

The Hogan Lovells logo consists of a solid lime green square on the left, with the words "Hogan" and "Lovells" stacked vertically in a black serif font to its right.

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Recent developments in pensions

Hogan Lovells pensions team

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Speaking today



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Overview of the webinar



DB surplus



FCA Consumer Duty



TPR update



Dashboards update



Lifetime allowance changes



TCFD Reporting



DB Surplus



Charlotte Yeates
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What will this session cover

- What does a surplus mean
- Legal background (legislation and case law)
- Ongoing v surplus on wind-up
- Types of surplus rules and whether rules can be amended
- Employer's perspective
- Possible win-win scenarios
- Trustee decision making

What do we mean by a surplus?

- Word “surplus” is used quite a lot in different contexts (eg a technical provisions surplus, an accounting surplus...)
- If thinking about distribution of surplus, we mean a buy-out/solvency surplus
- So if all benefits are bought out with an insurer (and costs of winding-up etc?) what would be left...

Legal background...

- Legislation covers surplus distribution from ongoing scheme and on wind-up
- Case law – mainly dates from 20+ years ago
- Case-by-case approach – strong focus on wording of Trust Deed
- Surplus doesn't by default belong to employer or members
- Within rules and legislation, Trustee/employer have limited constraints on how to deal with surplus
- **What do your rules say?**

Ongoing surplus v surplus on winding up

- Return of ongoing surplus to the employer (*s37 Pensions Act 1995*)
 - Requires a s251 resolution was passed before April 2016
 - Only possible if rules permit **and** resolution passed
 - Essentially restricted to return of surplus over buy-out liabilities
 - Post 2006, very rare to exercise that power
- Distribution on wind-up (*s76(3) Pensions Act 1995*)
 - Depends what the rules say
 - After all benefits are discharged
 - If power to augment benefits, can only return to the employer if Trustee has exercised or decided not to exercise that power
 - Increasingly common to have some surplus expected after wind-up

What might your rules look like on wind-up?

“The Trustee shall apply such part (or the whole) of any balance of the Trust Assets after benefits have been discharged as the Trustee, in consultation with the Principal Company and on the advice of the Actuary, shall decide in the provision of such benefits for or in respect of such Members, in such manner and in such proportions as the Trustee shall determine. The Trustee shall pay the remainder (if any) of the Trust Assets to the Employers.”

“If after securing the benefits in full, an excess remains in the Fund the Trustees will (and having regard to Actuarial Advice) apply any part or the whole of that excess in increasing the benefits payable under this R19 in such manner as they shall decide) up to the maximum limits for such benefits. Any remaining excess shall be distributed in accordance with relevant legislation”

“Any remaining assets may be used as the Trustees may in their discretion think fit to augment benefits of beneficiaries.”

Can you amend the rules?

- Maybe...
- Depends on any restrictions in the amendment power
 - Specific restriction on amending that rule
 - Restriction on returning funds to the employer
- *National Grid* case found that restriction on amendment power didn't mean other options weren't possible, eg contribution holiday for employer

Employer's perspective

- Likely to be concerned about “trapped surplus”
- Accounting/balance sheet impact
- Timing of any return
- Want certainty?
- Consent required to exercise of any powers or in practice to buy-in

Opportunity for a “win-win”?

- Trustee and employer may be able to agree way forward
- Agree upfront in buy-in/probable wind-up situation?
- Consider balance of powers:
 - What does surplus rule say
 - Who can trigger wind-up (is that an employer only power)
 - Consent to buy-in
- Options to consider:
 - Scheme merger to share surplus or cross-subsidy (eg surplus for DC accrual)?
 - Proportion set aside for member improvement and remainder returned to employer?
 - Rule amendments for certainty?

Trustee decision

- If Trustee decides not to use some or all to augment benefits
- All relevant and no irrelevant factors... (*Edge v Pensions Ombudsman*)
- Case law suggests these may include:
 - Balance of powers and likelihood of accessing surplus without employer cooperation
 - Main purpose of scheme – to provide retirement and other benefits
 - Legitimate expectation of members to share surplus **but** not a right, just fair regard to their interests
 - Impact on employer
 - Level of benefits compare to the market
 - Inflation and whether benefits keep up with cost of living
- Not exhaustive – other scheme specific factors?

DB Surplus



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Regulatory update



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FCA Consumer Duty

FCA Consumer Duty

What is the duty?

