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Current issues

July 2022

Articles this month:

Embedding investment-consultant & fiduciary-manager oversight into pensions law

Draft Regulations have been laid before Parliament to bring requirements for trustee oversight of investment consultants and fiduciary managers within the corpus of private-sector pensions law.[1] If approved by both Houses, they will shift compliance-reporting and policing responsibilities from the Competition and Markets Authority (CMA) to the Pensions Regulator.

Background

Following an investigation of the market for investment consultancy (IC) and fiduciary management (FM) services to institutional investors, the CMA in 2019 made an Order requiring (broadly summarised) that occupational pension scheme trustees—

- put their FM contracts out to tender in certain circumstances; and
- set objectives for their IC providers and review performance against those goals annually.[2]

Trustees (and others) are currently required to submit compliance statements to the CMA, by 7 January in each year. However, the requirements of the CMA Order are designed to fall away automatically when replaced by equivalent provisions within the ambit of a '*relevant sector regulator*', such as the Pensions Regulator. The Department for Work and Pensions (DWP) consulted on proposals for accomplishing just that, in 2019, but resolution of the issue was put on hold during the initial stages of the coronavirus pandemic.[3]

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[1] The draft *Occupational Pension Schemes (Governance and Registration) (Amendment) Regulations 2022* <www.legislation.gov.uk/ukdsi/2022/9780348235777>.

[2] The *Investment Consultancy and Fiduciary Management Market Investigation Order 2019*.

[3] *Consultation on delivering the Competition and Markets Authority (CMA) recommendation for trustee oversight of investment consultants and fiduciary managers* (July 2019) <www.gov.uk/government/consultations/trustee-oversight-of-investment-consultants-and-fiduciary-managers/consultation-on-delivering-the-competition-and-markets-authority-cma-recommendation-for-trustee-oversight-of-investment-consultants-and-fiduciary-managers>.

Consultation outcome & legislation

The DWP has now published details of the responses to the consultation exercise and its outcome.[4] The (draft) *Occupational Pension Schemes (Governance and Registration) (Amendment) Regulations 2022* have been laid before Parliament for approval, and are set to enter into force on 1 October 2022.

The draft Regulations would supersede the CMA Order to the extent that it currently puts obligations onto the trustees of private-sector, occupational pension schemes. They would do so by establishing new governance requirements for trust-based schemes[5], and new reporting obligations[6]. Some types of scheme, most notably small self-administered schemes and executive pension schemes, are explicitly excluded from the scope of the changes.

FM services

As with the CMA Order, the draft Regulations require trustees to go through a competitive tendering process before obtaining, or continuing to receive, FM services. In broad terms, the requirement applies when the proportion of the scheme's assets that are or will be covered by an FM mandate (or mandates) reaches twenty per cent of the total assets amenable to FM. Trustees must invite at least three fiduciary managers to bid for the work.

Competitive tender processes carried out in compliance with the Order will not need to be repeated merely because of the commencement of the Regulations.

IC services

The draft Regulations also replicate the provisions of the Order that oblige trustees to set objectives for their IC providers, and review the suitability of those objectives triennially (at least) and after any significant changes in investment policy. The IC provider's performance in relation to the objectives must be assessed annually. A newly appointed IC provider will need to have a set of objectives by the end of the day on which the appointment becomes effective.

Objectives set prior to 1 October 2022, in compliance with the CMA Order, will not have to be reviewed immediately upon commencement of the Regulations, but will come up for review three years after they were established.

Consultation proposals vs final draft Regulations

There are some differences between the Regulations laid in Parliament and the DWP's 2019 consultation-draft legislation. For example,

- asset-backed contributions are now excluded (in addition to buy-in policies) when determining whether a scheme has surpassed the twenty-per-cent threshold for mandatory FM tendering; and
- '*high level commentary*' about the investment strategy from an actuary performing a funding valuation will not count as investment '*advice*' for the purposes of the Regulations.[7]

Compliance

The Pensions Regulator (rather than the CMA) would be responsible for ensuring compliance, and compliance reporting information would become part of the '*registrable information*' that the Regulator collects from trustees via its scheme returns. The Regulator will update its guidance on the trustee-oversight obligations in time for the 1 October 2022 commencement date.

