidence' - GOV.UK (www.gov.uk)

Evolving the regulatory approach to Master Trusts - GOV.UK (www.gov.uk)

Helping savers understand their pension choices: supporting individuals at the point of access - GOV.UK (www.gov.uk)

Options for Defined Benefit schemes: a call for evidence - GOV.UK (www.gov.uk)

Trends in the Defined Contribution trust-based pensions market - GOV.UK (www.gov.uk)

Autumn Statement Pensions Reform 2023 - GOV.UK (www.gov.uk)

2 Looking both ways – 2023/2024

It's my first full week back at work in 2024. And I am sat thinking about the words of Socrates. Life has taken an unexpected turn for someone who usually would only associate Socrates with the film "Bill and Ted's Excellent Adventure".

So – how did I get here?

Socrates, according to Wikipedia, once wrote "I know that I know nothing".

As is always the way at the start of the year, my email inbox has been bombarded with predictions from allcomers within the pensions industry with their views on what to expect over the next 12 months (and beyond). And whilst I'm in no way seeking to compare myself to Socrates, I do find myself going down his line of thinking as regards to what the year will bring.

My wariness of trusting predictions stems from the fact that in January 2020 I attended a whole day's session from one of the world's largest fund managers. The sort of people who you would think have a fairly keen eye for forecasting. The conclusion I took away from that seminar was "it's going to be a pretty quiet year for markets". Yes – so that went well then……

Regardless, I feel it is my job to think through what is going to happen in the next couple of years and the implications for the schemes to which Dalriada is appointed as Trustee. Hence my reading.

For the last 20 years, the stated objective, as agreed with sponsors, for the majority of schemes to which I've been appointed as Trustee, has been to get to buy-out. The "gold standard" of member security provided by an insurance company's covenant and the additional layer of Financial Service Compensation Scheme protection. And, for the employer, getting the scheme off of the Company's balance sheet. Market conditions since the Truss budget have meant that what was once a distance dream has increasingly become a possibility. And the rush for "risk settlement" has started.

An increasingly vocal camp are though starting to challenge that mindset. The combination of the Mansion House Speech, the reduction in the Autumn Budget of the rate of tax on surplus paid to sponsors and the consultation on enabling investment in productive finance has fuelled their fire. Running schemes on COULD in the right circumstances (and with the right legislative backdrop and Regulatory regime) be a very viable attractive alternative.

But this is January 2024. We do not yet have the new Funding Code. We have just received the General Code. We do not yet have Pensions Dashboards. We are in election year. With the way we seem to get through Pensions Ministers, we have limited visibility as to who will be the decision-makers next week let alone who will be in power come the Autumn. Whilst all parties seem to think there is something better out there for the £1.6 trillion of assets in UK funded pensions, the devil is in the detail, and these are politicians – they are very well known for getting the press soundbites, but not exactly details people.

There appears to be, in my opinion, a massive circle to square between the Mansion House speech which talks of investment in the UK, and the messages which the Pensions Regulator has been sharing with us for the past decade about de-risking. And I don't see that particular problem being addressed in the short to medium-term.

So should trustees and sponsors stick or twist?

Run-on and await the promised land, or buy-in/out knowing that in doing so they are potentially handing over to an insurer an anticipated profit margin of upwards of 10%? That's an incredibly challenging question – the answer to which depends on the specifics of the scheme in question, the sponsor's covenant and objectives, and combined view of market developments. And it is a question which often involves material amounts of money. Amounts of money which in many cases could fund ongoing defined contribution sections for over a decade.

I think it is impossible to accurately forecast exactly which way this debate will go. And each scheme's circumstances will be unique. So, for now, in many cases the focus is on getting nimble – being able to react as the developments occur. Paying proper attention to data quality. Efficiently and effectively completing GMP Rectification and Equalisation projects. Thinking about the risk versus reward of illiquid assets. Keeping an eye on market and other developments.

When the mist clears, there will be a need to react. At that point, I don't want to be the Trustee who knows nothing.

3 Regulator guidance updated to tackle cyber threat

The Pensions Regulator (TPR) has revised its Guidance on Cyber Security which now forms part of the General Code published in January 2024.

TPR's latest guidance helps trustees and scheme managers meet their duties to assess the risk, ensure controls are in place, and respond to incidents. The guidance will also be of use to scheme suppliers and advisers.

For the first time, TPR is asking trustees and scheme providers to report significant cyber incidents, so it can build a better picture of the cyber risk facing the industry and its members.

TPR is asking schemes, their advisers and providers to report significant cyber incidents on a voluntary basis, in an open and cooperative way, as soon as reasonably practicable. A significant cyber incident is likely to result in:

- a significant loss of member data
- major disruption to member services
- a negative impact on a number of other pension schemes or pension service providers

The revised guidance covers:

- Ensuring controls are in place, including processes that should form part of an effective system of governance in this area
- Responding to incidents
- Reporting an incident

There is also a comprehensive 'useful links' section with links to information produced by the NCSC; ICO; PLSA and PASA . For ease of reference, this is reproduced below.

