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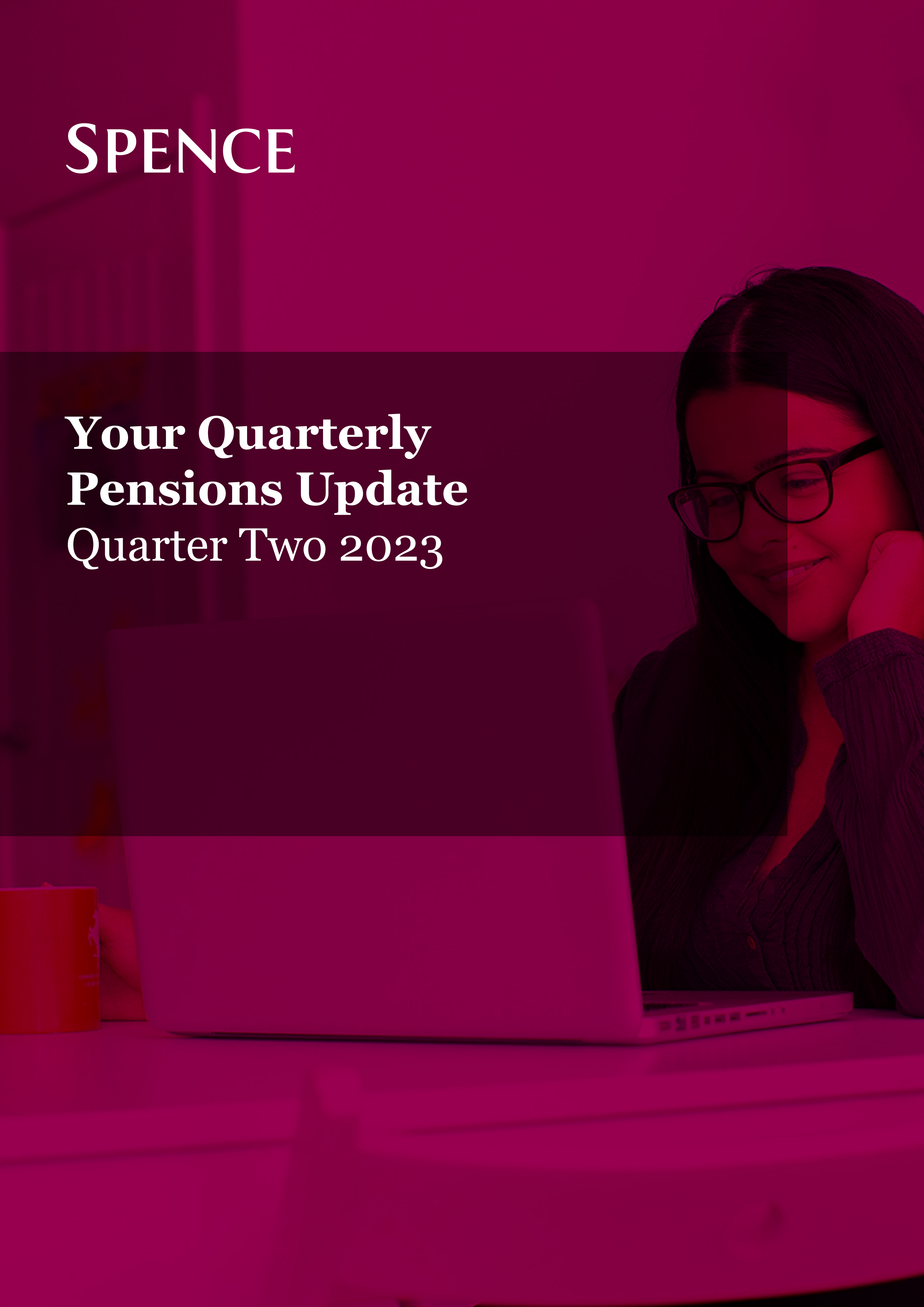


# Your Quarterly Pensions Update

## Quarter Two 2023

# What's inside?

# Welcome to your Quarterly Pensions Update

## The purpose of this report is to update sponsors and trustees with recent pensions industry changes in the quarter.

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

The report combines brief written comment with links to any 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 alan_collins@spenceandpartners.co.uk or your usual Spence contact.

# STOP PRESS! Mansion House Speech rundown

The Chancellor, Jeremy Hunt, outlined plans in his Mansion House speech on 10 July 2023 to encourage pension schemes to invest up to £75 billion in the economy, as part of broader regulatory reforms for the UK's capital markets. The plans are subject to calls for evidence and consultations, but decisions are still expected by the Autumn statement in November.

Key points to note include the following (we will explore these issues in more depth in Quarterly Update 3/2023):

