TRUSTEE KNOWLEDGE UPDATE

November 2020 – January 2021

LEGISLATION

Revaluation rates for 2021

(24 November 2020)

The annual revaluation order has been made confirming the revaluation rates to take effect from 1 January 2021. The higher and lower revaluation rates for the period 1 January to 31 December 2020 are both 0.5%.

CONSULTATIONS AND DRAFT LEGISLATION

RPI methodology reform set for 2030

(25 November 2020)

HM Treasury and the UK Statistics Authority (UKSA) have published a response to the March 2020 consultation on reforming RPI methodology, confirming that the Chancellor will not consent to the proposed change. The response document addresses some of the concerns raised in relation to DB pension schemes and acknowledges that some schemes will see a negative impact on their funding positions as a result of the UKSA's proposed reforms. It also confirms that the Government will not offer compensation to the holders of index-linked gilts.

UKSA has issued a statement confirming that it remains its intention to reform the calculation of RPI at the earliest time that it can practically and legally do so, which it considers to be February 2030.

Comment:

Now that there is more certainty as to when this change will be made, trustees will need to give further consideration as to whether it is appropriate to change transfer value calculations and actuarial valuation assumptions, as well as reviewing inflation hedging strategies.

Consultation on implementing the ban on corporate directors

(9 December 2020)

The Government has published further consultation on the implementation of the ban on corporate directors which will prevent a person from being appointed a director of a company unless the person is a "natural person", subject to exemptions to be prescribed in regulations. The Government confirms that it intends to bring forward regulations which will create a principles-based exemption whereby a company can only be appointed as a director if all of its directors are, in turn, natural persons. However, the specific proposed exemption for pension trustee companies which the industry had been expecting to be included has now been removed.

The legislation contains a period of grace so where a company already has a (non-exempt) non-natural person as a director, they will have 12 months from the ban coming into force to cease to be a director. The consultation closed on 3 February 2021.

Comment:

The proposal for a principles-based approach rather than an express exemption for corporate trustees of pension schemes could impact on some current trustee arrangements. We will need to await the detail of the regulations to understand this further, but it is to be hoped that the Government's promised pragmatic approach to the ban will not cause problems for pension schemes.

Government response to the review of the default fund charge cap and standardised cost disclosure

(13 January 2021)

In this response to the call for evidence issued in August 2020, the DWP confirms that it will not be changing the level of the default fund charge cap nor will it be including transaction costs within the charge cap at this time. It does however propose a prohibition on flat fees on AE default funds where the member's investment (in one or more pots) is £100 or less.

Guaranteed Minimum Pensions increases

(19 January 2021)

These draft regulations confirm that GMPs must be increased with effect from 6 April 2021 by 0.5%.

Automatic enrolment qualifying earnings

(19 January 2021)

These draft regulations confirm that from 6 April 2021 the earnings trigger will remain at £10,000, the lower end of the qualifying earnings band will remain at £6,240 (in line with the NIC LEL) and the upper end of the qualifying earnings band will increase to £50,270 (in line with the NIC UEL).

Trustee oversight of investment consultants and fiduciary managers

(26 January 2021)

The DWP has confirmed that the final regulations on trustee oversight of investment consultants and fiduciary managers will be further delayed until the first half of 2022. In the meantime, trustees are required to continue to comply with the CMA Order.

Taking action on climate risk: improving governance and reporting by occupational pension schemes

(27 January 2021)

The DWP has published its response to the August consultation on climate risk, together a further consultation on draft regulations and draft statutory guidance. This consultation closes on **10 March 2021**.

The proposals require trustees of schemes with £5 billion or more in assets (and all authorised master trusts and CDC schemes) to have effective governance, strategy, risk management, and accompanying metrics and targets for the assessment and management of climate risks and opportunities from October 2021 and to then report on these in line with the TCFD's recommendations. This will then be rolled out to schemes of £1 billion or more in assets one year later.

The Government has made some changes to its original proposals in response to the consultation including:

- bulk annuity contracts are to be ignored for the purpose of assessing scheme assets. However, arrangements such as longevity swaps under which the cost of specified benefits is not fully met in all circumstances will not be exempt from the asset threshold test; and
- some of the timings have been simplified and schemes will have 7 months from the end of each scheme year to prepare and publish their report.