The Regulator will have the power to issue a compliance notice if it thinks that a person is in breach of the requirements. The notice will specify the steps required to fix the problem. A third-party compliance notice will be available if the Regulator believes that the responsible person's failure to comply is attributable to the action or inaction of someone else.

Penalties may be imposed for contravention of the requirements or failure to heed a compliance notice. The maximum fine will be £5,000 for an individual, and £50,000 for corporate entities.

[4] <www.gov.uk/government/consultations/trustee-oversight-of-investment-consultants-and-fiduciary-managers/outcome/government-response-delivering-the-competition-and-markets-authority-cma-recommendation-for-trustee-oversight-of-investment-consultants-and-fiducia>.

[5] In the *Occupational Pension Schemes (Scheme Administration) Regulations 1996* (SI 1996 No. 1715).

[6] In the *Register of Occupational and Personal Pension Schemes Regulations 2005* (SI 2005 No. 597).

[7] The exception for high-level commentary in conjunction with actuarial valuations appeared in the CMA Order, but was not replicated in the consultation-draft legislation. It has been inserted following requests from consultation respondents.

Policy review

The draft Regulations provide for publication of a DWP review of the suitability and efficacy of the new governance requirements and the underlying policy by 31 December 2028 at the latest, and at least every five years thereafter.

It has long been the case that trustees must take advice before making most investments decisions, and can be fined as much as £5,000 per individual trustee or £50,000 per corporate body if they breach that requirement. So, compliance with the objective-setting requirements will be critical to avoid the risk of investment paralysis and regulatory penalties.

The CMA Order also places some obligations, for example concerning compliance reporting, on IC and FM providers themselves, as well as on Local Government Pension Scheme (LGPS) funds. As those requirements are not replaced by the provisions of the draft Regulations, the relevant CMA Order provisions will presumably continue to apply for now. The DWP notes that LGPS regulation is the purview of the Department for Levelling Up, Housing and Communities, which we understand may tackle the relevant aspects of the Order later this year. The CMA recommended that the Government extend the Financial Conduct Authority's 'regulatory perimeter' to cover investment consultants, but that has yet to take effect.

CDC Code of Practice finalised

The Pensions Regulator has laid the Code of Practice on the authorisation and supervision of collective defined contribution (CDC) schemes before Parliament.[8] The new code is expected to come into force before the end of July 2022 in time for trustees to apply for authorisation of a CDC from 1 August 2022.

The Regulator has also published its response to the consultation on the Code of Practice that ended in March 2022.[9]

The legislation allowing for the establishment of 'collective money purchase' (CMP) schemes, the legally defined phrase, is contained in the *Pension Schemes Act 2021* and the *Occupational Pension Schemes (Collective Money Purchase Schemes) Regulations 2022* set out the requirements for the authorisation of CDC schemes. Both come into effect on 1 August 2022. The first CMP/CDC scheme is very likely to be for Royal Mail employees.

The code contains guidance on how to apply for authorisation of a CDC scheme, and the criteria that the Regulator will use when considering those applications and during its ongoing supervision of authorised schemes. The authorisation criteria relate to—

- fitness and propriety,
- systems and processes,
- member communications,
- continuity strategy,
- financial sustainability, and,
- sound scheme design.

The code also sets out the ongoing supervision regime and the action schemes need to take if a triggering event occurs.

In response to the feedback received to the consultation, the Regulator has made several amendments to the code, including:

- making a distinction between the levels of competence expected for new or inexperienced trustees, and experienced or professional ones;
- clarifying that not all member communications need to be reviewed every year and member feedback does not need to be sought every quarter; and
- stating that the scheme administration system does not need to be fully functional at the point of applying for authorisation, but they should be developed enough to be assessed.

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8 <www.thepensionsregulator.gov.uk/en/media-hub/press-releases/2022-press-releases/tpr-on-track-to-accept-cdc-applications-from-1-august>.

9 <www.thepensionsregulator.gov.uk/en/document-library/consultations/collective-defined-contribution-code-consultation/response-to-cdc-code-of-practice-consultation>.

Guidance on the fitness and propriety criteria and how fees are to be calculated for authorisation of additional sections of a CDC scheme have been published.[10] Further guidance to support the code is expected in the future.