- **Trustee skills, capability and culture.** The Government has published a new call for evidence to support the development of policy options for improving the skills and capability of pension scheme trustees (of all types of scheme – DB, DC and hybrid) and to remove barriers to trustees' ability to make effective investment decisions. In particular, views are sought on whether trustees have the right knowledge and skills to consider investment in the full breadth of investment opportunities.
- **DB superfunds.** In its response to a 2018 consultation on the legislative framework for the regulation of defined benefit (DB) 'consolidators' or 'superfunds', the government states that it wants to see this market develop. Consequently, DB employers and trustees could have an alternative to pension scheme buy-out and superfunds could use their scale to invest in assets that support the UK economy. Primary legislation will be needed first and so it is still likely to be a while before we see the first transactions taking place.
- **DB innovation.** A new call for evidence has been published which could lead to more choices for DB schemes as well as supporting wider economic initiatives. The call for evidence covers the current rules around surplus refunds; more consolidation options (including the prospect of a public sector consolidator, potentially run by the Pension Protection Fund); and the role of DB schemes in "productive finance". The call for evidence emphasises that decisions on asset allocation will continue to be a matter for schemes themselves.
- **Collective Defined Contribution (CDC).** In a response to its consultation on extending CDC provision beyond single/connected employer schemes in order to accommodate unconnected multi-employer schemes, the government confirms that it will consult on draft regulations to fulfil this objective. There is also a commitment in respect of provision for CDC decumulation products. The government believes that, through CDC, schemes could invest more effectively by pooling assets.
- **Value for money.** In a response to an earlier consultation on a new value for money (VFM) assessment framework for defined contribution (DC) schemes, the government signals a shift of focus from costs to value through the consideration of factors, such as investment performance, essential to longer term saver outcomes. The VFM framework also aims to accelerate further consolidation in the DC market by, inter alia, providing the Pensions Regulator with powers to require wind ups and consolidation where schemes are not delivering VFM to their members. Again, the changes will require primary legislation and the intention is to introduce them in phases.
- **Helping DC savers with pension choices.** The Government has published a response to its call for evidence on helping savers understand their pension choices and a new consultation on a decumulation framework to support individuals when they access their pension savings (i.e. at the point of decumulation). Trustees of DC schemes will prospectively have a new duty to offer decumulation services to their members. This does not mean that schemes will have to offer all decumulation choices directly; they can instead partner with another supplier. Members will have the choice of the default service offered by their scheme or accessing options available under pension freedoms.
- **Deferred small pension pots.**: Alongside a response to its call for evidence on addressing the challenge of small pots, the government has issued a consultation on its proposed automated consolidation solution. The preferred option is a multiple default consolidator model, under which deferred small pots, meeting the eligibility criteria for automatic consolidation, will transfer automatically to one of a number of consolidators. Members will have an opportunity to opt-out as well as the option to choose their consolidator. An enhanced authorisation regime for schemes to act as a default consolidator is also proposed. Whilst these changes could help solve the problem of small pots, they will also necessitate the introduction of new processes for pension schemes.

# Single code published – we wish! rundown

## Oh Single Code, where art thou?

It seems extraordinary that the Single Code of Practice on Pension Schemes (now to be known as the General Code), despite being consulted on in March 2021, has still not been officially published, let alone brought into force.

Our current understanding is that a final draft has been produced by the Pensions Regulator and that this has been passed to the Pensions Minister, Laura Trott.

Nevertheless, the Code has yet to be laid before Parliament and, given that it must be laid for 40-days under the negative affirmation process, it cannot complete before the Summer recess, meaning that it will not see the light of day before the Autumn (for the House of Commons, the House rises on 20 July 2023 and returns on 4 Sept 2023).

It is further understood that, for the purpose of Own Risk Assessments (ORAs), once published, the Code will not take effect until April 2024. In addition, recent comments from a regulatory representative have indicated that the timing of the ORA will be 'more aligned' to the statutory instrument (SI 2018/1103), rather than the draft code.

Whilst the expectation was for the Code to be in force long before now, it is important to emphasise that the regulations underpinning the Code and requiring schemes to have 'an effective system of governance (ESoG) including internal controls' have been legally in effect since 13 January 2019 (yes, you read that correctly)!

So, given this 'mis-match' between the law and the detailed requirements expected to set out in the Code, what should trustees be doing now?

Our view is that Trustees are the stewards of the members' future financial wellbeing and it really doesn't get any more important then that. A Trustee's focus must therefore be to ensure that the right benefits are provided to the right members at the right time and having a system of governance in place that not only supports doing that but also evidences that it is effective. To want to operate an ESoG is a behaviour and doesn't require a code. However, to assist, the Regulator's draft code is available and recent comments from a regulatory representative indicated that the final version only has some small changes to the Risk Management Function, the Remuneration Agreement, the timing and content of the ORA.

To begin to document their ESoG, trustees should:

- Establish the Risk-Management team responsible for compliance with the ESoG requirements
- Read SI 2018/1103, the draft code and deliver training for the Risk-Management team
- Draft and agree policies for the Risk Management, Internal Evaluation and Actuarial Functions, together with the Outsourcing policy, as all four need the prior approval of the Trustees before undertaking the activities
- Complete a governance framework assessment, including documenting the proportionality applied to the Scheme's activities and the contingency plans (Gap analysis phase 1)
- Complete a review of all of the Trustees' documents, policies, processes, procedures, logs, registers, statements and lists, and using the draft code as a guide, evaluate what is needed for the Scheme (Gap analysis phase 2)
- List all possible improvements in order of priority
- Incorporate the agreed governance improvements in the Scheme's Business Plan, set the completion dates and make the improvements
- Await publication of General Code / final details of the ORA, the requirements of which will be much easier with all of the above steps completed (but don't hold your breath on the timing!)

**Helpful Links**

Single code of practice consultation | The Pensions Regulator

The Occupational Pension Schemes (Governance) (Amendment) Regulations 2018 (legislation.gov.uk)

# Pensions Dashboards Update

## Pensions Dashboards – Connection Deadline Update

The Pensions Minister, Laura Trott, has provided an update on the Pensions Dashboards Programme (PDP) reset, with amended regulations to include a connection deadline of 31 October 2026. In a written statement, Trott confirmed that she is laying amending regulations with a "new approach to delivery". The Minister's Statement is reproduced in full below.

Subsequent to the Statement, the Pensions Administration Standards Authority (PASA) has launched Guidance on providing 'value data' to pensions dashboards which can be used by defined benefit and defined contribution schemes. Value data answers two main questions for dashboards users – 'what have I got already?', and 'what might I have at retirement?'.

Also, the Pensions Regulator (TPR) has published a Blog on getting schemes 'data ready' for pensions dashboards. The blog reminds trustees that they are "responsible for [dashboard] duties and shouldn't underestimate the time they'll take. Time spent cleansing and updating data now will benefit the saver and schemes later".