Trustees should ensure that their information security policies and procedures are updated in line with current guidelines and market practices.

NATIONAL CYBER SECURITY CENTRE

- Advice & guidance
- Threat reports
- Cyber essentials
- 10 steps to cyber security
- Glossary
- Cyber security check tool - a free online tool which can use to check common vulnerabilities in your public-facing IT

INFORMATION COMMISSIONER'S OFFICE

- Breach response and monitoring
- A guide to data security
- Personal data breaches: a guide
- Information security checklist
- Responding to a cybersecurity incident
- Encryption
- Working from home
- Ransomware and data protection compliance

PLSA

– Cyber risk – made simple guide

PASA

– Cybercrime protection checklist
– Cybercrime guidance

Helpful Links

Cyber security guidance revised to help tackle threat | The Pensions Regulator

4 New insurance bill after Autumn statement – detail of abolition of LTA

Lat year, in Jeremy Hunt's budget speech, it was stated that:

"Some have also asked me to increase the Lifetime Allowance from its £1 million limit. But I have decided not to do that. Instead I will go further and abolish the Lifetime Allowance altogether. It's a pension tax reform that will … incentivise our most experienced and productive workers to stay in work for longer.… and simplify our tax system, taking thousands of people out of the complexity of pension tax."

There are have been a number of developments since then and the policy intent, to abolish the Lifetime Allowance (LTA) from 6 April 2024, remains intact. However, the journey is not yet complete.

To recap –

- On 23 March 2023, HMRC published a LTA Newsletter, in which HMRC invited persons to join a working group.
- The first tranche of implementation legislation is the Finance (No 2) Act 2023. Section 18(1) of that Act provides: "No lifetime allowance charge arises for the tax year 2023-24 or any subsequent tax year". The important word here is "charge". The LTA charge was removed in the 2023/24 tax year, but the LTA, itself, continued to be part of the pensions tax regime and will remain so until the 2024/25 tax year.
- Further, it became clear that, even after 2024/25, there will still be ceilings on tax relievable pension benefits. This is because, in section 19 of the above legislation, provision is made for certain lump sums or parts of lump sums which, disregarding section 18, would have been chargeable to income tax under sections 214 to 226 of Finance Act (FA) 2004, to remain chargeable. The lump sums in question are 'serious ill-health lump sums', 'lifetime allowance excess lump sums', 'defined benefits lump sum death benefits', or 'uncrystallised funds lump sum death benefits'. Under section 19(2), the lump sums, if they would have suffered a lifetime allowance charge, will instead be subject to tax at a marginal rate of income tax under the Income Tax Earnings and Pensions Act (ITEPA) 2003, section 579A. Thus, a charge to tax will be triggered for exceeding an amount equal to the amount of the lifetime allowance, albeit at a lower rate than the current 55% lifetime allowance charge rate.
- On 18 July, HMRC published, along with draft legislation, a policy paper entitled "Abolishing the pensions lifetime allowance". HMRC explained that the legislation abolishes the LTA, but limits –
    - the total amount of tax-free cash / pension commencement lump sum an individual can receive to a maximum of £268,275, unless they hold a valid lifetime allowance or lump sum protection; and
    - the total amount of lump sums - excluding the receipt of regular pension income - an individual can receive before marginal rate taxation applies to £1,073,100 (the most recent level of LTA), unless they hold a valid lifetime allowance protection.
- Then, on 20 December 2023, HMRC published a Lifetime Allowance Guidance Newsletter (which was reissued in January 2024 to correct a minor error) in order to clarify the way that lump sum benefits will be taxed.

We currently await final legislation, presumably to be included in the Finance Act 2024. However, it is envisaged that this will not be materially different from the draft legislation. That legislation is 41 pages long and, inter alia, provides that sections 214 to 226 of the Finance Act 2004 (lifetime allowance charge, including section 218 (definition of lifetime allowance)) are repealed. It also makes provision for an individual's "lump sum allowance". This is expressed in terms which include a definition of "relevant benefit crystallisation event". What this means is that the taking of certain benefits will still be treated as a crystallisation event where a test against a tax relievable allowance will need to be performed. Specifically, the individual's standard lump sum and death benefit allowance is defined as "£1,073,100".

So, in terms of the abolition of the LTA, we are not 'there yet' and, even when we reach the LTA abolition destination on 6 April 2024, lump sums will continue to trigger tax by reference to levels under the LTA regime (albeit at marginal income tax rates rather than LTA rates).

Whilst bearing in mind that we are in an election year and so cannot be certain of the longevity of any aspect of the pensions tax system, the abolition of the LTA is nevertheless only than three months away and the removal of the LTA, which has been a fundamental part of the single tax regime, along with the Annual Allowance (which is not being abolished), will have a material impact on pension scheme administration.

Key issues include –

- For administrations, updates to templates and processes
- For trustees and employers, ensuring there is no unintended increase in liabilities as a result of the LTA abolition (e.g. where members benefits are currently limited to the LTA)
- For employers, reviewing compensation arrangements for high earnings (e.g. use of unapproved arrangements).

