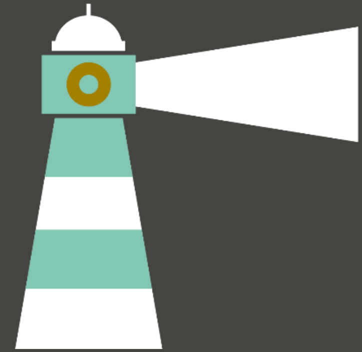
BRIEFING



What's Happening in Pensions

Issue 85 – November 2020

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Climate change: The Joint Government-Regulator TCFD Taskforce has published an interim report and roadmap for implementing the recommendations of the Task force on Climate-related Financial Disclosures (TCFD). The timetable for occupational pension schemes was already known but there are newly announced timings for asset managers and certain categories of company. There have been a number of other developments in this area, too, including a new TCFD consultation on forward-looking financial sector metrics.

RPI reform: The government and UKSA's response to their joint consultation on the timing of alignment of RPI with CPIH will be published alongside the government's Spending Review on 25 November 2020.

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DC member guidance: The government has published a policy paper confirming that it will be introducing regulations to require DC scheme trustees to refer members to pensions guidance when they apply to draw or transfer DC or cash balance benefits and to check if they have taken it or chosen not to do so.

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Investment consultancy and fiduciary management: A government web page update gives more detail on how trustees should certify to the CMA, by 7 January 2021, that they are in compliance with the requirements of the CMA's order in respect of setting objectives for investment managers and tendering for fiduciary management services.

Cyber security: PASA has published new cybercrime guidance for pension administrators.

VAT and DB schemes: The European Court has given its judgment in the *United Biscuits* case. The United Biscuits DB pension scheme argued unsuccessfully that the fees it paid to a non-insurer investment manager should not be subject to VAT because the same services provided by an insurer were VAT exempt (before a change of law from April 2019).

Public sector scheme indexation: The government is consulting on proposals for the future indexation of public sector pension scheme members' DB benefits including GMPs. The uncapped indexation that these schemes currently provide, on a temporary basis, avoids GMP equalisation issues but is expensive.

Sole corporate trusteeship: The Association of Professional Pension Trustees has published a voluntary code of practice for professional corporate sole trustees.

GMP equalisation – transfers-out

The High Court has given its latest judgment in the *Lloyds Banking Group* GMP equalisation case. This judgment addresses equalisation requirements for occupational pension schemes in respect of unlawfully unequal transfer payments they have made in the past. It also has implications in respect of transfer values that were underpaid for other reasons.

Mr Justice Morgan ruled that trustees are under a legal duty to make top-up transfers, including interest at 1% above base rate per annum, where they have made an individual statutory cash equivalent transfer in respect of benefits accrued between 17 May 1990 (the date of the European Court's Barber judgment) and 5 April 1997 (when GMPs stopped accruing) and where the calculation of that transfer payment was incorrect because it did not reflect a GMP equalisation requirement. Non-statutory transfers and bulk transfers are subject to different legal considerations; the position as to whether trustees are obliged to top-up transfer values in those cases may vary depending on the circumstances.

Furthermore, the judge ruled that there is no statutory limitation period to time-bar a member's claim to a correct transfer value and the Lloyds Bank schemes' various transfer discharge forms and forfeiture clauses did not operate to deny a member's right to bring such a claim. The Lloyds schemes therefore appear to be subject to member claims for a supplementary transfer for an indefinite period unless the trustees take proactive steps to determine and resolve such claims. The same may well be true for many other schemes, although this depends on a careful analysis of the scheme rules, member communications and wider circumstances.

It will not be a simple matter to calculate and pay top-up transfers for former members who took a transfer payment on an unequalised basis. There will clearly be significant issues with access to available and accurate data to calculate such additional amounts, and also with identifying and tracing former members who may have such a claim (assuming trustees wish to take a proactive approach to resolving such issues). In any event, the additional liabilities potentially payable as a result of this decision will need to be considered when preparing scheme valuations and by employers in respect of their corporate accounts.

The judgment indicates that trustees may be able to agree with members that their claim can be resolved by providing an alternative scheme benefit or even perhaps by cash compensation. However, this may give rise to additional legal complexities which do not appear to have been fully explored in the case.

The judgment leaves a number of questions and practical matters unresolved. We are continuing to consider the implications.

Pensions Regulator guidance on preparing for corporate distress

The Pensions Regulator has published new guidance for DB scheme trustees on being ready for possible sponsoring employer distress. This builds on existing integrated risk management (IRM) guidance and is being issued now due to the expectation of significant levels of employer distress and heightened corporate activity in the wake of the COVID-19 crisis and also the end of the Brexit transition period.