**Statement made by Laura Trott, Parliamentary Under Secretary of State for Pensions**

*"Pensions dashboards will transform the way in which people plan for retirement. On 2 March 2023, I announced that the Pensions Dashboards Programme would require additional time to deliver the connection of pension providers and schemes, in accordance with the connection deadlines set out in the Pensions Dashboards Regulations 2022 and the Financial Conduct Authority's corresponding pensions dashboard rules.*

*"More time is needed to deliver this complex build, and for the pensions industry to help facilitate the successful connection of a wide range of different IT systems to the dashboards digital architecture. As part of our reset of the Pensions Dashboard Programme, I am today laying amending Regulations with a new approach to delivery that allows us to work more collaboratively with the pensions industry. Rather than setting out the entire staging timeline in legislation, we will instead set this out in guidance which we will collaborate on with industry this year. This will give the Pensions Dashboards Programme the flexibility it needs to ensure this complex project is completed effectively.*

*"In recognition that the requirement to connect to the digital architecture should remain mandatory, we will include a connection deadline in legislation of 31 October 2026. This is not the Dashboards Available Point – the point at which dashboards will be accessible to the public – which could be earlier than this.*

*"The Government remains as committed as ever to making pensions dashboards a reality and we are ambitious about their delivery. I am confident that this re-appraised approach will enable us to make significant progress on delivering dashboards safely and securely, enabling consumers to take advantage of their benefits to plan for retirement."*

**Helpful Links**

Written statements - Written questions, answers and statements - UK Parliament

PASA releases Dashboards Values Guidance – The Pensions Administration Standards Association (pasa-uk.com)

Make time to get your data pensions dashboards-ready (thepensionsregulator.gov.uk)

# Annual funding statement

## Key messages from TPR's Annual Funding Statement 2023

The 2023 annual funding statement provides guidance for valuations with effective dates between 22 September 2022 and 21 September 2023 (Tranche 18 schemes).

There are a number of key messages from the Pensions Regulator (TPR):

- Most schemes have improved funding levels through a combination of investment out-performance from return-seeking assets and a significant rise in gilt yields. Trustees will need to consider if their long-term targets remain appropriate.
- If funding levels have improved significantly, trustees should consider whether continuing with the existing strategy and level of risk is in the best financial interests of their members and beneficiaries.
- Funding levels will have fallen for a small number of schemes, Trustees should reset funding and investment strategies to reach their long-term targets and should review their operational governance processes to ensure future resilience. Trustees, their investment managers and advisers should read TPR's LDI guidance for more information.
- The level of risk that trustees decide to build into their scheme's funding and investment strategies should be supported by the employer covenant. It is important to avoid complacency when monitoring the employer covenant, ensuring effective information sharing protocols are adhered to, and assessing the impact of any changes.

TPR splits schemes into three groups:

| Group 1<br>Funding at Buyout or above | Group 2<br>Funding between Buyout and Technical Provisions | Group 3<br>Funding below Technical Provisions |
|---|---|---|
| •Consider whether to secure terms with an insurer or run the scheme on? consider risk/reward strategies of all options for members and employer.<br>•Note capcity of insurer market and likely increased timescales. | •Ensure the long-term funding target remains appropriate given funding position and covenant.<br>•If Trustees don't have a long term funding target in place one should be agreed as a matter of priority. | •Focus on bridging the gap to Technical Provisions.<br>•Ensure the funding plan is consistent with the covenant.<br>•If the funding position has improved, understand how this fits in with long term plan and any action that should be taken. |

Other points to note:

- Investment Strategy. TPR note a number of points around illiquid assets – Trustees should take advice to make sure these assets are still appropriate. Trustees should also consider ability to meet LDI collateral calls.
- Covenant. On average, covenant is likely to improve due to reductions in scheme size. However there are a number of negative impacts on covenant including low economic growth, high borrowing costs and high energy costs. Trustees should ensure they understand the covenant, and the period of covenant reliability.
- Mortality. TPR noted that mortality has begun to stabilise following the Covid 19 pandemic. However Trustees should still approach assumption setting with care.
- Schemes with active members. TPR notes that the cost of providing benefits will have fallen significantly and these schemes may see more material changes in funding level due to their long-time horizons.

Overall, Trustees managing schemes in an integrated way - i.e. looking holistically at funding, investment and covenant - will be well placed to ensure valuations meet TPR expectations. TPRs helpful classification of schemes into bands also helps with understanding TPR expectations for specific schemes.

One eye should also be kept on the new DB funding code, which is currently expected to take effect in April 2024.

**Helpful Links**

Annual Funding Statement 2023 | The Pensions Regulator

# Pensions Regulator ED&I guidance

## Equality Diversity & Inclusion

### Thoughts from an advisor's perspective

The launch in March of TPR's guidance on Equality, Diversity & Inclusion (EDI) was a milestone for pensions. Although for many years well-run schemes have been incorporating EDI into their structure and decision making, the guidance from TPR supplied clear direction for all trustee boards, and crucially, their corporate sponsors.

The guidance from TPR is principles driven and pragmatic, recognising that while EDI issues can be complex, there are "quick and easy steps that some schemes can and should take to improve EDI now".

So how can the advisory community that exists to assist Trustees and Sponsors with their decision-making help in this area?

A good first step is to recognise that the guidance from TPR, although directed at Trustees and Sponsors, provides a great set of principles for their advisors to follow also.

One thing TPR suggest is that EDI outcomes can be improved by widening the pool of people from which Trustees are generally drawn. Advisors can support in this area by ensuring that new trustees that may not have come from a finance or legal background can receive tailored training and development as they move into their trustee role.

While Trustees hold the ultimate responsibility for running their scheme, some actions are commonly delegated to advisors. Ensuring EDI is considered as a core part of items such as running a MNT selection exercise, and designing member communications will help schemes maximise their EDI potential.

This extends to situations where an advisor acts as secretary to the trustee board and where they can help to organise and structure meetings in a way that is inclusive for all and encourages full participation from every member of the board. Where there is a risk of "groupthink" emerging, mechanisms that encourage divergent and individual thinking will help better decisions to be made. This could lead to better policy design, better investment choices, and a reduction in the risks faced by the pension scheme.

Where advisors are supporting clients in making changes to their pension arrangements or setting up new schemes, it is important to consider the wider impact of these changes in terms of their impact on their employees. There is a well-researched gender pensions gap in terms of the value of funds at retirement and similar gaps will exist when looking at different socio-economic groups. Scheme design changes that look to address this (for example when considering how maternity leave is accounted for within pension schemes, and dealing with members wishing to work part-time) will be beneficial in terms of supporting the narrowing of these gaps and promoting economic stability.

There is an enormous array of ways that pension schemes can improve their EDI impact, and the TPR guidance sets these out in a very accessible level of detail. Following these principles and challenging the status-quo will lead to better decisions being made and an improvement in the impact that individual pension schemes can make to their members, trustees and corporate sponsors.