5 The First Superfund Transaction – Alternative to Buyout?

A Superfund is a vehicle for Trustees to secure member benefits rather than via the purchase of a bulk annuity policy. A transaction with a Superfund still breaks the link to the sponsoring employer, potentially at a lower cost.

Clara Pensions was the first Superfund to complete The Pensions Regulators assessment process at the end of 2021 and, almost two years later, it completed its first transaction.

The transaction covered 9600 members of the Sears Retail Pension Scheme.

While Clara Pensions' model aims to secure insurance contracts for members eventually, the initial transfer does not require a scheme to be fully funded on a buyout basis. Assets and liabilities are transferred into a separate section within the Clara Pension Trust (in some cases augmented by a one-off final contribution from the Scheme sponsor) alongside a capital buffer provided by Clara themselves.

The assets will then grow over time, with the aim to meet the cost of insurance once the scheme has further matured, plus a return on capital for Clara if the initial transfer assumptions are realised.

The link to the sponsoring employer is broken on transition to Clara.

The additional capital is akin to the additional reserves a bulk annuity provider is expected to hold for prudence. As part of the Sears transaction, £30m of additional capital was provided by Clara.

In certain circumstances, superfunds can be an alternative to an insurance buyout. There are a number of considerations applicable:

- The Gateway Rule.
    - At the moment, if a scheme can afford to insure all benefits immediately or over the next five years, then a Superfund could not accept it.
- Funding level.
    - A Superfund transaction will still be out of bounds if a scheme is quite poorly funded. So there will be a "goldilocks zone" – buyout is not affordable in the short to medium term but the scheme is reasonably well funded on a solvency basis – outside which a transaction is not financially viable.
- Covenant.
    - Trustees are exchanging the covenant of the sponsor, for the covenant of the superfund (i.e. the capital provided by its investors). One key question for Trustees is therefore if the covenant of the Superfund is likely to provide a better outcome for members. This assessment will be much easier to complete if the covenant of the sponsor is weak or non-existent, such in the case of Sears.
- Population.
    - Generally, pricing for Superfunds is more attractive for immature schemes as these are more expensive to insure and so there are arbitrage gains that can be achieved by delaying insurance.
- Advisory costs and execution risk.
    - Both of these are higher for a Superfund transaction than for a bulk annuity purchase, although costs should decrease once a few transactions have proceeded, and standard documents and processes develop as a result. Execution risk will potentially remain substantial as the transfer process is inherently more complex and time-consuming.

The recent yield increases have improved buyout affordability for many schemes and for a lot of these other aspects of preparation, such as data quality, are now a barrier to a transaction rather than funding levels. Some schemes and sponsors are also re-visiting their endgame objectives and solvent run-off (with the members and sponsor sharing the benefits from any surplus) is increasingly seen as a viable alternative to buyout and wind up.

A Superfund endgame is more niche than either of the above given the specific circumstances a scheme needs to be in for a transaction to take place and be likely beneficial for all parties. However, there will be a number of schemes meeting the relevant criteria, and for these a Superfund transaction will both be viable and likely to improve member outcomes – the Sears transaction being a clear example of this.

6 Benefit statement changes – assumption around TM1

Potentially some pro-active member communication from trustees is needed, or pro-active drafting of explanatory responses to member queries that may be raised, in respect of the 2024 Statutory Money Purchase Illustration ("SMPI") statements or Simplified Annual Benefit Statements ("SABS") for the trustees or managers of DC pension schemes that provide money purchase benefits only and that are used for automatic enrolment.

BACKGROUND

The Actuarial Standard Technical Memorandum 1: Statutory Money Purchase Illustrations ("AS TM1") sets out the methodology and assumptions to be used for calculating annual SMPIs / SABS. With effect from 1 October 2023, the Financial Reporting Council published a new version of this document which applies to statutory illustrations issued on or after this date.

The key changes that have been introduced in the latest version of the guidance:

- A standardisation of the benefits members will be assumed to take on retirement; and
- A prescribed methodology for deriving the rate at which members funds will be assumed to increase until retirement age (known as the "accumulation growth rate assumption")

Previously, the guidance was less prescriptive as to how the accumulation growth rate assumption was to be derived. This led to wide ranging assumptions being adopted. The aim of the new guidance is to produce more consistent and comparable results across different schemes.

WHAT IS THE IMPACT OF THESE CHANGES?

The above changes will have no impact on the actual value of members funds or the performance of these funds; it is only a change to how retirement projections are carried out.

When members receive their next SMPI / SABS, they may see a considerable difference in the projected value of their fund at their retirement date and the resulting level of income they may expect to receive.

Given the new guidance outlines what form of benefits the member is assumed to take on retirement, this may lead to material differences in the estimated retirement benefits shown in the 2024 SMPI / SABS compared to previous statements, and may therefore lead to a number of member queries. For example, if the previous illustration reflected a member taking tax-free cash at retirement, then the new estimated income at retirement may have changed significantly due to the illustrations now assuming that no tax-free cash is taken under the new guidance.