Trustees are told that they should be ready to act quickly if they spot warning signs of employer distress or insolvency, many possible examples of which the guidance lists (see Annex 2 to the guidance). They should be actively monitoring the employer's health to look for any such warning signs and should be watchful for other stakeholders seeking to improve their position, often to the detriment of the scheme. Conversely, there may be opportunities to improve the scheme's position that can be investigated. Trustees should promptly seek appropriate advice from relevant advisers based on the developing situation. They should be mindful of actual and potential conflicts of interest and have procedures in place to address them.

The guidance includes (among others) the following sections:

- Best practice IRM approach (this section draws from existing IRM guidance)
  - Understand legal obligations to the scheme (Annex 1 to the guidance lists a number of aspects to consider)
  - Ensure effective risk management processes are in place
  - Review scheme governance
- Sponsor showing signs of financial distress
  - Knowing your sponsor's industry challenges
  - Increasing the frequency of covenant monitoring
  - Performing a detailed review of the scheme's position
  - Reviewing your investment strategy
  - Understanding the role of other stakeholder interests
  - Considering employer requests for scheme easements (e.g. contribution deferrals)
  - Information sharing
  - Transaction activity
  - Communicating with members
  - Being alert to scams and unusual transfer activity
- Sponsor facing the prospect of insolvency
  - Practical steps
  - Restructuring plans for employers in financial difficulty
  - Notifiable events

Annex 3 to the guidance considers some example scenarios: lenders seeking or enforcing security ahead of the scheme; a request for a deficit recovery contributions easement; and an employer selling a valuable business.

Pension Schemes Bill

The Pension Schemes Bill has passed its House of Commons stages.

The proposed new criminal offences, including a broad one of conduct that puts accrued scheme benefits at risk, were briefly debated at the committee stage. Scottish National Party amendments which were intended to limit the scope by introducing a requirement for negligence were rejected by committee vote. The Pensions Minister held firm on the existing Bill clauses, based on the inclusion of the reasonable excuse defence, saying that the Pensions Regulator would

have to prove that an excuse is not reasonable and will be consulting on draft guidance. He agreed to engage in further discussions.

Other matters considered in detail were collective DC schemes, pensions dashboards, scheme funding and pension scam transfer protections. As expected, the House of Lords' non-government amendments were overturned so the Bill once again reflects government drafting in all respects.

On transfer scam protections, the Pensions Minister has written to the chair of the Work and Pensions Select Committee confirming that there will be a consultation on regulations setting out 'red flags' that will allow trustees to stop suspicious transfers.

The Bill is now in its "ping pong" stage, where the Commons and Lords will seek to resolve their differences. It seems unlikely that the Lords will hold sway on any of the outstanding issues, meaning that Royal Assent is now close.

DB consolidators

The Pensions Regulator has published new guidance for trustees and employers who are considering transferring their DB scheme to a superfund (DB consolidator scheme) or similar model.

This replaces the December 2018 separate guidance for trustees and employers (see WHiP Issue 74). Among other things, the guidance reiterates that a transfer to a superfund is a 'Type A event' under the Regulator's clearance guidance and accordingly it expects employers to apply for clearance. It also repeats that employers should pay for advice to the trustees.

The guidance focuses on the suitability (or otherwise) of superfunds as an endgame solution, including the gateway tests for being permitted to transfer to a superfund that were proposed in February 2019 by the government (see WHiP Issue 74 – the consultation response is still awaited). These were adopted in the Regulator's interim guidance for superfunds themselves (see WHiP Issue 82). Only transfers to superfunds that are schemes approved for this purpose by the Regulator should be considered: a list is expected to be published on the Regulator's website shortly.

The Pensions Minister said in a speech to the PLSA conference that he is expecting there to be another Pension Schemes Bill in the current Parliament to include provisions on the regulation of superfunds.

Climate change

The Joint Government-Regulator TCFD Taskforce has published an interim report and roadmap for implementing the recommendations of the Task force on Climate-related Financial Disclosures (TCFD). The broad aim is to make TCFD-aligned climate risk disclosures mandatory across the UK economy by 2025 at the latest and with a significant number of mandatory requirements in force before then, by 2023.

The government has already consulted on proposals and a timetable for occupational pension schemes (see WHiP Issue 84). The new announcements in this interim report and roadmap concern UK-authorised asset managers (see our Financial Services and Markets department's briefing note); listed and large companies; and banks, building societies and insurers – including personal pension providers.

The report and roadmap conspicuously do not mention implementation of the EU Sustainable Finance Disclosure Regulation (SFDR), at least not in 2021, which suggests that the government's TCFD approach may currently encompass everything it will be doing in this area. (EU member states are required to implement SFDR by 10 March 2021 – see WHiP Issue 83.) TCFD disclosures are much narrower in scope than those under SFDR: TCFD only addresses climate change risks whereas SFDR covers a much fuller range of ESG issues.