- New consumer principle
 - *“A firm must act to deliver good outcomes for retail clients.”*
- Three cross-cutting rules requiring firms to:
 - Act in good faith
 - Avoid causing foreseeable harm
 - Enable and support retail customers to pursue their financial objectives
- FCA expects the new duty to promote good outcomes in:
 - Quality of firm’s products and services
 - Price and value of products and services
 - Consumer understanding
 - Support for consumers



FCA Consumer Duty

Application

- Applies to FCA-regulated firms
 - From 31 July 2023 to all new products and services in relation to retail customers
 - From 31 July 2024 to all closed products and services
- Does not apply to unregulated business
 - But does apply to unregulated activities which are ancillary to regulated activities
- Applies to all firms with material influence over, or which determine, retail customer outcomes
 - Firms must consider end customers, whether or not are direct client of firm

FCA Consumer Duty

How does the duty apply to personal pension schemes?

- Personal pension schemes:
 - Providers of personal pension schemes are subject to the new duty, eg providers of workplace GPPs and SIPP operators
 - Providers will therefore need to consider whether their products and services are designed to help customers achieve good outcomes
 - Duty applies throughout pension and investment journey
- FCA letter to SIP operators in May 2023, concerns regarding:
 - Firms failures
 - Consumers not receiving fair redress when it is due or not receiving it in a timely manner
 - Pension scams and fraud

FCA Consumer Duty

How does the duty apply to occupational pension schemes?

- The new duty does not apply to trustees of occupational, trust based schemes
- BUT firms providing services to trustees of such schemes are in scope
- End customers include *“beneficiaries of trust-based pension schemes where the FCA authorised firm’s client may be the trustee”*
- FCA: *“In practice, if an FCA authorised firm could have a material influence over outcomes for members of an occupational scheme, it should comply with the Duty within the scope of its activities”*

Consumer duty: impact on occupational schemes?

- What occupational scheme services may need to comply with Consumer Duty?
 - Direct communications with members
 - Providing support directly to members
 - Modelling tools provided to members
 - Key test: whether activity has a material impact on member outcomes
- Discuss with your administrators and service providers – potential additional costs to trustees?



An aerial photograph of a lush green agricultural field, showing rows of crops. A blue callout box is overlaid on the left side of the image, containing the text 'TPR update'.

TPR update

Speech by TPR CEO Nausicaa Delfas

- Highlights include:
 - Further encouragement towards consolidation:
 - *“The choice is simple: can I compete with the biggest master trusts? If not, its likely time to move your members to a better value scheme and leave the market”*
 - Working towards removing barriers and addressing practical issues
 - Move towards mandatory professional trustees?
 - *“Fundamentally we believe that every trustee body should include someone who meets professional standards”*
 - Considering trustee registration and formal accreditation for professional trustees

Speech by TPR CEO Nausicaa Delfas

- Highlights include:
 - Value for money
 - Change of mindset needed, from prioritising low costs to putting value first
 - Driving innovation in the interests of savers
 - Role of investment in illiquid assets?
 - Focus on “at retirement solutions”
 - Savers find themselves vulnerable to poor advice, loss of value of even fraud
 - Does “inertia-based” saving require a different solution at retirement?
 - Working with DWP to ensure savers are supported to make good decisions

An aerial photograph of a lush green agricultural field, showing rows of crops. A blue callout box is overlaid on the left side of the image, containing the text 'Dashboards update'.

Dashboards update

Update on pensions dashboards

New approach to connection date

- Recently published statement and draft regulations adopt a new approach:
 - Mandatory staging dates for connection to dashboards have been replaced
 - Under new approach:
 - Longstop connection date of 31 October 2026
 - Staging timeline to just be included in guidance rather than legislation
 - Appears that guidance will encourage schemes to connect earlier than they are legally required to, to avoid a rush in 2026

Update on pensions dashboards

New approach to connection date

- Concerns with this approach:
 - How prescriptive will the DWP be about its non-legislative timescales?
 - Schemes will delay!
 - Will infrastructure cope with many schemes connecting at the same time?
 - Previous arrangement had larger schemes connecting first, with any teething issues being ironed out earlier
 - Schemes and administrators face competing demands on time and resources

Regulatory update



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Lifetime allowance changes



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LTA: its introduction

- Prior to 6 April 2006 (“A-Day”)
 - Tax favoured schemes were subject to Inland Revenue limits
 - IR limits were hard limits, ie strict requirements on both form and level of benefit
- A-Day: tax “simplification”
 - Tax favoured schemes (registered pension schemes) subject to soft limits
 - Authorised and unauthorised payments, key one for us is pension commencement lump sum (PCLS) capped at 25% of value of pension rights
 - Lifetime allowance and annual allowance