Furthermore, with the change in accumulation growth rate assumption, members may see considerably different projected fund values on retirement from that provided on previous statements. This will be dependent on how the new prescribed growth rate assumption compares to that previously adopted.

THINGS TO CONSIDER

The expectation of the new methodology for deriving the accumulation rate growth assumptions is that it should provide consistency year on year in the assumptions that are adopted for each investment. With the spike in interest rates in recent times, the Association of Consulting Actuaries highlighted their concerns that 2024 SMPI / SABS may provide some potentially unusual or misleading results.

Their analysis suggested there is the potential assets such as long-dated government bonds and index-linked government bonds may be assigned a higher assumption than would historically be expected as a result of recent market volatility. This would result in members projected funds on retirement being unduly optimistic and may have a detrimental impact on members retirement planning and decision making.

There is a consultation ongoing in which the above concerns (along with a few other suggested changes) are being considered. If updated guidance from the consultation is not produced in advance of 6th April 2024, trustees may want to consider writing out to members to forewarn them the 2024 statements they will receive may be overly optimistic and to treat the projected retirement benefits with a level of caution.

7 Pensions Ombudsman not a 'competent court'

The Court of Appeal has held, in the case of CMG Pension Trustees V CGI IT UK, that the Pensions Ombudsman (TPO) is not a "competent court" for the purposes of Section 91 (6) of the Pensions Act 1995. The decision has important implications in relation to pension overpayments.

The case arose through a claim against the CMG pension scheme principal employer by the Trustee. The judge was asked to consider a number of issues including whether the Trustees had to obtain an order from a competent court or if the TPO could be regarded as a competent court for Section 91 (6) of PA 1995. This issue arose in the context of a member being overpaid and the Trustee seeking to recoup the monies. The Judge decided that the Pensions Ombudsman was not a "competent court" for the purposes of Section 91 (6) of the Pensions Act 1995.

This effectively means that, where there is a dispute, the PO does not have the power to give permission to Trustees to deduct overpayments from members, so the Trustees must first get an order from a competent court. It's important to note that, where the member agrees they have been overpaid and is willing to repay, then no application to court is needed.

Following the CMG Ruling by the Court of Appeal, the TPO has published a factsheet, and it advises that the Department of Work & Pensions (DWP) intends to bring in legislation to formally empower the PO to end an overpayment dispute without going to court.

In the meantime, the factsheet provides guidance on managing overpayment disputes, this includes the process to be followed when application to the court is to be made. It is important to note the County Court will not revisit the merits of the case as that has been carried out by the PO. The most appropriate court is the one closest to the member.

"When issuing the Determination, the Ombudsman will also provide a certified copy of the Determination for the County Court. Civil Procedure Rule 70.5 and Practice Direction 70A set out in detail the procedure that must followed. The court form (currently N322A) needs to be completed, with attached fee, referencing s151 Pension Schemes Act 1993 (the provision under which enforcement is being sought). The County Court will deal with the matter on the papers."

Helpful Links

Factsheet

8 Investment Update

MARKET COMMENTARY

Markets experienced a strong rally during the quarter with Global Equities and Global Bonds generating positive returns of 6.3% and 8.1%* respectively.

The key driver of returns had been the end of the 'higher for longer' interest rate narrative which helped support valuations across most asset classes. As inflation declined across most of the developed world during the quarter markets became increasingly comfortable with the view that central banks had achieved their aim of combatting higher levels of inflation with their interest rate hiking policies.

This view was supported by the December Federal Open Market Committee, where the latest projections suggested three interest rate cuts over 2024.

EQUITY MARKETS

Global Equity markets reversed the third quarter narrative. From a regional perspective European Equities generated the strongest returns at 7.6% followed by the U.S at 7.1%. Despite the majority of the U.S Market's returns being attributed to the 'magnificent 7' tech and AI stocks for most of the year, this quarter saw the rally broaden out to the rest of the index. The U.K and Japan were key laggards this quarter at 3.2% and 3.3% respectively.

In Japan concerns around the appreciation in the Yen following the Bank of Japan's decision to relax its yield curve control weighed on equity market returns. Despite Chinese Equities falling -4.8%*, off the back of concerns around the growth of the Chinese economy, broader Emerging Markets managed to deliver 7.9%*, mainly driven by Latin America.

OTHER ASSETS

Commodities declined during the period at -4.6%* as gains in precious and industrial metals were offset by weaker agriculture, energy and livestock prices. Energy was the key detractor this quarter mainly driven by oil where prices fell despite output cuts from Opec+ (the Organization of the Petroleum Exporting Countries, plus some other oil-producing countries).

Slowing growth with greater regional divergence alongside elevated political risks has created a complex environment for currency markets. Over the quarter, fading US optimism and prolonged overvaluation led to the USD falling relative to other developed market currencies.