In other developments:

- Correspondence about climate-related disclosure requirements for asset managers and contract-based pension schemes, between the FCA and Pensions Minister, states that the FCA will be consulting shortly on rules for asset managers and contract-based schemes and will be mindful in particular of the information that occupational pension schemes will need from their asset managers in order to meet their developing regulatory obligations.
- TCFD is consulting on forward-looking financial sector metrics. See our briefing on this consultation here.

- The Chancellor announced that the government will issue its first sovereign green bond.
- The same announcement also said that the Chancellor hopes to launch the UK's first Long-Term Asset Fund within a year, to encourage investment in long-term illiquid assets such as infrastructure and venture capital.
- The Pensions Minister has written a foreword to a report by the Association of Member Nominated Trustees on shareholder voting, in which he says he is determined to bring about real change as regards trustees' ability to influence voting where they invest in pooled funds. He agrees with the report's recommendation that there be a working group to develop solutions.
- A 'Responsible Investment Bill' is being proposed by ShareAction, with the support of the All Party Parliamentary Group on Sustainable Finance, chaired by Liberal Democrat leader Sir Ed Davey.

Our Sustainable Business Hub has a number of useful resources on this topic and is being regularly updated.

RPI reform

A letter from the Chancellor of the Exchequer to the Chair of the UK Statistics Authority (UKSA) Board states that the government and UKSA's response to their joint consultation on the timing of alignment of the Retail Prices Index (RPI) with CPIH (the Consumer Prices Index including owner-occupied housing costs) will be published alongside the government's Spending Review on 25 November 2020.

Subject to certain requirements, the UKSA is able to align RPI with CPIH from 2030 and has indicated that it is minded to do so. The Chancellor's consent is needed to make such change any earlier. The consultation was principally on the possibility of making the changes before 2030, but not before 2025. See WHiP Issue 81 for more background.

DC benefit statements

The government has published a response to its October 2019 consultation on simplifying DC scheme annual benefit statements (see WN Issue 78). It will require DC schemes that are automatic enrolment 'qualifying schemes' to issue simpler annual statements based on a template.

A consultation will follow shortly, in which the government will propose using the PLSA's two page template which has been endorsed by the Pensions Regulator. There may also be a mandatory DC benefit statement 'season', such that members receive all their DC statements at around the same time.

The government does not intend to require the statements to include detailed information on costs and charges: this information will be communicated by signposting members to the information that such schemes are already required to publish.

DC member guidance

The government has published a policy paper confirming that it will be introducing regulations under the Financial Guidance and Claims Act 2018 to require DC scheme trustees to refer members to pensions guidance when they apply to draw or transfer 'flexible benefits' (i.e. DC or cash balance benefits) and to check if they have taken it or chosen not to do so. There will be a consultation first and the Pensions Regulator has indicated that it will be producing guidance for trustees.

There is already a requirement to signpost to Pension Wise guidance in certain similar circumstances. The government is therefore calling this a "stronger nudge". It concluded from a research report on retirement planning and decumulation behaviour that trials demonstrate that such nudges are effective.

The FCA will be introducing parallel rules for personal pension providers.

Pension scams

The Pensions Regulator is asking schemes, providers and administrators to pledge to make certain commitments to help protect scheme members from scams. These are based on principles of the Pension Scams Industry Group Code of Good Practice on Combating Pension Scams (see WHiP Issue 76).

It says:

"To make the pledge you should commit to:

- *regularly warn members about pension scams*
- *encourage members asking for cash drawdown to get impartial guidance from The Pensions Advisory Service*
- *get to know the warning signs of a scam and best practice for transfers by completing the scams module in the Trustee Toolkit and encouraging all relevant staff or trustees to do so; studying and using the resources on the Financial Conduct Authority (FCA) ScamSmart website, our scams information and the PSIG code; considering becoming a member of the Pension Scams Industry Forum by contacting PSIG*
- *take appropriate due diligence measures by carrying out checks on pension transfers and documenting pension transfer procedures*
- *clearly warning members if they insist on high-risk transfers being paid*
- *report concerns about a scam to the authorities and communicate this to the scheme member"*

Pensions dashboards

A Pensions Dashboards Programme progress report says that the initial public launch has been delayed until 2023. An initial version of the proposed data standards for dashboard providers is expected in December 2020.

Coronavirus - Job Retention Scheme / Job Support Scheme

The Coronavirus Job Retention Scheme (furlough), which was due to end on 31 October 2020, has been extended following the announcement of the new lockdown period in England. The extension as originally announced was "until December" but the Chancellor announced on 5 November that it will last until 31 March 2021. Pension contributions (and National Insurance Contributions) are not covered. (They ceased to be covered under this scheme after 31 July 2020.) Our Employment department's updated briefing is here.