**Helpful Links**

Governing body ED&I guidance

# Pensions Regulator update on Capita Security breach

### The 'Capita cyber incident'- What should trustees be doing?

The Pensions Regulator (TPR) has issued a Statement on the Capita cyber security incident. The regulator urges trustees to check whether their pensions scheme's data has been affected and to remain in contact with Capita as the situation evolves. The Statement also includes a reminder about TPR's cyber security guidance which should be reviewed by all trustees whether or not affected by the Capita breach.

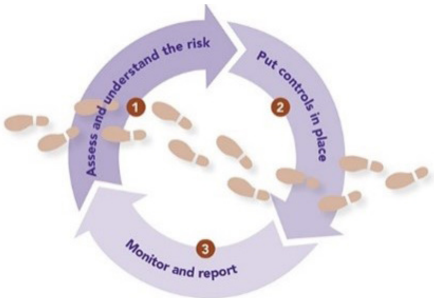
In more detail, the Capita breach occurred over the period from 22 March to 31 March 2023, with evidence showing that Capita's actions to interrupt it managed to restrict the amount of data accessed. Nevertheless, enough of a risk was created for TPR to write to pension funds asking them to check if their member data was affected.

TPR has subsequently issued a reminder to trustees of their duties relating to the security of scheme members' data.

For trustees of schemes that use Capita's services, they should check whether their pension scheme's data could be affected and ensure they continue to communicate with Capita. Trustees should also be prepared to:

- Answer questions from members who have concerns about possible data breaches.
- Keep members informed as information becomes available where a data breach has taken place.
- Proactively warn members about pension scams.
- Monitor for increased or unusual transfer requests.

For trustees of all schemes, reference should be made to TPR's cyber security guidance with a view to checking that, in line with TPR's cyber risk assessment cycle, the risk is understood; relevant controls are put in place; and there is a process in place for monitoring and reporting –




Where a data breach occurs, trustees may need to notify affected individuals and should also direct them to relevant guidance from the National Cyber Security Centre. Trustees may also need to notify TPR and the Information Commissioner's Office (IC).

More generally, this is a timely reminder of ensuring that an up-to-date information security policy is in place along with related documents (privacy notice, record of processing activity, breach log, etc.). It is also reminder of the importance of ensuring member date is secure and up to date and, if necessary, putting in place a data management plan.

**Helpful Links**

[Capita cyber security incident | The Pensions Regulator]

[Cyber security principles The Pensions Regulator | The Pensions Regulator]

# FRC publication of corporate governance code

## Consultation on new Corporate Governance Code

In May 2023, the FRC released a consultation document in relation to changes to the UK Corporate Governance Code. This consultation has been prepared following the UK Government's response to its 2021 White Paper, Restoring Trust in Audit and Corporate Governance. This paper highlighted aspects of the corporate governance regime that the government invited the FRC to consider reforming.

The main areas the consultation paper focuses on relate to:

– Risk management and internal control
– Improving functionality of the "comply-or-explain" approach to corporate reporting
– Revisions needed to reflect the responsibilities of the board and audit committee for sustainability and ESG reporting, and associated assurances - in accordance with a company's audit and assurance policy
– Updating the Code to ensure that it aligns with new legal and regulatory requirements as set out in the Government's response to the White Paper.

On pensions, the Code states –

– The board should identify in the annual report each non-executive director it considers to be independent. Circumstances which are likely to impair, or could appear to impair, a non-executive director's independence include, but are not limited to, whether a director is a member of the company's pension scheme
– Only basic salary should be pensionable. The pension contribution rates for executive directors, or payments in lieu, should be aligned with those available to the workforce. The pension consequences and associated costs of basic salary increases and any other changes in pensionable remuneration, or contribution rates, particularly for directors close to retirement, should be carefully considered when compared with workforce arrangements.

The proposed changes have been developed with engagement from stakeholders with the aim of restoring trust in audit and corporate governance. The proposed changes to the Code aim to improve accountability, build trust and support investment and stewardship decisions in the UK.

The FRC hope that there will be a wide range of stakeholders engaging in the consultation and views put forward which can improve the functioning of the Code. Responses to the consultation should be made by 13 September 2023.

To allow sufficient time for implementation, the revised Code is expected to apply to accounting years commencing on or after 1 January 2025.

Risk management and internal control

The Government invited the FRC to make amendments to the Code to strengthen board accountability and reporting in relation to internal controls. The Government has requested that there is a requirement for an explicit directors' statement regarding the effectiveness of the company's internal controls, including over financial reporting, but also about broader operational and compliance risks. This report should include:

– a declaration on the effectiveness of the control systems in place;
– an explanation of the basis for its declaration; and
– a description of any material weaknesses or failures identified and the remedial actions being taken.

The proposed changes to the Code will make the board responsible for establishing and maintaining the effectiveness of the risk management and internal control framework, emphasising the accountability of the board.

Comply or explain approach

The code uses a "comply or explain" approach to allow for flexibility and for companies to consider their individual circumstances, rather than using a legislative approach. Companies not complying will have to give clear and meaningful explanations for any departures from the Code. These explanations will need to show that the departure from the Code still complies with effective governance arrangements and maintains the application of the Code's principles.

The aim of this is to strengthen board accountability and enhance transparency and investor confidence. It will also avoid placing disproportionate burdens on businesses.

Sustainability and ESG

ESG factors are becoming important considerations for companies across the world, and there have been several amendments throughout the code to ensure it is properly considered as part of a company's governance. Revisions include:

- expanded sustainability and ESG reporting and appropriate assurance reflecting the company's Audit and Assurance Policy;
- new responsibilities for the audit committee in relation to monitoring the integrity of narrative reporting, including reporting on sustainability; and
- assurance of ESG metrics and other sustainability-related information in the annual report.
- Aligning the Code with the Government's response to the White Paper
- The Governments response to the consultation on its White Paper confirmed proposals in relation to introducing new reporting requirements:
- an annual Resilience Statement, which sets out how a company is managing its risks in the short, medium and long-term;
- a triennial Audit and Assurance Policy, which explains how the company suggests assuring non-financial reporting during the next three years;
- an annual statement containing information on distributable profits and the company's policy on distribution; and
- an annual statement on steps taken to prevent and detect any material fraud

Proposed changes have been made to the Code to improve transparency of malus and clawback provisions around directors' remuneration.