FIXED INCOME AND INFLATION

The fall in inflation numbers over the quarter increased expectations that interest rates will be cut by central banks in 2024 and meant that sovereign bonds (in particular the UK and Italy) rallied during the period. Within the UK, long-term UK gilt yields decreased by -0.7% to 4.1%. Real yields decreased by -0.5% to 0.9%. Long-term inflation moved from 3.4% to 3.2% over the period.

More broadly within fixed income, increased expectations of falling interest rates in 2024 also led to tighter credit spreads (falling by -0.2%) which helped the more interest rate sensitive investment grade bonds outperform relative to high yield. Spreads on high yield and emerging market debt fell. Global indices enjoyed enhanced positive returns as the USD weakened boosting USD returns.

Outlook

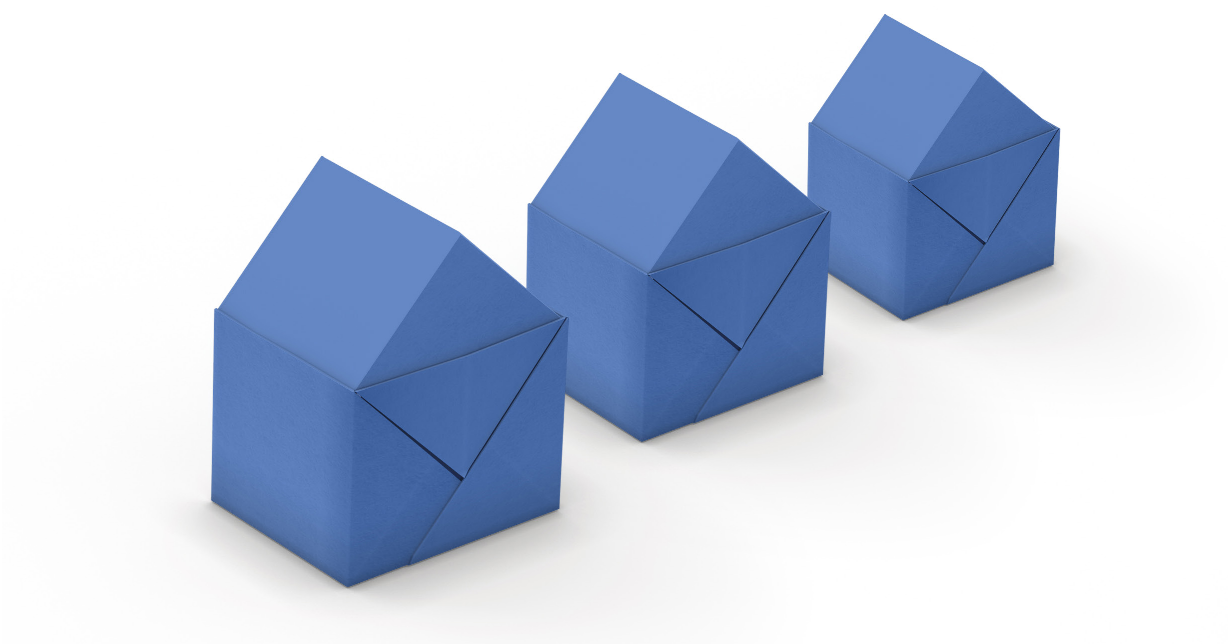
Whilst the rally experienced by most asset classes over the quarter can be seen as positive news after a weaker prior quarters, investors must be mindful of what the figures could imply for markets and economies going forward.

If central banks aim to start cutting interest rates in 2024 then this could indicate further economic weakness which in turn could be negative for equity valuations. However, falling interest rates and a weaker economic environment should generally be positive for sovereign and investment grade bonds which have struggled in recent periods due to persistently high levels of inflation and high interest rates.

All returns shown are shown in GBP terms unless stated otherwise, sourced: FTSE, Markit iBoxx

*Local currency, except for EM and global indices, which are in US dollar, sourced: JPM and MSCI Past performance is not a reliable indicator of current and future results.

Data as of 31 December 2023.



9 Pensions Dashboards - the slow dash to connection

You could be forgiven for thinking that the whole Pensions Dashboard thing has gone away.

Given the rate of progress since they were first announced it's seemed less like a dash and more of a meandering walk.

To assume that Dashboards are dead would however be a big mistake. Recent intelligence suggests that the intent to progress remains and a new staging timetable isn't far off.

HOW DID WE GET HERE?

The Dashboards program was conceived to make it easy for people to find and view information about their pensions. A staging timetable was announced outlining when schemes would need to connect to the new infrastructure. The industry then set about meeting the not inconsiderable challenge. It soon became apparent that meeting the requirements and timetable would be exceedingly difficult for some schemes. The issues to be navigated included, and still do,

Data quality

Digitisation of the data

Administrator technology, or lack of it

Resource and budget

Feedback from many of the large administrators and platform providers was that it wasn't achievable, at least not in the proposed timetable.

It wasn't too much of a surprise when in June 2023 it was announced that there was to be a "pause". No new timetable was announced but there was a new endpoint of 31st October 2026 for all in scope schemes to connect.