The Government is continuing to actively consider whether schemes should in future be required to report on progress towards alignment with the goal on global average temperature rise set out in the Paris Agreement. The Government also intends to consult in due course on a requirement for authorised DB superfunds to undertake climate change governance and reporting, irrespective of the value of assets under management.

GOVERNMENT AND PARLIAMENT

Coronavirus Job Retention Scheme – further extension

(Updated 17 December 2020)

On 17 December a further extension of the CJRS to 30 April 2021 was announced. Eligible employees will receive 80% of their salary for hours not worked, up to a maximum of £2,500 per month. Employers will be required to cover all NICs and pension contributions. Please see this CMS Law-now for more information on the CJRS.

New DC disclosure and transfer requirements in the pipeline

(28 October 2020)

The DWP has published a paper setting out the Government's policy intent (referred to as 'Stronger Nudge') to encourage individuals with DC pensions to take appropriate pensions guidance. New duties will be placed on trustees to refer members to Pension Wise where they make a transfer application or ask to start receiving flexible benefits. Before proceeding with the transfer or benefit payment trustees will have to ensure that the member has either received the guidance or opted out of receiving it. There will be consultation on draft regulations in due course.

Comment:

The Government is committed to making Pension Wise a normal part of the retirement journey for DC members. These proposals will require trustees to review their transfer and retirement processes and communication materials.

Protecting pension savers – WPC inquiry

(27 January 2021)

In giving evidence to the Work and Pensions Committee inquiry into pension scams, the Pensions Minister confirmed that regulations imposing restrictions on transfer rights are likely to come into force in September or October 2021. He also said that HM Treasury is undertaking a review of the pensions advice allowance.

HMRC

Pension Schemes Newsletter 126

(4 December 2020)

This newsletter includes a 'clarification' of HMRC's position in relation to in-specie contributions following the *Sippchoice* case in May 2020. HMRC has amended the relevant paragraphs in the Pensions Tax Manual (PTM) to reflect its view that a 'contribution' for Finance Act purposes could in some circumstances be made where the trustees agree to purchase an asset from a person who has a separate obligation to make a monetary pension contribution, and the payment of the pension contribution is then effected pursuant to a contractual offset agreement.

HMRC is reviewing in-specie cases in the light of the *Sippchoice* decision. Any contribution that has been paid pursuant to an effective contractual offset agreement or where HMRC clearance has been obtained in relation to an asset-backed contribution arrangement will be unaffected.

THE PENSIONS REGULATOR

Pledge to combat pension scams

(11 November 2020)

TPR has launched a campaign, aimed at trustees, providers and administrators, asking them to pledge their commitment to combating pension scams. To make the pledge, participants should commit to:

- regularly warning members about pension scams;

- encouraging members considering drawdown to get impartial guidance;
- getting to know the warning signs of a scam and best practice for transfers by completing the scams module in the Trustee Toolkit;
- studying and using the resources on the FCA ScamSmart website, TPR's scams information and the PSIG code;
- considering becoming a member of the Pension Scams Industry Forum;
- taking 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;
- reporting concerns about a scam to the authorities and communicating this to the member.

Participants who meet the commitments in the pledge are invited to self-certify this to TPR.

Comment:

Combating pension scams is a priority for TPR. This new campaign is aimed at encouraging trustees, providers and administrators to be proactive in protecting members.

Protecting schemes from sponsoring employer distress

(12 November 2020)

TPR has published guidance for trustees of DB pension schemes, reminding them of good practice, offering practical recommendations for spotting signs of corporate distress, and setting out what they should do to protect the pension scheme. Trustees should take action before a sponsor shows signs of distress to increase the chances of mitigating downside risk in the future. This includes:

- understanding legal obligations to the scheme, include hypothetical outcomes in an insolvency.
- ensuring effective risk management processes are in place.
- reviewing scheme governance including TKU, conflicts, recording keeping and information sharing.
- monitoring the covenant.
- taking appropriate advice.