The Job Support Scheme that was due to start on 1 November 2020, when the Job Retention Scheme was due to end, has accordingly been postponed and might never be commenced. Pension contributions are not covered at all under either element of this scheme.

The Pensions Regulator initially updated its COVID-19 guidance on automatic enrolment and DC pension contributions and DC pension contributions technical guidance for large employers, to address the Job Support Scheme. These changes were, however, reversed when the Job Retention Scheme was extended.

Coronavirus – temporary fund closures

The Pensions Regulator has amended its DC scheme management and investment: COVID-19: guidance for trustees in relation to the 'gating' (temporary closure) of funds and the risks of creating an unintended DC default arrangement.

The Regulator had previously covered in this guidance the implications of gating, including that trustees who redirected contributions from a member option fund to a replacement fund might thereby be turning the replacement fund into a new default arrangement (see WHiP Issue 82). That would mean that charge cap, statement of investment principles and information requirements for default funds would apply to the replacement fund selected by the trustees.

The latest update to this guidance addresses the movement of contributions and assets accrued in the replacement fund during the gating back into the gated fund when the latter reopens. The Pensions Regulator indicates that this switch is less likely to make the original fund into a default arrangement because the member did originally choose it, although this will depend on what has been communicated to members previously. The guidance says:

> *"We would expect that the pre-existing expression of choice will still apply where members have either:*
>
> - *consented to the redirection of the contributions on a temporary basis, until the original fund ceases to be gated*
> - *been informed by the trustees that their contributions are being diverted into a default fund but that this will be corrected as soon as the original fund reopens*
>
> *We would anticipate that a pre-existing expression of choice could also be preserved in the following circumstance. Members whose contributions have been diverted are informed that, in the trustees' view, the pre-existing expression of choice remains in place and they are given the opportunity to object before those contributions are redirected back into the original self-select fund.*
>
> *If, having taken legal advice, you determine that the pre-existing expression of choice no longer applies, we would expect members to be contacted and offered the option of completing a new expression of choice to enable contributions to be re-directed back to the original self-select fund. However, if contributions are directed back to the original fund without obtaining a new expression of choice from the member, that original fund would fall within the definition of a 'default arrangement'."*

It is also sensible for trustees to think about where to direct future contributions relating to periods after the gated fund has reopened. The guidance does not discuss this issue in detail but it is likely that many of the same considerations would apply in practice, including the validity of the member's original fund choice and the content of previous communications.

Note that (at the time of writing) the amendment dates on the Regulator's web page are not accurate: this latest update is from November, not June, 2020.

Investment consultancy and fiduciary management

A government web page update gives practical information on how trustees must certify to the CMA, by 7 January 2021, that they are in compliance with the requirements of the CMA's order in respect of setting objectives for investment managers and tendering for fiduciary management services. Please note the deadline and see our recent briefing note CMA Order: don't forget to self-certify for more information on this requirement.

Cyber security

The Pensions Administration Standards Association (PASA) has published new cybercrime guidance for pension administrators.

VAT and DB schemes

The European Court has given its judgment in the *United Biscuits* case. In this case, the United Biscuits DB pension scheme argued unsuccessfully that, on grounds of fiscal neutrality, the fees it paid to a non-insurer investment manager should not be subject to VAT because the same services provided by an insurer were VAT exempt. (This is before this was changed from 1 April 2019 – see below.)

This argument was dismissed: the European Court ruled that *"investment fund management services supplied for an occupational pension scheme, which do not provide any indemnity from risk, cannot be classified as 'insurance transactions', within the meaning of that provision, and thus do not fall within the value added tax (VAT) exemption laid down in that provision in favour of such transactions"*.

Since April 2019, all investment management services to DB schemes, even where provided by an insurer, are subject to VAT (see WHiP Issue 68). This decision therefore related to historic VAT treatment. Since April 2019, there is now fiscal neutrality (though not in the way the United Biscuits scheme wanted).

The position for DB schemes here contrasts with the provision of these same services to DC schemes, which is VAT exempt (provided that certain criteria are met).

Public sector scheme indexation

The government is consulting on proposals for the future indexation of public sector pension scheme members' DB benefits including GMPs. The uncapped indexation that these schemes currently provide, on a temporary basis, avoids GMP equalisation issues but is expensive. This interim measure expires on 5 April 2021 (see WHiP Issue 69).

One option is GMP conversion but the paper notes that this will not be possible before a decision on extending the current arrangements has to be made and legislative changes are needed. The two options under consideration are therefore extending current arrangements for another three years or (seemingly more likely) extending indefinitely.

The consultation closes on 30 December 2020.

Sole corporate trusteeship

The Association of Professional Pension Trustees has published a voluntary code of practice for professional corporate sole trustees, applicable from 1 January 2021. It was developed in consultation with the Pensions Regulator.

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