Despite the industry pressing for detail on when a new timetable would emerge and if anything, substantive would change, there has been little news.

Recent noises, however, suggest that the announcement of a new timetable is just months off. April 2024 has been mentioned.

An 18-month dash?

The first schemes may well connect from April 2025. That means all schemes in scope will sit within an 18-month window ending October 2026.

WHAT NEXT?

Well basically all the things that have been flagged for action since Dashboards were first announced. There's lots of good recent guidance on getting ready from PASA & the TPR, nothing new but a good prompt for schemes that aren't yet there.

The key points are,

Make sure the underlying technology is up to the job of meeting The Dashboards requirements.

Get on top the data. It needs to be good enough to enable a match from a find message as well as supporting the calculation of an Estimated Retirement Income.

Communicate to members in advance of the staging date and ensure the administrator has a plan to handle the inevitable queries.

Watch for developments, looks like at last the pace is hotting up!

10 The Taskforce on Social Factors

The consultation of the 'Guide from the Taskforce on Social Factors' ('the Guide') took place over the final quarter of 2023. The Taskforce on Social Factors ('TSF') was set up following the Department for Work & Pensions ('DWP') July 2022 consultation, 'Consideration of social risks and opportunities by occupational pension schemes'[1]. The TSF's role included:

- Identifying reliable data source and other resources to enable pension schemes to assess and manage financially material social risks and opportunities, informing guidance on investment risks from social factors.
- Monitoring and reporting on developments with the International Sustainability Standards Board ('ISSB') and other international standards.
- Developing thinking around how trustees can identify, assess and manage the financial risks posed by modern slavery and supply chain issues[2].

The Guide from the TSF, 'Considering Social Factors in Pension Scheme Investments' includes 4 sections:

1. Social factors and pension funds
2. Social factor data
3. Addressing social factors in pension portfolios
4. Recommendations from the Taskforce

The appendices provide a wide range of data sources, guidance for trustees on what good looks like from asset managers and investment consultants, specific considerations, asset manager practice on modern slavery and seven case studies.

SOCIAL FACTORS AND PENSION FUNDS

The Guide begins by exploring why material social factors are important from an investment perspective, highlighting their inseparability from businesses and investments. Whilst it is recognised that causing, contributing to or ignoring adverse social impacts can lead to short term benefits, the Guide details the longer-term costs that can affect pension funds and businesses, potentially spilling across the economy, creating systemic risks. Systemic risks must be addressed directly as their impacts are economy-wide, meaning they cannot be avoided, mitigated or diversified away. Given the large, diversified portfolios of pension schemes - whether individual large schemes or through the passive strategies of smaller funds, they are considered universal owners ('UOs'). UOs hold a slice of the economy and are both susceptible to systemic risks and have influence over them.

A distinction is drawn between material and salient risks to help trustees effectively analyse social factors. Material risks have 'the strong potential to effect tangible, negative impacts on the investee company' whereas risks to people are the starting point for saliency. Salient social issues can be identified and prioritised using four parameters of severity - scope (number affected), scale (serious of adverse impacts), remediability (restoring those affected to at least equivalent to their previous situation and any limits on this) and likelihood of occurrence. Modern slavery is given as an example of a highly salient risks despite relatively low financial exposure for pension schemes.

This section also considers pension trustees' fiduciary duties and how these align with consideration of social factors. The key terms of the 2015 report, Fiduciary Duty in the 21st Century, are laid out to help trustees stay on the right side of pensions law. Furthermore, the Impact Investing Institute's 2020 paper, Impact investing by pension funds: Fiduciary duty – the legal context, is used to show how impact investing and fiduciary duties can also be compatible. However, as noted the Society for Pension Professionals ('SPP'), more recent reports which detail the scope and limits of fiduciary duty and impact investment have not been referenced[3]. Understanding in this area will be crucial for trustees to gain comfort when addressing social issues. Concerns have been raised on whether fiduciary duty is sufficiently broad to allow such considerations with experts calling for greater clarification in this area[4].

SOCIAL FACTOR DATA

This section recognises the difficulty in quantifying social risks. Particularly where these are systemic, modelling is not straight forward. However, scenario analysis, stress testing and qualitative assessments can all serve as strong justifications for action. Where using ESG ratings or score, particular attention will need to be given to the underlying weightings of data points, what the rating framework is trying to assess, the attributes used and the different data points that can be used to assess the same attributes. If ratings are aggregated with environmental and governance factors, any offsetting in performance in one area or the masking of significant concerns for individual companies should be borne in mind.

Metrics are given that could be standardised and compared if disclosed consistently. This includes gender and ethnic pay gap data, accident incidence rate and proportion of a workbook on '0' hours contracts. Although, data quality is crucial. The accuracy of data, frequency of updates, seniority of staff who review it and whether it can be independent and objectively verified will all be important to consider when presented with social risk metrics.

A materiality assessment framework is also provided to help prioritise areas for action. This breaks the assessment down into three stages, beginning with country assessments, then moving to sector assessments and finally corporate assessments. Four categories are given for corporate assessments - workforce, supply chain workers, affected communities and consumers and end users. Each stage includes a range of data sources.