Trustees should increase the intensity and frequency of covenant monitoring when the employer shows signs of financial distress. They should also take steps to understand the potential returns on a future insolvency, including understanding the position of other creditors. Trustees should also review their investment strategy.

The guidance refers trustees to TPR's Covid-19 guidance on considering employer requests for scheme easements in distressed scenarios. TPR expects trustees to be engaging in regular, open discussions with the sponsor and to make sure the scheme is being treated fairly compared to other stakeholders.

Where a sponsor is facing insolvency trustees should take professional advice from specialist restructuring advisers to make sure that all options to protect the scheme's position have been explored. They should also follow the PPF's contingency planning guidance.

In relation to members, trustees should be alert to scams and unusual transfer activity and carefully consider what communications are appropriate.

Comment:

TPR is urging trustees to take a 'be prepared' approach to the health of their sponsors in the light of the economic difficulties arising from Covid-19 and the impact of Brexit. Even trustees with sponsors in strong positions should be taking action to put their pension scheme in the best possible position should the situation change.

DC scheme management and investment: COVID-19 guidance for trustees

(updated 11 January 2021)

TPR has updated its guidance relating to gated funds to include a section on dealing with transfer requests. TPR does not believe that the law permits it to grant a time extension for payment of a CETV where all or part of the member's investment is held in a gated fund. Trustees should do everything they can to process transfer requests promptly and TPR may issue fines where trustees fail to take all reasonable steps to pay a transfer value within six months of the application date. If only part of the investment is in a gated fund, reasonable steps might include offering the member a partial transfer as an interim measure.

Trustees should continue to report any significant failures to pay transfer values within the statutory period.

Scheme return guidance

(updated 20 January 2021)

TPR has updated its guidance on DB and hybrid scheme returns. Scheme returns will be issued from mid-February and must be completed by 31 March 2021.

THE PENSION PROTECTION FUND

PPF levy policy statement 2021/22

(27 January 2021)

The final PPF levy policy statement for 2021/22 has been published alongside a number of appendices, guidance and forms. As the PPF flagged last month, it is going ahead with its levy estimate of £520m and existing levy parameters and will (as proposed in September):

- implement a small scheme adjustment to halve levies for schemes with less than £20m of liabilities and to taper them for schemes with between £20m and £50m of liabilities;
- reduce the risk-based levy cap from 0.5% to 0.25% of liabilities; and
- continue to measure insolvency risk on the basis in use since April, using credit ratings and the Dun & Bradstreet PPF-specific insolvency risk model.

The PPF has also:

- issued its response on its separate consultation on changes to its insolvency scoring methodology; and
- issued a new consultation on draft guidance for commercial consolidators. This closes on 16 February 2021.

Comment:

Trustees and employers should be considering whether they could take any action now to reduce their levy. Any contingent assets need to be finalised and certified by 31 March 2021 in order to be taken into account.

CASES

Heskett v Secretary of State for Justice – *age discrimination: refinement of the "cost plus" principle*

(11 November 2020)

In this non-pensions case an employee claiming indirect age discrimination argued that the employer's need to save costs could not, on its own, amount to a legitimate aim justifying the discrimination in law. This led the Court of Appeal to analyse the "cost plus" principle, set out in earlier case law and under which the financial burden of acting in a manner which does not discriminate can only be relied on as an element in a justification which involves other factors.

The Court accepted that there cannot be a legitimate aim justifying discrimination if cost is the only reason for the employer's actions. However, the phrase "cost plus" was a form of shorthand, best avoided. The correct position was that it is only if an aim was solely to avoid increased costs that it must be treated as illegitimate. If an employer was subject to financial constraints which obliged it to reduce costs, then that was still capable of amounting to a legitimate aim for the purpose of a justification defence. An employer's need to reduce its expenditure to 'balance its books' could therefore be a legitimate aim.

Comment:

The "cost plus" rule has proved a critical, but often confusing, feature of the age discrimination landscape. This judgment may make it easier for employers to defend age discrimination claims, particularly where an employer is operating under genuine financial pressure.

