Essential UK Pensions News

January 2021

Introduction

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

Pension Schemes Bill approved

The Pension Schemes Bill was approved by the House of Lords on January 19, 2021. It will now receive Royal Assent.

The Bill includes new powers for the Pensions Regulator (TPR), amends the scheme-specific funding regime and the statutory transfer regime, and paves the way for further developments in relation to a pensions dashboard, climate change governance and collective defined contribution schemes.

Secondary legislation will be needed to bring the various provisions of the new Pension Schemes Act into effect and, for most areas covered by it, to set out further detail.

We expect to see different parts of the new Act coming into force at different times, some over the course of this year. For example, the new powers for TPR may be available to use by the autumn (see below).

For more information, see our recent briefing on this issue.

Minister confirms TPR's new powers will not have retrospective effect

Guy Opperman MP (the Minister for Pensions) has confirmed that TPR's new powers under the Pension Schemes Bill, including criminal sanctions and information gathering, will not apply retrospectively. This resolves a long-standing area of uncertainty and is welcome news for employers and others involved in the running of defined benefit (DB) pension schemes.

Responding to a question from a Labour MP, Mr Opperman said that TPR will publish and consult on draft guidance on the use of the new criminal sanction powers. The aim was for the remaining new powers, which require implementing regulations, to be available for TPR to use by autumn 2021. Given the intention to consult on the use of criminal sanctions, it seems likely that those particular powers may only become available later.

DWP responds to climate risks consultation and consults on draft regulations

The DWP has issued its response to its August 2020 consultation about the government's proposed policy on climate risk governance and reporting by occupational pension schemes. It has now launched a second consultation (taking into account the responses to the first one), this time on the detailed legislation that would implement the government's policy. The consultation closes on March 10, 2021. These obligations build on but are distinct from the ESG requirements imposed on trustees in recent years (which require disclosure of trustee's investment policies regarding climate change) and are much more directive in terms of the steps trustees need to take to tackle climate risk.

The legislation takes the form of draft regulations to be made under the new Pension Schemes Act (once enacted) and draft statutory guidance. The regulations set out what schemes are

required to do and the statutory guidance explains how to do it. Schemes will be allowed to diverge from the statutory guidance but they will have to explain why they have chosen to do so.

What are the new requirements?

The draft regulations and guidance require trustees to assess and report on the climate change risks and opportunities in their investment portfolio. Specifically trustees will be required to take the following steps:

- **Disclosure**: make climate change disclosures in line with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).
- **Governance**: have oversight of climate-related risks and opportunities which are relevant to the scheme and report annually (in their TCFD report) how they are achieving this.
- **Strategy**: identify and assess the impact of climate-related risks and opportunities on the scheme's investment and (for DB schemes) funding strategy over the short-, medium- and long term.
- **Scenario analysis**: conduct scenario analysis to test the impact on the scheme's assets and liabilities and the resilience of the scheme's investment and funding strategies. This needs to be done in the first year and then at least every three years.
- **Risk management**: have processes for identifying, assessing and effectively managing climate-related risks which are relevant to the scheme, which are integrated into the scheme's overall risk management.
- **Metrics**: select and "as far as they are able" calculate climate-change metrics in respect of the scheme's assets, including emissions metrics (e.g. total emissions and carbon footprint metrics).
- **Targets**: set a non-binding target for the scheme in relation to at least one of the selected metrics and measure performance against it annually ("as far as are they are able").
- **Trustee knowledge and understanding**: have the appropriate degree of knowledge and understanding of climate change risks and opportunities to be able to properly exercise their functions.

The DWP has clarified that trustees can take a proportionate approach to obtaining data, carrying out scenario analysis and using metrics and targets, "taking into account the costs, or likely costs, which will be incurred by [the] scheme and the time required to be spent by the trustees or people acting on their behalf". This may give some reassurance to trustees who are concerned about the potential for resources to be diverted from other necessary scheme work.

When will the new requirements start to apply?

The new regulations are expected to come into force in October 2021. The new requirements will be introduced as a phased roll-out, starting with the largest pension schemes.

DWP envisages that schemes with £5 billion assets or more and all authorised master trusts must meet all of the climate change governance requirements from October 1, 2021. They would have 7 months from the end of the scheme year which is underway in October to make the necessary TCFD disclosures.