**Helpful Links**

[Consultations | Financial Reporting Council (frc.org.uk)](frc.org.uk)

# Like a Virgin (Media v NTL Pension Trustees)

After a number of false starts, the 'section 37 question' finally went all the way to court. Judgment in the case was delivered on 16th June, leaving the industry waking up to the issue and, frankly, feeling scared and cold.

The case was about these vexed questions:

– Whether the lack of written confirmation by the Scheme Actuary that the scheme continued to match the reference scheme (the mythical scheme which you had to match to contract-out of SERPS/S2P) could scupper an amendment to the rules of a contracted-out scheme;
– If so, could it scupper amendments in relation to future service as well as past service; and
– If so, could it even scupper amendments which improved benefits?

In a judgment even less popular with the industry than Lloyds[1] (1, 2 and 3 - I think we're all hoping for better sequels this time), the court said 1. Yes; 2. Yes; 3. Yes!

**Didn't know how lost I was**

The Judgment is pretty short (at least in comparison to some pensions Judgments) but that masks a great deal of complexity. And that's because, as is common with pensions legislation, the legislation under consideration[2] is written in a very convoluted fashion (with a sort of three way effect of prohibition, permission and then prohibition again, along with definitions mixed in). And, ultimately, that legislation simply didn't make any real policy sense.

Virgin's Counsel offered the court a plethora of credible reasons to avoid a result quite so hard to swallow; in particular, by making the legislation all about the past (given it uses the words "accrued rights") which would have made it virtually irrelevant. However, instead, the court tried to make the legislation they were looking at[2] mean the same as the shiny and new legislation that was made in 2013 to "clarify" matters. In fairness, the court hadn't the hands on experience to appreciate that pensions legislation (understandably, given the complexity) sometimes just doesn't say what it should do (indeed, DWP had all but admitted as much in 2013).

The result is that those whose advisers used their hands on experience to judge what was a sensible interpretation of the muddled legislation and/or didn't give enough credence to how the words might be read, will now potentially find themselves with a problem child. The kind that seriously adds to your liabilities and causes you untold hassle in establishing what went on 20 odd years ago.

**Making it Through the Wilderness**

I don't think there is much doubt that there will be a significant number of benefit amendments that, on the basis of this case, will be void. Depending on who you ask, this could include the most fashionable amendment this millennium - closure to accrual[3]. Plainly, it could include benefit improvements (though that will be rare in this period) and it could also include schemes which have wound up, or are in the PPF or FAS.

If there is an appeal (and a hearing on this and other issues will take place during July), Virgin could fare better - as there are judges in the Court of Appeal whose practice included pensions and who may be more familiar with the established meaning of pensions-speak.

There's also a question of what exactly is needed to evidence the confirmation required. It seems clear that will fall short of a certificate but exactly what will be needed is still to be seen.

My own view is that, ultimately, DWP may need to come to the rescue and make some regulations to allow retrospective validation of amendments which did not offend the principle the legislation ought to have been aimed at (which, as I see it, was stopping schemes which did not match the reference scheme continuing to contract-out). Otherwise, there may be many schemes touched by a long awaited and dreaded judgment - admittedly perhaps not for the very first time

[1] on GMP equalisation

[2] For the period from 6 April 1997 until 5 April 2013

[3] Albeit this feels very odd, since the contracting-out certificate would have been surrendered at this point.

# Transfer Value regulations

## Are the Transfer Value Regulations working?

The government had committed to publish a review of the Occupational and Personal Pension Schemes (Conditions for Transfers) Regulations 2021 (the regulations that introduced the red, amber and green flags systems for members interested in taking a transfer) within 18 months of the regulations coming into force (i.e. by the end of May 2023). The object of the review was to determine whether the regulations remain appropriate / effective in targeting pension scams and whether they give rise to unintended consequences.

After a small delay, the results of this review have been published, with the DWP concluding that it will conduct further work with the pensions industry and the Pensions Regulator to consider if changes could be implemented to the regulations to improve the pension transfer experience but without undermining the policy intent.

To given some context to the conclusion, based on the data gathered (from over pension schemes, administrators and industry bodies), the government estimated that, from 290,000 transfers, only 1% (i.e. 2,900 transfers) had a red or amber flag present (i.e. flags which could have prevented or at least delayed a transfer). Moreover, 2,400 of those were amber flags. This leads the government to believe that:

- the low percentage of transfers with a red or amber flag (1%) indicates there has not been a disproportionate cost to business following the implementation of the regulations,
- while data suggests that the regulations have not significantly lengthened transfer times, the increase in waiting times for a Money and Pensions Service (MaPS) pension safeguarding appointment may have potential costs, and
- the original policy intent of the regulations remains appropriate.

It is disappointing that no specific proposals have been made to address issues such as overseas investments (where delays in transfers can occur simply because a member’s transfer will be invested in a pooled fund which may include such assets) and incentives (where otherwise legitimate marketing strategies can prevent a member from transferring).

That said, given the pensions industry’s concerns on the application of the regulations (particularly, the incentives and overseas investment flags), the DWP will conduct further work to consider if changes could be implemented to improve the pension transfer experience but without undermining the policy intent. Any changes are though unlikely to take effect before next year.

**Helpful Links**

Conditions for Transfers Regulations 2021: Review report - GOV.UK (www.gov.uk)

# Risk transfer

## The Risk Transfer Market

Increases in gilt yields since the last quarter of 2022 have resulted in significant improvements in funding for some schemes.

Many schemes that were on medium to long term paths to buyout can now afford to buyout now. The consequence is that the insurance market is now saturated with requests and the expectation is that buyout projects will take a lot longer to complete. Feedback from insurers is that they are now turning down over 50% of requests – sometimes well in excess of that.