Lloyds Banking Group Pensions Trustees Ltd v Lloyds Bank PLC – *GMPs: trustees' duty to top-up past unequalised statutory transfer payments*

(20 November 2020)

In the original Lloyds judgment in 2018, the High Court decided that trustees of pension schemes must equalise pension benefits for the effect of guaranteed minimum pensions (GMPs) accrued between 17 May 1990 and 5 April 1997. The latest part of the proceedings concerned the treatment of members who had previously transferred benefits from the Lloyds schemes to other pension schemes, given that those transfers were not calculated on a basis which equalised for the effect of GMPs.

The Court decided that where a scheme had made a cash equivalent transfer, which had not reflected the equalisation of benefits for the effect of GMPs, the member who had transferred out had a claim against the trustees for the shortfall in the transfer payment. The transferring trustees could not rely on the statutory discharge in the Pension Schemes Act 1993 nor any discharge forms signed by members at the time. Although the member's right was to a top-up transfer payment, it would be open to the trustees and member to agree an alternative remedy. Any top-up payment should bear interest at 1% above base rate.

For other, non-statutory, transfers the Court held that the member no longer had rights under the transferring scheme. However, the member might still have a claim for a top-up if they could demonstrate the trustees had breached their duties when making the transfer payment.

Where a bulk transfer providing mirror image benefits had been made in line with pension preservation law requirements, the transferring trustees would also no longer have liability for the member's benefits.

The parties asked the Court whether transferring trustees were under a proactive duty to identify, calculate and correct shortfalls in previous transfers out, or whether they could wait until a request was made by the affected member or the receiving scheme. The judge was reluctant to be drawn on detail and did not say that trustees must proactively search for all former members who have a claim relating to a transfer out, simply concluding that: *"the Trustee does need to be proactive in that it must consider the rights and obligations which I have identified, the remedies available to members and the absence of a time bar and then determine what to do."*

Comment:

The confirmation of the need to consider revisiting past transfers means that trustees will need to build additional steps into their GMP equalisation project plans. The starting point will be to understand the potential exposure they have to such claims and what scope they have in practice to take proactive steps to resolve those claims. The case also flags the limits on the extent to which trustees can rely on a statutory, rules-based or contractual discharge in any circumstances (not just GMP equalisation) where they have made past errors in calculating statutory transfers.

Re Prudential Assurance Company Ltd and Rothesay Life Plc - *Court of Appeal overturns High Court block on proposed annuity transfer*

(2 December 2020)

Last year, the High Court refused to sanction an 'insurance business transfer scheme' application under the Financial Services and Markets Act 2000, involving Prudential's proposed £12bn annuity sale to Rothesay Life. The judge had accepted the argument of the opposing policyholders that they chose the Prudential on the basis of its age and established reputation and the court should give weight to their contractual choice. The judge also said that if either provider required external financial support over the annuitants' lifetime, Rothesay did not have the comfort of the same likely substantial resources as the Prudential.

The Court of Appeal overturned the High Court decision. The Court of Appeal agreed that the judge was entitled to take into account a range of factors, but those did not include speculation as to what owners of an insurer might decide to do in future to support a regulated subsidiary. The judge was also wrong to have given weight to the objecting policyholders having chosen Prudential on the basis of its age and established reputation.

Comment:

The proposed transfer has not been waved through: the Court remitted the decision to the High Court. However, the judgment seems to restore the former status quo and is likely to be very welcome for the insurance industry, not least newer market entrants. It is also pertinent to trustees currently considering buy-ins and buy-outs.

MISCELLANEOUS

PASA

PASA Cybercrime guidance

(10 November 2020)

PASA has published guidance aimed at scheme administrators outlining four key areas covering different elements of cybercrime. The guidance covers:

- meeting legal and regulatory standards;
- understanding their organisation's vulnerability to cybercrime;
- ensuring resilience; and

- in case of an attack, remaining able to fulfil critical functions.

GMP Equalisation Working Group Update

(27 January 2021)

The GMPEWG has published a review of its work in 2020 and its plans for 2021. It anticipates that it will issue guidance on the tax implications of GMP equalisation by the end of February 2021 and its guidance on conversion by the end of April 2021. It also hopes to issue some example methodology on anti-franking during the second quarter of 2021. It will give a further update on the timing of its guidance on past transfers during the first quarter of 2021.