ADDRESSING SOCIAL FACTORS IN PENSION PORTFOLIOS

Here baseline, good and best practice indicators for addressing social factors are provided. The Guide recognises the size, type and resource constraints of Scheme's may impact its application but has designed the framework to encourage progressive improvements of trustee practices.

There is also a deep dive on modern slavery, an umbrella term that covers offences such as slavery, servitude, forced or compulsory labour and human trafficking. Regardless of intent, modern slavery can impact the financial performance of business in a host of areas, such as criminal sanctions, loss of access to capital, asset freezing and supply chain disruption where modern slavery has been discovered. Areas for trustees to take note of are data availability, identifying risks to people, the difficulty of detection and the fact that many victims receive little remediation for abuse despite that providing remedy to survivors is a key pillar of the UN Guiding Pricniples on Business and Human Rights.

RECOMMENDATIONS FROM THE TASKFORCE

In this section, the Guide provides recommendations to set out what good looks like for social factor recommendations. 35 recommendations are given across stakeholders including pension trustees, regulators, asset managers, investment consultants and legal advisors. The Department of Work and Pensions ('DWP') are specifically recommended to consider formally setting expectations on social factors to be overseen by The Pensions Regulator ('TPR').

INDUSTRY RESPONSE

The TSF closed the consultation on 1 December 2023 and ran face to face roundtables to discuss the draft early that month.

The Guide has largely been welcomed by the industry. The Association of Professional Pension Trustees ('APPT') praised its clarity in defining social issues and said it provided 'a comprehensive framework, case studies, and practical guidance that can equip trustees with insights into the integration of social factors'[5]. Whilst the Association for Consulting Actuaries ('ACA') expressed a preference for a short, practical guide, they acknowledged it would be a useful source of information and references[6]. Both the SPP and the APPT highlighted specific circumstances of schemes will vary, affecting how they adress social factors. Along this vein, the SPP support that non-binding recommendations are given to develop market practice rather than giving mandatory reporting requirements.

Helpful Links

[Consideration of social risks and opportunities by occupational pension schemes - GOV.UK (www.gov.uk)]

[Launch of Taskforce on Social Factors for UK Pensions Industry]

[SPP response - DWP Taskforce Guide on Social Factors - The Society of Pension Professionals: The Society of Pension Professionals (the-spp.co.uk)]

https://www.pensions-expert.com/Law-Regulation/Rethinking-fiduciary-duty

[APPT responds to Considering Social Factors in Pension Scheme Investment – APPT (Association of Professional Pension Trustees)]

[ACA responds to Considering Social Factors in Pension Scheme Investments consultation – ACA – Association of Consulting Actuaries]

Coming Up Next

The transition into both a new calendar and financial year feels like the right time to prepare for the changes and challengers ahead. Here is a rundown of just some of the significant dates and event you might want to put in your diary for 2024.

January

1st : OPS (Revaluation) Order

The Occupational Pensions (Revaluation) Order 2023, SI 2023/1265, will come into force on 1 January 2024.

5th : Pension Fund Clearing

'Call for Evidence: Pension Fund Clearing Exemption' closes.

6th : NI Contributions Bill

This Bill will implement a cut in the main rate of NICs paid by employees ('primary Class 1 NICs') from 12% to 10%.

24th : Greater Member Security and Rebalancing Risk

Call for Evidence 'Looking to the Future: Greater Member Security and Rebalancing Risk' closes.

Q1: 'VfM' in DC schemes

Introducing a common framework for assessing value for money in workplace defined contribution schemes. Schemes will have to publish their results each October.

Q1: Online Safety Act 2023

Ofcom is due to publish detailed Codes of Practice on the implementation of the Online Safety Act 2023. The Act is expected to help with the combatting of pension scams.

April

1st : Pension Protection Fund (PPF) Levies 2024/25

Start of PPF Levy Year for 2024/25. Invoicing will take place in the Autumn.

6th : Abolition of Lifetime Allowance

Under the 2023 Finance Bill, the lifetime allowance will be replaced with two new allowances - a 'lump sum allowance' (which will limit the total amount of tax-free lump sum an individual can receive to £268,275, unless they hold a valid lifetime allowance protection or lump sum protection) and a 'lump sum and death benefit allowance' (which will also limit the total amount of lump sums an individual can receive before marginal rate taxation applies to £1,073,100, unless they hold a valid lifetime allowance protection).

6th : Tax on refunds of surplus

Tax charge on refunds of surplus reduced from 35% to 25%.(The government has also promised to launch a consultation on surplus extraction arrangements for DB pension schemes.)

Also in April

Single/General Code

New Pensions Regulator Single Code of Practice (now to be known as the 'General' Code of Practice) is expected come into force. The code combines ten existing codes and incorporates changes introduced by the Occupational Pension Schemes (Governance) (Amendment) Regulations 2018 relating to effective systems of governance (ESoG) and the own-risk assessment (ORA).The ORA must be completed within 12 months of code coming into force and then at least triennially thereafter.