Trustees to assess fit with 1.5ºC increase goal

The Department for Work and Pensions (DWP) is proceeding with plans to make the trustees of some (mostly larger) pension schemes report on the conformity of their investments with the Paris Agreement climate goal.[11] It has published draft Amendment Regulations, stewardship guidance covering both trustees' statutory obligations and best practice, and an update to its existing statutory guidance on climate-risk governance and reporting.[12] The changes will apply for scheme years ending on or after 1 October 2022.

The changes are the outcome of an October 2021-to-January 2022 consultation exercise.[13] It proposed that trustees of large occupational pension schemes (in broad terms, those with assets of at least £1 billion) be obliged to adopt a '*portfolio alignment metric*' in addition to the climate-change metrics already required under recent legislation.[14] A portfolio-alignment metric is one that assesses the consistency of the scheme's asset holdings with the goal set in the Paris Agreement of limiting the increase in the global average temperature to 1.5 degrees Celsius above pre-industrial levels. The DWP proposed that trustees would have to perform such an assessment annually, '*as far as they are able*', and publish their findings online for all to see.

Some relatively minor, technical adjustments have been made to the draft legislation as a result of the consultation exercise. For example, the new portfolio-alignment-metric obligation has been brought within the scope of a relaxation of the rules for schemes that become subject to the climate-change-governance requirements part-way through a scheme year (they will be able to make use of an analysis conducted earlier in the year, before the rules applied).

The DWP has also published guidance for trustees on the mandatory and non-mandatory aspects of pension scheme investment stewardship. It says that its plans for corporate sustainability reporting will support trustees in their efforts in this area. It also indicates that the Pensions Regulator will update its guidance on the subject in time for the coming-into-force of the amending legislation.

The inclusion of a forward-looking metric should help focus trustees' attention on decarbonisation pathways and the changes that organisations are making to reduce the emissions associated with their activities. This can in turn drive stewardship action as trustees use the information to ensure that their asset managers are holding climate laggards to account, thus pushing for change.

[10] <www.thepensionsregulator.gov.uk/en/document-library/scheme-management-detailed-guidance/collective-defined-contribution-schemes/identifying-persons-for-the-fit-and-proper-assessment> and <www.thepensionsregulator.gov.uk/en/document-library/scheme-management-detailed-guidance/collective-defined-contribution-schemes/how-the-authorisation-fee-will-be-set>.

[11] *Climate and Investment Reporting: Setting Expectations and Empowering Savers—Government Response* (June 2022) <www.gov.uk/government/consultations/climate-and-investment-reporting-setting-expectations-and-empowering-savers>.

[12] *Reporting on Stewardship and Other Topics through the Statement of Investment Principles and the Implementation Statement: Statutory and Non-Statutory Guidance*; *Governance and Reporting of Climate Change Risk: Guidance for Trustees of Occupational Schemes*. For a longer summary of the proposals, see *Climate & Investment Reporting: Setting Expectations & Empowering Savers*, in *Current Issues* December 2021 <www.hymans.co.uk/insights/research-and-publications/publication/current-issues-december-2021>.

[13] *Climate and Investment Reporting: Setting Expectations and Empowering Savers—Consultation on Policy, Regulations and Guidance*.

[14] The *Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021* (SI 2021/839).

DWP seeks views on supporting members’ retirement decisions

The Department for Work and Pensions (DWP) has called for evidence on the types of support that members of trust-based defined contribution (DC) schemes need when accessing their pensions, and the options that are, or may in future, be available to them.[15]

The Government is looking for feedback on whether the legislation governing trust-based schemes should be more closely aligned with the FCA rules. Specifically, the DWP asks whether trust-based schemes should be required to provide ‘wake-up packs’ to members earlier and more often, and whether they should offer ‘decumulation investment pathways’ to help members who go into drawdown without taking advice.

Views are being sought from pension members about the information and support they receive about their pension schemes and whether it is enough to help them make informed decisions about using their funds. Trustees are asked what information they currently provide to members approaching retirement and when and how it is given. Trustees are also invited to comment on other support they provide to members accessing their pensions (e.g. tools to help members calculate sustainable levels of withdrawal), the income options or products offered and whether they see a role for collective money purchase (CMP or CDC) schemes in the decumulation market.

The call is open for responses from 14 June to 25 July 2022. Responses ‘*will inform what, if any, government action is required*’ in this area.