ICO

ICO code of practice on data sharing

(17 December 2020)

The Information Commissioners' Office (ICO) has published its data sharing code of practice. The code sets out steps data controllers should take before deciding to share data. The code confirms that the ICO considers that it is good practice to have a data sharing agreement in place which should set out the purpose of the data sharing, cover what happens to the data at each stage, set standards and help all the parties involved in sharing to be clear about their roles and responsibilities.

The code is not legally binding, but data controllers who do not comply may find it more difficult to demonstrate that their data sharing is fair and lawful. The code will come into force 40 sitting days after it has been laid before Parliament, this is likely to be in late February 2021.

ICO statement on dataflows

(28 December 2020)

The Information Commissioner's Office (ICO) has confirmed that the Government has announced that the EU-UK Trade and Cooperation Agreement will allow personal data to flow freely from the EU (and EEA) to the UK, until adequacy decisions have been adopted, for no more than six months. Although this will allow personal data to flow freely for the time being, as a "sensible precaution" the ICO recommends that controllers put in place alternative transfer mechanisms to safeguard against any interruption to the free flow of EU to UK personal data.

Other organisations

Institute & Faculty of Actuaries (IFoA) Pension scheme cyber risk

(17 November 2020)

This IFoA paper summarises and explains types of cyber risk to which pension schemes are vulnerable, including ransomware attacks, data theft, cyber fraud (including e-mail 'spoofing') and DDOS attacks (which disrupt service by using multiple computers to flood host servers with superfluous traffic). It reminds trustees of their responsibilities under Pensions Act internal controls provisions and the GDPR. The paper then sets out the IFoA's view on how trustees can manage the risk by reviewing their own personal 'cyber hygiene', third party assessment, cyber insurance and having incident management plans in place.

The Pensions Dashboards Programme (PDP) Data Standards Guide

(15 December 2020)

The PDP has published the key data standards that will underpin pensions dashboards, covering data for all UK pensions that individuals have not yet accessed (pensions in payment are not yet in scope). The data standards guide covers the data elements required to find and view basic information about an individual's pensions.

A final set of implementable data standards will be produced once MaPS has a supplier on board for the associated digital architecture. MaPS urges trustees and providers to start to prepare their data now, in advance of onboarding in 2023.

Pensions Climate Risk Industry Group - Climate Risk Guidance for trustees

(27 January 2021)

The Pensions Climate Risk Industry Group (a cross-government and industry group) has published non-statutory guidance designed to help all pension scheme trustees comply with their duties to manage climate-related risks. It is published in four parts (each of which has a separate "quick start" guide):

- **Part 1 - Introduction** - introduces climate risk as a financial risk to pension schemes, trustees' legal requirements and the TCFD recommendations;
- **Part 2 - Trustee governance, strategy and risk management: how to integrate and disclose climate-related risks** - sets out a suggested approach for the integration and disclosure of climate risk within the typical governance and decision-making processes of pension trustee boards, including defining investment beliefs, setting investment strategy, manager selection, and monitoring;
- **Part 3 - Scenario analysis** - contains technical details on recommended scenario analysis;
- **Part 4 - Setting metrics and targets to measure and manage climate-related risk** - recommends metrics that trustees may wish to consider using to record and report their findings.

The guidance suggests that where schemes are not subject to the upcoming legislative requirements to make TCFD disclosures then they could consider a two-step process, first adopting robust governance procedures relating to climate risk and later moving to disclosure (it is the Government's intention for this to be mandatory across the economy by 2025).

Dates for diaries: Trustee training remains one of the most important ways of ensuring that trustees have the knowledge and understanding required to perform their duties. CMS runs regular trustee training days. If you would like to be updated of upcoming dates or have any other enquiries about this course please contact Megan Thorogood (megan.thorogood@cms-cmno.com).

If you are interested in any additional trustee or employer training please contact Kieron Mitchinson (kieron.mitchinson@cms-cmno.com) who can provide you with a list of our current training topics or discuss any particular training needs you might have.