DB Funding Regulations

Expected that new defined benefit funding regulations will come into force, but will not take effect until the Pensions Regulator's new DB funding code is published later in 2024 (see 'Funding Code' below).

Social Security Benefits Uprating

Uprating Orders are produced each year and specify the rates of various Social Security benefits for the coming tax year. The new State pension full rate is expected to increase from £203.85 to £221.20 per week.

GMP Increase Order

Expected to specify 3% as the percentage by which that part of guaranteed minimum pensions (GMPs) attributable to earnings factors for the tax years 1988–89 to 1996–97 and payable by contracted-out, DB occupational pension schemes is to be increased.

June

Court of Appeal to hear appeal in 'Virgin Media' case

In this case, Virgin Media Ltd v NTL Pension Trustees II Ltd, the High Court that section 37 of the Pension Schemes Act 1993 rendered void an alteration to the rules of a formerly contracted-out pension scheme relating to section 9(2B) rights in so far as the amendment was introduced without the actuarial confirmation required by regulations. Leave to appeal the decision was granted in 2023.

July

31st : Consumer Duty

For new and existing products or services that are open to sale or renewal, the rules came into force on 31 July 2023. For closed products or services, the rules come into force on 31 July 2024. Amendments to the FCA's Handbook are made by Consumer Duty Instrument 2022, FCA 2022/31, which came into effect on 31 July 2023.

Summer: DB Funding Code

Revised Code of Practice expected, applying to schemes with valuation dates after October 2024.

September

PPF consultation on 2025/26 Levy rules

PPF expected to publish its consultation on the 2025/26 levy rules.

Throughout 2024

Deadline for changes to Statements o of Investment Principles (SIPs)

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) and Pensions Dashboards (Amendment) Regulations 2023, SI 2023/399, introduce a 'disclose and explain' requirement. The regulations amend requirements relating to default SIP to ensure that relevant DC schemes disclose and explain their policy on illiquid investments in respect of default arrangements. This information must be included by trustees in the first updated version of their statement of investment principles to be produced after 1 October 2023 or by 1 October 2024 at the latest.

Economic Crime and Corporate Transparency Act

The government has explained that, in parallel with the Act coming into force, it intends to implement the ban on corporate directors provisions not yet brought into force under the Companies Act 2006, and issue regulations which will outline the limited basis by which companies may retain or appoint corporate directors going forward.

In effect, this will mean that only corporate directors with legal personality will be permitted under the available exceptions and all the directors of those permitted corporate directors will have to be 'natural' persons whose identity has been verified. This would affect schemes with a corporate professional trustee who would need to ensure that all of their directors are 'natural' persons.

Conversion of GMP Act 2023

The main provisions of the Act will come into force on a day to be appointed. The Act amends provisions in the Pension Schemes Act 1993, the Pension Schemes (Northern Ireland) Act 1993, the Pensions Act 2007 and the Pensions Act (Northern Ireland) 2008 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.

Royal Assent for new Data Protection Bill

Will replace the EU's data protection laws following Brexit.

Notifiable Events Regulations

The delayed regulations may be brought into force in 2024. Revisions are made to scheme and employer-related events that must be notified to The Pensions Regulator and new declarations of intent are introduced so that better and earlier information is provided to trustees and TPR in connection with corporate activity.

Climate risk reporting

The Government will review climate risk governance and reporting requirements for occupational pension schemes, with a view to extending them to sub-£1bn schemes.

'And beyond'

28 January 2025: General Election

The next general election must take place no later than this date. It marks five years from the day the current Parliament first met (17 December 2019), plus the time required to run an election campaign.

Spring 2025: Completion of first 'ORA'

First Own Risk Assessment under the new Single Code must be completed if, as expected, the Code is effective by Spring 2024.

31 October 2026: Pensions Dashboards

Pensions Dashboards connection deadline.

The pensions dashboards will continue to apply to trustees and managers of all registrable UK-based occupational pension schemes with 100 or more relevant members. However, the reference date for calculating the number of relevant members is being changed by the regulations from the scheme year end that fell between '1 April 2020 and 31 March 2021' to the scheme year that falls between '1 April 2023 and 31 March 2024'.

2026: Public Sector Consolidator

The government plans to work with the pensions industry to establish a public sector consolidator by 2026, aimed at schemes that are unattractive to commercial providers.

2026 – 2028: State pension age

SPA will incrementally rise to 67 between 2026 and 2028.

The government plans to have a further review within two years of the next Parliament to reconsider the rise to age 68.

6 April 2028: Normal minimum pension age (NMPA)

The minimum age for drawing benefits (other than in ill health) is increased to age 57, subject to transitional provisions around protected pension ages. Members will need to be informed of these changes.

2030: RPI reform and switch to CPIH

The Government proposal that RPI be replaced by CPIH in 2030 is expected to go ahead, following a failed judicial review of the proposal by a number of large pension schemes.

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