Comment

The consultation documents acknowledge this will be a steep learning curve for many trustees and many will be feeling daunted by the task ahead. To prepare themselves for these changes – and bearing in mind that there will be a statutory requirement for trustees to have the requisite knowledge and understanding of these issues – trustees may wish to consider having training on the new regime.

Trustees should also speak to their advisers to understand when these requirements will start to apply to their scheme. The consultation acknowledges that, particularly for the larger schemes and authorised master trusts, timings will be tight. Trustees may find it helpful to draw up a project plan to work out what steps they need to take and when, to ensure they meet their governance and reporting deadlines.

The end of the Brexit implementation period: Implications for pensions

The Brexit implementation period ended at 11 pm on December 31, 2020 and the trade deal agreed by UK and EU negotiators took effect through the EU-UK Trade and Cooperation Agreement.

In the short term, this has a limited impact on UK pensions law which for now remains basically unchanged and is not expected to change significantly in the immediate future. However, there may be some divergence from EU law over time.

There are a number of practical steps we recommend trustees consider taking to ensure the continued smooth running of schemes. Key actions include:

- **Employer covenant**: Considering the impact of recent Brexit developments on the sponsoring employers' business and covenant.
- **Investment**: Checking the scheme's longer-term investment strategy remains suitable.

- **Pensions for overseas members**: Ensuring that any members living outside the UK in Europe can continue to receive their pension despite the closure of some UK bank accounts for ex-pat members.
- **Member communications**: Being prepared to answer questions from members (particularly those resident in the EU) about how the end of the implementation period will impact their pension savings.
- **Data protection**: Where schemes receive personal data from the EU or EEA, building satisfactory data protection clauses into relevant service provider contracts to ensure this data flow can continue after April, when a temporary agreement between the UK and EU on data transfers may end.

For more information, see our Brexit briefing.

TPR publishes interim response to first funding code consultation

On January 14, 2021, TPR published an interim response to its first consultation on the draft DB Funding Code which closed in September 2020. This had invited views on, amongst other things, the proposed twin-track regulatory approach (fast track and bespoke) and the principles that TPR considers should underpin all funding valuations.

TPR has received a record number of responses (127 responses with a total of over 6,000 comments) which it says were broadly supportive of the proposed approach and principles.

Some concerns were raised, which TPR summarised as:

- Risks associated with where Fast Track guidelines would be set (such as some schemes 'levelling down' and an increase in the cost of DB pension provision for others).
- Proposed Fast Track guidelines for open schemes.
- Potential loss of flexibility (e.g. through benchmarking the Bespoke route against Fast Track).
- An increased evidential burden if choosing to submit a Bespoke valuation.
- The Bespoke route may be perceived as being 'second-best.'
- Reliance on covenant being watered down and what a greater trustee focus on covenant visibility would mean for schemes' ability to rely on covenant beyond the medium term.

David Fairs, TPR's Executive Director of Regulatory Policy, Analysis and Advice, had already commented on some of these points (in particular the open schemes issue) in an earlier blog. The blog seemed to reassure trustees and employers that the new code would not be a radical departure from the current system.

The next step will be a second consultation on a revised funding code of practice. TPR will also give a full response to the first consultation.

As the revised code will need to reflect the new funding legislation, TPR will hold off publishing this until the Department for Work and Pensions (DWP) consults on draft funding regulations. TPR says the DWP consultation is "currently expected to be in the first part of this year. We therefore anticipate publishing our second consultation in the second half of 2021."

Comment

This brief interim response contains some further reassurance for trustees and employers. Schemes that are likely to need Fast Track may be comforted by TPR's commitment to take the impact of COVID-19 and "the very challenging current economic conditions" into account when developing Fast Track guidelines. TPR also says that some of the concerns that have been raised stem from misunderstandings of what it is proposing, which it intends to clarify soon.

PPF publishes final levy rules for 2021/22 and consults on commercial consolidators levy guidance

The PPF has published the final PPF levy rules for 2021/22, following a consultation last year. The rules confirm that the PPF:

- Will reduce the levy for small schemes, so that only those schemes with £50 million or more in liabilities will be charged in full – this is expected to be a long-term adjustment.
- Will reduce the cap on each scheme's own levy from 0.5 per cent to 0.25 per cent of its liabilities – to be kept under review for future years.
- Estimates that it will collect a reduced levy (when compared with the previous levy year) of £520 million.