GMP equalisation: checklist for historical transfers

The Pensions Administration Standards Association (PASA) has published a checklist on the administration implications of past transfers out on guaranteed minimum pension (GMP) equalisation.[16] It contains a list of questions for trustees to consider when equalising transfers made in the past for the effects of GMPs. For each issue covered, the PASA gives a list of trustee decisions required and the implications for administration. The PASA hopes that the checklist will be used to ‘*inform discussion, capture decisions made and provide an audit trail.*’

The checklist highlights that, if they are not already doing so, trustees should seek advice on how to equalise transfers, and adopt actuarial factors that eliminate any GMP inequalities in respect of the period from 19 May 1990 to 5 April 1997. Leaving transfer values unequalised could have significant administrative implications.

Refreshed Actuarial Standard highlights significance of less-traditional risks

The Financial Reporting Council (FRC) has published proposed changes to *Technical Actuarial Standard (TAS) 100: Principles for Technical Actuarial Work*.[17] They would bring clarity to the existing principles and ensure that the TAS is relevant to new practices and risks.

The consultation forms Phase 2 of the post-implementation review of the sector-specific TASs following FRC’s Call For Feedback (CFF) in February 2021[18], and the Position Paper published in November 2021[19]. The FRC has confirmed that it will continue to discharge its duty to keep the TASs and other actuarial standards under review during the period before the Audit, Reporting and Governance Authority (ARGA), FRC’s successor, is created.

The consultation closes on 7 September 2022.

In line with the current version of TAS 100, the refreshed TAS 100 will be principles-based to ensure it is future proof to the emergence of new areas of actuarial work. There are 3 key changes proposed:

- The introduction of a new Risk Identification Principle;
- The inclusion of a new application section; and,

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[15] <www.gov.uk/government/consultations/helping-savers-understand-their-pension-choices/helping-savers-understand-their-pension-choices>.
[16] <www.pasa-uk.com/wp-content/uploads/2022/06/Admin-Implications-Checklist-FINAL.pdf>.
[17]<www.frc.org.uk/getattachment/43ac03b6-f183-4d29-8210-956814446ef6/-;.aspx>.
[18] <www.frc.org.uk/getattachment/9ba317dd-f728-4a01-a0e2-b4bd2d4d1ff4/TAS-CFF-Final.pdf>.
[19] <www.frc.org.uk/getattachment/0b857435-5c8f-431a-b399-5cc57f0ec935/FRC-Post-Implementation-Review-of-Technical-Actuarial-Standards_November-2021-FINAL.pdf>.

- The relocation of the Reliability Objective to the introductory section.

The new Risk Identification Principle will require members of the actuarial profession to have regard to all material risks which they might reasonably be expected to know about at the time of carrying out their work. The aim of this principle is to encourage the consideration of less-traditional risks such as climate change and other environmental, social and governance (ESG) related risks.

The new application section is designed to provide actuaries with a better understanding of how the existing high-level principles of TAS 100 should be interpreted and complied with. This section will comprise a collection of 'application statements' setting out the expectations of the FRC/ARGA, and are designed to clarify the principles of TAS 100.

To reflect the importance of the Reliability Objective to the TASs, it will be made more visible by bringing it within the introductory section of TAS 100. The purpose of this Objective is to ensure that users of actuarial information can place a high degree of reliance on the advice they receive. To that end, actuaries are obliged to ensure that the information is relevant, based on transparent assumptions, complete and comprehensible. In addition, this Objective will be included within the Glossary[20] of defined terms used for all FRC TASs.

Other proposed changes include:

- Nomenclature updates to align the TASs with the standards of the International Actuarial Association, including ISAP 1 (International Standard of Actuarial Practice 1: General Actuarial Practice)[21], by replacing the term 'user' with 'intended user';
- Alignment of TAS 100 terminology with existing insurance and pension regulation in the UK, by replacing the term 'shall' with 'must' throughout;
- Appending the relevant parts of the Glossary of defined terms—currently a separate document—to TAS 100, to allow easier reference; and,
- Miscellaneous other minor clarifications and amendments to the existing Principles.

We welcome the proposed updates to TAS 100 and the retention of the current principles-based approach. In particular, the addition of the application section should make compliance with each principle easier, which can only improve the quality of technical actuarial work. The trade-off for the inclusion of supplementary guidance within the Standard is an associated increase in length: the draft TAS has grown from five pages to eleven.