Insurers are working to make pricing processes more efficient by introducing indicative pricing tools which will help them better triage cases to cope with additional demand. Insurers are also streamlining processes for smaller schemes as well as developing some interesting solutions for larger schemes that have found themselves unexpectedly ahead of their journey plan while still holding material amounts of illiquid assets.

For the three insurers most active in the market for schemes with liabilities less than £100m, the current position is as follows:

- Just have a good streamlined pricing model for smaller transactions. They are usually able to take on up to 20 schemes each month and can turn an indicative price into a guaranteed premium within 2 weeks.
- L&G have a similar model (called "Flow"); they are more selective on which cases to quote for. If you are invested with LGIM it may help you get in the triage process.
- Aviva have historically struggled to efficiently turn indicative pricing into guaranteed quotes and are currently working on a process to do this. They are being selective at the current time while they work through a large number of implementations.

M&G are a new entrant in the bulk annuity market, although their parent company (Prudential) was one of the earliest bulk annuity providers alongside L&G. Their minimum size requirement is in excess of £300M and we expect them to be very selective while they refine their proposition and pricing.

Capacity restriction may cause Trustees look at alternative risk transfer solutions such as superfunds and capital backed journey plans (CBJP). Clara, the only superfund with regulatory approval, have yet to transact a case despite having quoted for a large number of schemes over the past 4 years. A number of CBJP contracts have been struck, but we believe they remain in single digits, despite the emergence of new providers. Regulatory changes (i.e. the development of a "Solvency UK" framework) and concerns (including the BoE's letters about the spread of asset reinsurance and the systemic risk that this could pose) may result in alternative endgame solutions gaining more traction in the future.

Trustees should ensure that any approach to market is solid to pass triage processes:

- Complete and accurate data (see our previous articles on the importance of data quality – link below)
- Benefits fully understood and legally reviewed
- Investment strategy matches intentions/covenant
- Proof of transaction intention/evidence of affordability

We expect exclusive processes with a pre-selected annuity provider (i.e. exclusivity) to become the norm for transactions up to £100m-£150m.

**Helpful Links**

[PASA data quality and the insurance market]

# PASA e-admin engagement strategy

PASA recently published an excellent paper on getting members digitally engaged. One thing they called out was,

Savers generally want to be treated as individuals and expect a personalised experience. However, traditional, and legacy methods of data capture, retention, and manual administrative processes have led to unreliable data and high costs. This means savers don’t get a seamless and joined up experience.

At Spence, we are on a mission to engage members and simplify what can be a very complex area, so this paper really resonated.

We started our journey 3 years ago when we developed and launched a smartphone app.

There were three key design principles which very much tie in with PASA’s thinking

- Easy to access
- Easy to use
- Easy to understand

**Easy to access**

We already had a member website which was accessed using the traditional username password and one time code. Typical registration rates were around 25%.

Experience showed that people struggled with this process, and it could be a barrier to getting them online. It doesn’t matter how good you member experience is if you can’t get people into it. There was also the issue of people forgetting passwords once registered.

Our phone app uses a unique QR code in place of the password. Scanning this and adding their own National Insurance Number allows most members to download and register in less than a minute. Selecting a 4-digit PIN allows them to re-enter the app.

Feedback from members has been strong on the registration process. The ultimate proof is that we have seen registration rates as high as 71% for one scheme.

**Easy to use**

Having got the member online its vital to make it easy for them to quickly get the information they need and allow them to interact with the administrator.

The design of the app allows for easy access to live benefit information and a current Transfer Value.

One benefit of the smartphone route is that members can use the phone’s native capabilities such as messaging. It’s a modern convenient way for people to communicate and we are seeing high usage.

Its also  quick and easy for members to update personal details which is a great way to improve data quality.

**Easy to understand**

Pensions is full of jargon and with the average UK reading age being 12 it’s vital to avoid this.

Our approach is to simplify giving people the “helicopter view” of rules with access to more detail as suits the member.

We also use short animations to explain complex topics.

It’s important however to recognise the limitations of any digital service so experienced administrators are only a phone call away.

**Build it and they will come.**

We track weekly usage of the app which ranges between 15% to 30%. That's significant usage, proving that if you get the design right you can get members online in a way that works for them.

**Helpful Links**

PASA releases Guidance on creating an eAdmin engagement strategy – The Pensions Administration Standards Association (pasa-uk.com)

# Investment Update

**Market Review**

The second quarter of 2023 bought into focus the idea that the journey to economic recovery may be a long and windy road!

Given the backdrop of 2022 and early 2023 investors entered the quarter with the expectation of a looming recession and the potential for rate rises to level off. In actual fact inflation remained stubbornly high, despite prior rhetoric of its short term presence many central banks continued with the policy of increasing short term borrowing rates. Against this backdrop both shares (with the exception of the US and Japan) and bonds delivered disappointing returns as investors priced in further interest rate rises and an increased risk of recession.

**Global markets**

Global equities edged higher over the quarter, driven by the US and Japan, with a noticeable rebound in mega-cap stocks (which underperformed in 2022), whilst emerging market regions continued the trend of lagging behind. The UK and Asia Pac region (excl Japan) delivered negative returns over the period.

Credit and government bonds are yet to recover from the "crisis" in 2023, with longer dated UK government bonds particularly impacted falling a further 6% in value over the quarter. Those few asset classes that delivered positive returns last year, such as commodities (driven by energy price increases) have struggled year to date. This inflection in performance shows the importance of reviewing portfolios on a regular basis and ensuring portfolios remain diversified.

Many central banks continued the movement of raising interest rates to combat inflationary pressures although the Fed bucked the trend and held rates in June. In almost all regions government bonds yields rose and prices fell.

**UK**

UK equities fell over the quarter following heightened recessionary risks and continued hawkish comments emanating from the Bank of England (BoE). The Bank continued its strategy of rate rises during May and June. The most recent surprise 0.5% increase was viewed by some commentators as an attempt to shock the economy to combat continued and stubborn inflation. The action of the Bank suggested controlling inflation in a steady measured way remains somewhat aspirational, which resulted in UK gilt yields rising further (falling prices) to levels last seen during the during the "gilts crisis" in late 2022.

By the end of the quarter, gilt yields had again fallen slightly suggesting investors viewed the action taken by the Bank as potentially being successful in taming inflationary pressures, albeit with the impact of potentially forcing the economy into a recession.