LTA: its operation

- LTA was introduced at £1.5m at A-Day and rate has gone up and down since
- Benefits in excess of LTA subject to LTA charge
- Some members had already earned benefits in excess of £1.5m pre-A-Day
- Others had earned more than the LTA when it started to decrease in 2010/11
- To stop these members being hit with an LTA charge they could benefit from transitional protection, including:
 - Enhanced protection at A-Day
 - Fixed protection in 2012, 2014 and 2016

LTA: its abolition

- Government announced abolition of LTA
- Under Finance (No. 2) Bill:
 - LTA charge will be abolished for tax year 23/24
 - LTA legislation otherwise remains in place
- Government intends to legislate to remove LTA completely for tax year 24/25
- PCLS capped at £268,275 (25% of current LTA) for most members – more complex where members have transitional protection, more of which later

Transitional protections: enhanced protection

- Where a member has enhanced protection:
 - Not subject to LTA;
 - Can also take a PCLS broadly equal to lump sum the member could have taken pre-A Day where member qualifies for lump sum protection too; but
 - Can't "accrue" further benefits
- Broadly a member is eligible for lump sum protection where the lump sum they were entitled to pre-A-Day exceeded new limits
- Required application to HMRC

Transitional protections: fixed protection

- Under fixed protection:
 - Member retains LTA prior to its reduction; but
 - Cannot “accrue” further benefits
- Therefore, PCLS capped at 25% of rights immediately before reduction in LTA
- Required application to HMRC

Transitionally protecting transitional protections

- What does the abolition of the LTA mean for these transitional PCLS protections?
- Default position for members without transitional protection is lump sum is capped at the lower of:
 - 25% of value of their benefits at retirement;
 - £268,275
- This doesn't apply for members with transitional protections
- Members with the following retain their current rights to a PCLS in excess of the FA maximum:
 - Primary protection
 - Lump sum protection
 - Individual protection
- Restrictions on the PCLS for a member with EP or FP are slightly different
- This is because the policy is to allow future accrual – which was previously not permitted with these protections – but to direct accrual towards additional pension rather than additional PCLS in excess of FA04 limits

EP and FP under the new regime: the easier bit

- A member with FP is entitled to a PCLS capped at the lower of:
 - 25% of the value of their benefits at retirement; and
 - 25% of the LTA they retained under fixed protection
- Where a member has EP but no lump sum protection, his lump sum will be capped at the lower of £375k or 25% of value of benefits at retirement
- A general (and generic) communication to members

EP and lump sum protection: practical issues (1)

- A member with EP and lump sum protection is entitled to a PCLS up to maximum of the lower of:
 - The PCLS they could have taken on 5 April 2023; and
 - The percentage of pre-A-Day benefits they could take as PCLS applied to the value of their benefits at retirement
- Key issue: the first limb above, requires the trustee to know the value of the member's benefits as at 5 April 2023:
 - Deferred DB members, straightforward
 - Active DB members, need to make sure that employer can supply necessary salary data
 - DC members or DB members with AVCs, need to know fund value as at 5 April 23. Need to obtain fund values

EP and lump sum protection: practical issues (2)

- EP works across multiple schemes
- Therefore need to make sure members have this information in respect of any other schemes they're a member of
- Communications
 - General communication, for example a newsletter
 - Targeted communications?
 - May not know all affected members because members didn't have to tell trustees
 - Is it worth it? Only relevant for members with large pensions as at A-Day – ie 17 years ago – who still haven't retired. How many will there be?
 - Think about how many members will or could be affected by issue

Lifetime allowance changes



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TCFD reporting



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TCFD requirements: what is TCFD?

The Task Force on Climate-Related Financial Disclosures made recommendations to improve reporting of climate-related financial information.

The DWP borrowed concepts developed by the TCFD when drafting climate-change reporting legislation – so it is referred to as “TCFD” reporting.

The logo for the Task Force on Climate-Related Financial Disclosures (TCFD). It features the acronym 'TCFD' in a large, bold, white sans-serif font on the left. To its right is a vertical white line, followed by the full name 'TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES' in a smaller, white, all-caps sans-serif font, arranged in two lines.

TCFD | TASK FORCE ON CLIMATE-RELATED
FINANCIAL DISCLOSURES

TCFD requirements: the legal landscape for Trustees

- Regulations
 - **The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021**
 - The Occupational Pension Schemes (Climate Change Governance and Reporting) (Miscellaneous Provisions and Amendments) Regulations 2021
 - The Occupational Pension Schemes (Climate Change Governance and Reporting) (Amendment, Modification and Transitional Provision) Regulations 2022
- Guidance
 - Statutory guidance from the DWP (updated in 2022)
 - Non-statutory guidance from the Pensions Regulator
 - Guidance from the Pensions Climate Risk Industry Group and other industry bodies

TCFD requirements: the 6 key obligations for trustees



Knowledge & understanding

Trustees must have knowledge and understanding of principles relating to the identification, assessment and management of relevant climate change risks and opportunities.