While these levy reductions will undoubtedly be welcomed by many schemes in the current climate, they may seem counter-intuitive given the expectation of increasing employer distress this year and a likely increase in the number of schemes entering the PPF. The PPF has said that it wants to be supportive of schemes and employers during the pandemic.

However, it seems likely that the levy will have to increase again in future if this year sees significant calls on the PPF. For now, the PPF simply notes that "We will continue to monitor economic and other developments carefully and consider what, if any, changes to our rules are necessary in view of these exceptional circumstances in future years."

The PPF has also reminded schemes who have PPF-compliant contingent assets to submit the required supporting documentation (such as guarantor strength reports) to the PPF by 5pm on April 1, 2021. A PPF email address is provided for this purpose. Where guarantors could be adversely affected by Brexit, schemes may wish to commission the report early in case it needs to be materially updated.

Invoices for the 2021/22 levy year will be issued in the autumn.

The PPF has also started a consultation on draft levy guidance for DB commercial consolidators. When deciding the levy for these schemes, the PPF proposes to focus on buffer funds and winding-up triggers. A levy would be charged where a transfer is made to a commercial consolidator and could be revised following the transfer-in of new liabilities.

Review of DC default fund charge cap: no reduction for now

Following a call for evidence on the default fund charge cap and standardised cost disclosure, the Government has concluded that the DC market is working competitively. The charge cap level will not be changed "at the present time" and transaction costs will not be included within it as they are unpredictable and could discourage innovation. However, flat fees will be banned for auto-enrolment pots worth less than £100 (this threshold to be kept under review).

The Government also notes that information about charges is still inconsistently presented to both trustees and members. It will consider this further.

The DWP's survey of charges across DC schemes, conducted in parallel with the call for evidence, found that the average charge for members in auto-enrolment qualifying schemes is 0.48 per cent, i.e. significantly below the cap.

Small pots working group publishes recommendations

A DWP working group has recommended potential solutions to the problem of members having multiple small deferred money purchase pension pots, particularly in master trusts, largely as a consequence of auto-enrolment. For example, the working group recommends further work on a "default consolidator" solution (i.e. everyone has a default scheme into which only their deferred pots would be transferred) or "pot-follows-member" (i.e. when an employee moves jobs their pension pot moves with them to the new employer's scheme). These would both be automatic processes not requiring member consent.

TPR updates COVID-19 guidance on DC schemes to address transfer requests from "gated" funds

TPR has updated its COVID-19 guidance on DC management and investment to address the issue of member transfer requests from funds (e.g. certain property funds) that have been temporarily closed or "gated".

Key points to note are:

- While TPR acknowledges that making a transfer payment is likely to be difficult where all or some of a member's investment is held in a gated fund, no extension to the statutory timeframe is possible in these circumstances and fines may apply if the transfer deadline is missed.
- If only part of the member's investment is in a gated fund, the scheme could try offering a partial transfer with the remainder to follow once the fund has reopened.
- Schemes must report any significant failures to pay transfer values on time.

FCA update on timing of finalised transfer guidance

The FCA has announced that "in the coming months" it will publish its "Finalised Guidance GC20/1" about pension transfers alongside an updated FCA tool to assess the suitability of transfer advice.

Comments in the draft FCA guidance GC20/1 aimed at scheme trustees caused controversy in the pensions industry at consultation stage last summer. The FCA:

- Said that it considered that giving members illustrative figures, which compare what their benefits would look like within the DB scheme or after transfer to a DC environment, could constitute regulated advice. This could include making benefit calculators available to members (illustrating possible DB and DC outcomes) or giving indicative annuity prices in a member communication alongside information about the member's scheme benefits.

- Left unclear whether giving unsolicited transfer values could be a form of regulated advice.

The uncertainty over the FCA's views on unsolicited transfer values caused particular concern in the industry. A significant number of schemes routinely provide illustrative transfer values, for example on member websites or in at-retirement warm-up communications. Responses to the consultation argued that illustrative transfer values are intended to increase member engagement with their benefits and to help members make informed choices, so including this information for members is helpful and should not be discouraged.