Following the market volatility in autumn 2022, the Pensions Regulator (TPR) has published new guidance on the practical steps trustees should take to manage risks when using leveraged liability-driven investments (LDI). The guidance sets out that TPR expects trustees to invest only in leveraged LDI arrangements where there is an appropriately set of conditions including:

- Being very clear where LDI fits within a scheme's investment strategy both longer term goals as well as shorter term issues such as liquidity
- Setting, operating and maintaining a collateral buffer including ongoing testing for resilience
- Making sure schemes have the right governance and operational processes in place
- Ongoing monitoring of all the above

Whilst many schemes will have been considering these points the compliance across the industry will not have been uniform partly because of the structure of the Trustee function, it's legacy attitude and the input of it's adviser. We will be putting in place additional controls to make sure that an appropriate level of governance is included in annual business plans and in budgets and that the work is then undertaken. As always we are comfortable to engage with the Sponsor on these matters.

Also, the Work and Pensions Committee (WPC) has published a report on DB pension schemes with LDI investments. According to the WPC more still needs to be done to address significant weaknesses in the ability of defined benefit pension schemes to manage risk. The report warns that investments must never again be allowed to jeopardise the stability of the UK economy as they did during the events of September last year.

**US**

The US market performed strongly in local currency terms, up 9%. These gains were almost entirely due to a rebound in mega-cap stocks which make up a very large proportion of the US market.

The dollar weakened against sterling during the quarter, as a consequence of higher base rates implemented by the BoE.  As a result investors hedging US exposure back to sterling would have received 6% in sterling terms.

US inflation fell, due to the observed 2022 oil price increases falling away, allowing the Fed to pause any rate increases in June.

**Euro**

Eurozone shares posted positive returns, returning 3% over the period.

Like the BoE, in order to combat higher inflation, the European Central Bank (ECB) raised interest rates twice over the quarter, despite this inflation crept up over the period, increasing the probability of a recession in the region.

**Japan**

Japan was the best performing equity market over the quarter in local currency terms. The region benefitting from a weak yen, as a result of relatively low interest rates in Japan compared to other countries where rates have risen.

The Bank of Japan (BoJ) met for the first time under their new governor which led to little policy change suggesting the Banks dovish position appears set to continue.

**Asia (ex Japan)**

Asia (ex Japan) equities recorded negative returns during the second quarter. Weak demand for exports following interest rate rises in the US and Europe dampened returns.  Within regions technology stocks (linked to AI-related firms) drove returns.

**Emerging markets**

EM equities generally lagged developed markets, although delivered a marginally positive return over the period. Concerns over China's reopening held back the region in general.

**Fixed Income**

Within fixed income, credit assets delivered muted returns, failing to recover lost ground in 2022, with investors facing up to the fact that rates aren't likely to come down any time soon.   Higher yields continued with elevated inflation data, hawkish central banks and rising interest rates.

Assets at the riskier end of the spectrum, high yield and emerging market debt drove returns, whilst defensive classes retracted.  UK Gilts in particular suffered with inflationary concerns and BoE actions taken to address this, likely to mean rates are likely to stay higher for longer.

**Summary**

The volatility and dispersion of asset class returns demonstrates the importance of diversification in portfolio construction.  Increased base rates, brings cash back to the table as a strategic allocation, pending investment in undervalued asset classes, but doing so without the historic impact of return dilution.

Enhanced yields also means fixed-income investments are potentially more attractive than they have been for a number of years.

For schemes which have had underhedged positions, elevated gilt yields and the outlook for rates to remain higher for longer presents an opportunity to lock in potential reduced deficits.

The outlook suggests things remain rocky and the journey ahead may have a number of turns to take.

**Helpful Links**

Defined benefit pensions with Liability Driven Investments - Committees - UK Parliament

# DC update

## Supporting DC savers

The Pensions Regulator (TPR) has published a guidance statement setting out how trustees of defined contribution (DC) schemes should communicate and support savers in the current challenging economic climate and how they can strengthen the governance and oversight of DC schemes and ensure their investment strategies support stronger saver outcomes.

The guidance statement takes many of its key themes from TPR's DC code of practice and associated guides on investment governance and communicating and reporting. It also builds on TPR's earlier statement on managing investment and liquidity risk in the current economic climate, which focused on the issues TPR expects trustees to consider when managing investment and liquidity risks in the face of current market conditions.

Although DC schemes do not involve leverage in their investment strategies and have not been affected by the issues facing liability-driven investment (LDI) funds, DC savers are not immune to market events. Significant market volatility from both equities and falling bond values, along with increases in inflation and interest rates, has affected those accessing their pension savings.

In the guidance statement, TPR says that, while those who are early in their saving journey can take a longer-term view on their investments, savers who are close to retirement could be impacted depending on the investment strategy of their scheme.

Savers in 'lifestyle' funds need to understand whether the strategy they are in, as they approach retirement, is consistent with their plans on how they intend to access their retirement benefits.

Trustees should also communicate with savers to help them understand what a fall in their DC pension means for them, depending on their personal circumstances, and to avoid making hasty decisions that could lead to risks such as being victims to pension scams.

In particular, trustees can direct people to the Money and Pensions Service's MoneyHelper service, which offers free, independent help and guidance for people of all ages and includes free guides, a pension calculator and free appointments or those over 50 with an expert via Pension Wise. MoneyHelper can also help people find a regulated financial adviser, if they need one, to make a final decision. From 1 June 2022, schemes have been subject to requirements to 'nudge' members to Pension Wise when they are accessing or transferring to access flexible (DC) benefits. In addition, just before going to print, the Pensions and Lifetime Savings Association (PLSA) has published 'Supporting savers through the cost of living crisis'; a resource for pension schemes, which is intended to provide guidance to schemes that wish to share additional information with savers struggling due to the increased cost of living; including pension credit, cost of living payments, help with energy costs and childcare, and income support.

On a related note, the DWP has just launched a new 'Midlife MOT Website' to aid older workers with financial planning, including understanding their money, pension and any debt; to help workers with health guidance; and to evaluate what their skills mean for their careers and futures.