Governance

Trustees must establish and maintain (i) oversight of climate related risks and opportunities and (ii) processes to satisfy themselves that some parties they work with take adequate steps to identify, assess, and manage these risks & opportunities.



Strategy

Trustees must consider the impact of climate related risks and opportunities on the scheme and undertake scenario analysis to assess what impact this would have on the scheme.



Risk management

Trustees must establish and maintain processes to identify, assess, and manage climate related risks and integrate those processes into the scheme's overall risk management.



Metrics and targets

Trustees must calculate certain metrics relating to the scheme's climate impact and set targets for improvement.



Publication

Trustees must publish a TCFD Report explaining how they have complied with these obligations.

The TCFD report: key content of the report



Governance

- How the Trustee maintains oversight of climate-related risks and opportunities (“CRROs”)
- The role of people assessing CRROs for the Scheme and how the Trustee has satisfied itself of their expertise



Strategy

- Short, medium & long-term horizons
- Resilience of the funding and investment strategy resulting from the scenario testing
- What CRROs has the Trustee identified?
- Impact of CRROs on funding & investment strategy
- Result of the most recent scenario-testing
- Impacts of the scenario testing on assets & liabilities – or an explanation as to why this information is not available



Risk management

- Risk management processes for climate-related risks and opportunities.
- How CRRO risk management processes are integrated into the overall Scheme’s risk management



Metrics and targets

- Metrics the Trustee has calculated – or an explanation as to why it cannot calculate such metrics
- Scheme’s emission targets and performance against these targets

“We appreciate there may be some current practical challenges in drafting the disclosures...trustees should seek to demonstrate that they have acted to fully understand the range of climate-related risks and opportunities their scheme is exposed to and have taken action to address those – where proportionate ...”

David Fairs, TPR

The TCFD report: publishing the report

- Trustees must publish the report within **7 months of the scheme year end date** in which they were required to comply with TCFD requirements
- Where:
 - The scheme return – it must include the address of the website where the report has been published
 - Annual Benefit Statements and Annual Funding Statement – they must include a statement that the report is available online, the website address, and details of where and how to access the report
 - The annual report – it must include the address of the website where the report has been published and a short summary explaining where that link will take the reader to
- Failure to...
 - Publish the report: mandatory fine (between £2.5k and £50k)
 - Comply with the content requirements: discretionary fine (up to £50k)

TCFD: 5 top tips for pension trustees

1



Make sure you follow the pension-specific regulations and guidance

Remember – the Regulations and guidance for trustees are based on the recommendations of the Taskforce on Climate-Related Financial Disclosures (“TCFD”) but **it is the Regulations and guidance that trustees must follow** – not the recommendations themselves (as they are more general and less prescriptive)

TCFD: 5 top tips for pension trustees

1



Make sure you follow the pension-specific regulations and guidance

2






Signposting is key to having a comprehensive report

The best way to ensure you have complied with all of the (many) requirements is to clearly signpost them in your report by:

- using headings that reflect the requirements of the Regulations; and
- mirroring the language of the statutory and regulatory guidance where possible.





This helps members understand your report and helps you ensure you have covered every heading in the Regulations and guidance.

TCFD: 5 top tips for pension trustees

- 1  Make sure you follow the pension-specific regulations and guidance
- 2  Signposting is key to having a comprehensive report
- 3  You are reporting on what you have done






Reporting is only one TCFD obligation – don't forget to comply with your governance, strategy, risk management, and other obligations!

TCFD: 5 top tips for pension trustees

- 1  Make sure you follow the pension-specific regulations and guidance
- 2  Signposting is key to having a comprehensive report
- 3  You are reporting on what you have done
- 4  Focus on your executive summary






Most members will start with (and some will stop at) your executive summary.
Use this summary as an opportunity to provide the plain English summary of the TCFD report's findings and conclusions.

TCFD: 5 top tips for pension trustees

-  1 Make sure you follow the pension-specific regulations and guidance
-  2 Signposting is key to having a comprehensive report
-  3 You are reporting on what you have done
-  4 Focus on your executive summary
-  5 Ensure your report is easily accessible to all

- Make sure your report can be easily found and is widely accessible – meaning it is:
- on a publicly available website, accessible free of charge;
 - indexable by search engines;
 - Can be accessed without usernames, passwords or requiring personal information; and
 - compatible with screen reading software etc.

TCFD: 5 top tips for pension trustees

-  1 Make sure you follow the pension-specific regulations and guidance
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TCFD reporting



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Any questions?



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