While both the FCA and TPR wish to see an increase in member engagement, they have also been clear that it will be in the best interests of most members to stay in a DB pension scheme (particularly given the increase in scam activity). The challenge for the FCA now is to steer a satisfactory path between those two aims.

Since giving regulated advice without the necessary FCA authorisation is a criminal offence, trustees should identify any part of their current communications strategy which could be problematic under the draft GC20/1 guidance, consider what changes to member communications it would be sensible to make now, keep a watching brief for finalised guidance and be prepared to make further changes urgently, if necessary to ensure compliance.

Extension of temporary suspension of winding up petitions

Temporary, pandemic-related restrictions on the use of statutory demands and winding-up petitions against businesses have been extended from the end of 2020 to March 31, 2021. The restrictions (introduced by the Corporate Insolvency and Governance Act 2020) aim to give companies extra protection during the pandemic by stopping creditors from bringing about an employer insolvency event.

The restrictions also apply to trustees of DB pension schemes and could make it harder for them to enforce outstanding debts, such as deficit repair contributions or "Section 75" employer exit debts. Faced with an employer that refuses to pay such debts, trustees cannot currently threaten winding-up proceedings. In some cases this could significantly (although temporarily) change the balance of power between trustees and employers of DB pension schemes.

Mr O (CAS-32204-V0P4) – Burden of proof on former employee to demonstrate historic scheme membership

Summary

The Pensions Ombudsman (TPO) has held that the burden of proof was on the former employee to show that he had been a member of a historic scheme. He placed a certain amount of reliance on HMRC's GMP records when coming to his conclusion.

Background

Mr O was employed by Amnesty International (AI) between 1973 and 1983.

AI set up the Amnesty International Superannuation Scheme in 1988 (the "Scheme") to replace a previous AI pension scheme, which was wound up in 1992 (the "Old Scheme"). At that point members of the Old Scheme were offered the opportunity to transfer into the Scheme.

In 2018, several years after retiring and starting to draw his state pension, Mr O became aware through former AI colleagues that AI operated occupational pension schemes. He contacted the Scheme's administrator to claim an entitlement to a pension.

The Scheme's administrator investigated but could not find any evidence that Mr O had been a member of either the Scheme or the Old Scheme, and Mr O was unable to produce any documentary support for his claim. A list of members of the Old Scheme did not include Mr O and there was no evidence of a transfer in respect of him to the Scheme or any entitlement under it. As the Old Scheme had been contracted out, the administrator also checked with HMRC which confirmed that it had no GMP noted on its records for Mr O in relation to the Scheme.

Mr O complained to TPO.

Pensions Ombudsman's determination

TPO held that the burden of proof to show that he was a member of the Old Scheme lay with Mr O, but he had failed to do this. Since HMRC records suggested Mr O held no pre-1997 GMP liability, it was unlikely that he was a member of the Old Scheme.

Comment

This case is consistent with previous Ombudsman decisions. TPO will look at the evidence for and against the complainant's claim that he has a pension entitlement and decide the question on the balance of probabilities.

TPO will often consider HMRC's GMP records alongside other information for a contracted-out scheme. As here, in the absence of definitive evidence from the scheme or member, HMRC's records can be persuasive.

The determination can be viewed here.

Pensions issues in the pipeline

March 10, 2021 – Deadline for responses on DWP's second consultation on climate change governance and disclosure.

October 1, 2021 – New requirements apply for trustees to publish information on a publicly available, free website relating to voting and capital structure of investment companies under the Occupational Pension Schemes (Investment and Disclosure) (Amendment) Regulations 2019 following the transposition into UK law of the revised Shareholder Rights Directive (SDR II).

October 1, 2021 – New requirements for trustees of DB schemes to publish an implementation statement online under amendments to the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013. For "relevant schemes" (broadly, money purchase schemes with 100 or more members), the requirement to publish an implementation statement online applies as soon as the accounts have been signed after October 1, 2020 (but in any event no later than October 1, 2021).

Revised Funding Regime – A revised Code of Practice is expected by the end of 2021, after the new Pension Schemes Act comes into force and the DWP has issued and consulted on draft funding regulations.

Contacts

Lesley Browning
Partner
Tel +44 20 7444 2448
lesley.browning@nortonrosefulbright.com

Shane O'Reilly
Partner
Tel +44 20 7444 3895
shane.o'reilly@nortonrosefulbright.com

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