TPR has also reminded trustees about the importance of annual benefit statements (and accompanying information and guidance) as part of member communication, suggesting that trustees consider follow-up targeted communications as part of a continuous process. The regulator states that *"Trustees should consider what information and guidance goes alongside those statements to help savers, but within the format requirements for simpler annual benefit statements, where these apply."*

While acknowledging there is no one-size-fits-all answer, TPR expects all trustees to consider the issues raised in the guidance statement and take appropriate action as part of their ongoing governance responsibilities.

**There is a handy checklist for trustees to develop an action plan (see the links, below).**

Separately, TPR has published the results of a survey, stating that too many defined contribution (DC) schemes, especially smaller ones, are failing to meet expectations on assessing value. The survey results showed that only around one-quarter (24%) of DC schemes met TPR's key governance requirement and that there is a lack of awareness from small schemes around the Value for Money (VfM) assessments, with smaller schemes also less likely to take action on financial risks caused by climate change than larger ones.

Also, while we eagerly wait for the outcome of the consultation on the new Value for Money (VfM) framework and the metrics to measure VfM, the general 'new' direction of travel for engaging members is the promise of tide of digital connectivity, which seems, initially at least, to be based around delivering what has been discussed for a number of years; connecting digital Banking and Pensions to enable Open Finance to provide members with a more holistic view of their overall finances. However, the development of the Dashboard, which is now intended be live from October 2026, seems to be accelerating this progress and which, together with the development of AI, has the potential to revolutionise how pensions are administered and communicated, in order to create good member outcomes.

Finally, ahead of the Chancellor's Mansion House speech, some of Britain's biggest DC pension providers have agreed a voluntary pact, estimated to be covering two-thirds of the DC pensions market, to commit 5% of their investments to private equity and early-stage businesses. This will potentially invest up to £50bn by 2030. The Chancellor's speech is expected to develop his "budget for growth" and the promised package of measures by the autumn, setting out a series of reforms intended to channel tens of billions of pounds of Britain's pensions savings into high-growth companies.

**Helpful Links**

Supporting defined contribution savers in the current economic climate | The Pensions Regulator

DC code of practice | The Pensions Regulator

Investment DC pension schemes | The Pensions Regulator

Communicating reporting DC pension schemes | The Pensions Regulator

Statutory guidance: Simpler annual pension benefit statements - GOV.UK (www.gov.uk)

Check the status of your work, health and money - Midlife MOT (jobhelp.campaign.gov.uk)

# Coming up next

Half of 2023 is gone… how did that happen!? Perhaps this writer is just getting old, but the pace of the passage of time is truly terrifying. Which, I suppose, is the whole rationale behind this Quarterly Update and, in particular, this ever-present piece where we look at what is Coming Up Next in the pensions calendar.

When drafting this traditional end to our report, one can sometimes question including some of the key dates and events as they simply feel too far away. "Winter 2023, April 2024, Summer 2024… sure they are ages away! We have an actuarial valuation to sign off this week, our investment manager selection is in two weeks and there is a trustee meeting at the end of the month… I don't have time to worry about Summer 2024!" All perfectly natural reactions but, with how time passes, it is amazing how quickly Summer 2024 can be upon us.

So, as ever, we end the Quarterly Report by offering up a brief summary of those future events – both near and far – that we think you should be preparing for. We urge you to take a beat, move your focus (temporarily) from the urgent, should-have-been-done-yesterday tasks on your to-do list, and ponder what needs to be put in place to deal with tomorrow's onrushing issues.

## TPR General Code of Practice

- Patience is a virtue. A favourite line of my mother's, which is certainly a line that is being tested by the wait for the General Code, first consulted on in 2021.
- While Spring didn't bring the publication, DWP have said it will be this year and it surely cannot be far off.
- If trustees hadn't started preparing for the General Code (previously the Single Code), now is definitely the time to review the requirements and get an ESOG in place. They should also be preparing for their first own-risk assessment (ORA), as this will need to be completed within a year of the General Code coming into force.
- Who knows, by the time this Quarterly Report has been published, the General Code may be before Parliament and be coming into force within 40 days. Good things come to those who wait. Another favourite of my mother's!

## Online Safety Bill

- This Bill is focused on establishing a regulatory framework for certain online service providers, creating new offences relating to online harms, including offences of false communications. While certainly not focussed on pension scams, the provisions of the Bill will be useful in tackling pension scams before members become victims.
- The Bill will require search engines, websites and social media platforms to tackle illegal activity, with a legally enforceable duty to remove suspected scammers and scam adverts immediately on notification. These online providers will need to improve their due diligence processes, to make it more difficult for scammers to advertise and propagate pension frauds online and via paid adverts.
- While there may not be direct requirements on pension scheme trustees or employers from the Bill, it should serve as a reminder for schemes when communicating with members, to flag the dangers of pension scams, and in particular via social media adverts.

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

- **Summer 2023 –** Economic Crime and Corporate Transparency Bill expected to receive Royal Assent, bringing in requirement that corporate professional trustees to ensure all of their directors are 'natural' persons.
- **Summer 2023 -** Royal Assent for the Finance Bill bringing in changes to the Annual Allowance and prospective abolition of the Lifetime Allowance.
- **Summer 2023 –** Royal Assent is also expected for the Online Safety Bill.
- **Summer 2023 –** The phased compulsory on-boarding of schemes to the pensions dashboard was due to begin, but we are now expecting a revised staging timetable to be published.

- **1 October 2023 –** New ‘AS TM1’ assumptions for money-purchase illustrations.
- **October 2023 –** the new DB scheme funding regulations should be available with new requirements coming into force for schemes with valuation effective dates from April 2024.
- **Autumn/Winter 2023 –** revisions to scheme and employer-related events notifiable events, we well as the introduction of new declarations of intent.
- **Autumn/Winter 2023 –** Royal assent for the Data Protection Bill is expected, which will replace the EU’s data protection laws following Brexit.
- **6 April 2024 –** the Lifetime Allowance will be abolished.
- **Summer 2024 –** Requirement for schemes, with more than 100 members, to undertake their first Own Risk Assessment (ORA) and publish it by April 2025.

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