[20] <www.frc.org.uk/getattachment/76f4fd0a-6339-4453-8409-947163b7607a/Glossary-Dec-2016.pdf>.
[21] <www.actuaries.org/IAA/Documents/CTTEES_ASC/Final_ISAPs_Posted/ISAP1_Review_adopted_1Dec2018_V2_16April2019.pdf>.

Pensions dashboards: further consultation

The Department for Work and Pensions (DWP) is running a follow-up to its January 2022 consultation exercise on pensions dashboards, seeking comments on two additional issues: the point at which dashboards service should be made available to the general public, and the rules about information sharing between Money and Pensions Service (MaPS) and the Pensions Regulator.[22] It proposes that the industry be given at least 90 days' notice of the '*Dashboards Available Point*' (DAP), being the date from which the DWP (having consulted the MaPS, the Regulator, and the Financial Conduct Authority) considers that the dashboards system will be ready for open usage.

Comments on the proposals should be submitted by 19 July 2022.

We do not believe that 90-days' notice will provide enough time in which to match required resources to anticipated demands. The industry does not have the capacity to deal with the extra member engagement that dashboards are likely to generate for administrators: profitability is tight, and resourcing to meet needs at 90 days' notice will be almost impossible in the current recruitment market. We will encourage the DWP to minimise the disruption from the full market launch.

DC scheme returns: a game of two halves

The trustees of defined contribution (DC) schemes who will need to complete the Pensions Regulator's scheme return for this year will receive notices in the period from July to December 2022.[23] Those required to conduct enhanced '*value for members*' (VfM) assessments or to publish documents (Chair's statement information, statements of investment principles and the associated implementation statements, and climate-change governance reports) online will be expected to provide their returns in two parts. [24]

The trustees of schemes with 2-to-11 members are asked to make returns triennially, whilst those with larger schemes must do so annually. They must submit their responses by the due dates specified in the scheme-return notice, and the task is usually accomplished via the Regulator's online *Exchange* system.

The enhanced VfM assessment and public online disclosure obligations are relatively new, and apply, broadly speaking, to schemes in the 'larger' category.[25] The details of the assessment and the website addresses for the disclosures are part of the '*registrable information*' that must be provided to the Regulator. Whilst other registrable information will continue to be collected via Exchange (with no changes to this year's questions), the new items will have to be provided in a separate online form. Trustees should have been told whether they are required to complete the two-part return during June 2022.

Watch out for the arrival of the scheme-return notice, note the deadline for completion, and convey the information to the person responsible for the work.

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[22] *Pensions Dashboards: Further Consultation* (June 2022) <www.gov.uk/government/consultations/pensions-dashboards-further-consultation/pensions-dashboards-further-consultation>.

[23] <www.thepensionsregulator.gov.uk/en/trustees/submit-reports-payments-and-requests-to-us/scheme-return/dc-scheme-return>.

[24] <www.thepensionsregulator.gov.uk/en/trustees/submit-reports-payments-and-requests-to-us/scheme-return/dc-scheme-return/two-part-dc-scheme-return>.

[25] Enhanced VfM assessments are required only for schemes with assets worth less than £100 million. Climate-change governance reporting began to be introduced for schemes with assets of £5 billion or more for scheme year-ends after 30 September 2021.

HMRC Newsletters, June 2022

Pension Schemes Newsletter 140, from Her Majesty's Revenue and Customs (HMRC), clarifies the tax treatment of interest on arrears payments, such as those arising from guaranteed minimum pension (GMP) -equalisation adjustments.[26] In summary, the interest element is likely to be a '*scheme administration member payment*', and therefore an authorised payment for pensions tax purposes; and when paid by trustees to a UK recipient there should be no obligation to deduct tax (the payee will need to liaise with HMRC directly if tax is due).

There are also articles on migrating schemes to HMRC's new(ish) online *Managing Pensions Schemes* service, the submission of returns via that service, and the reporting deadlines in association with recent changes to 'scheme pays' (when annual allowance pension input amounts are revised retrospectively in light of new information—for example in connection with '*McCloud'* adjustments in the public sector).

The clarification about HMRC's policy on interest payments is welcome. It comes following guidance in a February 2022 *GMP Equalisation Newsletter* and the Revenue's *Pensions Tax Manual*.

[26] <www.gov.uk/government/publications/pension-schemes-newsletter-140-june-2022/pension-schemes-newsletter-140-june-2022>.