# Recent developments in pensions

*Hogan Lovells Pensions Team*

7 October 2020

# Investment: changes in relation to pension schemes

*Faye Jarvis*
Partner, London
*Pensions*

# Assessing climate change risk

# New legislation on climate change risk

- New provision introduced into Pension Schemes Bill

- Regulations may require trustees to secure effective governance of the scheme with respect to the effects of climate change, in particular:
    - Risks from steps being taken by governments and others
    - Opportunities relating to climate change

- Trustees may be required to:
    - Review scheme's exposure to prescribed risks and adopt risk management strategy
    - Assess assets in prescribed manner, including exposure to prescribed risks
    - Adopt & measure performance against climate change risk targets
    - Publish information on effects of climate change on scheme

# DWP consultation: Taking action on climate risk

- Regulations & statutory guidance to embed Task Force on Climate-related Financial Disclosures (TCFD) recommendations in pension law

- Investment decisions remain with trustees and no expectation that trustees must invest / disinvest in particular way

- Regulations in 2021, following further consultation

- Consultation on mandatory Paris alignment reporting soon
    - Portfolio warming / implied temperature rise (ITR) of investment portfolio (aka degree warming, temperature score, portfolio warming potential)
    - Model likely global temperature rise with which holdings are consistent
    - Govt sees value in reporting ITR in annual benefit statement but current methodologies insufficient

# Climate consultation: scope and timing

- From 1 October 2021 apply to:
    - master trusts
    - collective money purchase (CMP) schemes
    - schemes with ≥ £5 bn assets
- From 1 October 2022 apply to schemes with ≥ £1 bn assets
- Review in 2024, potential roll out to all OPSs
- Initially comply “as far as they are able”, recognising issues with obtaining data

# Climate consultation: 5 key requirements

1. **Strategy:** identify and assess on ongoing basis climate-related risks and opportunities which will affect investment (and funding if DB) strategy over short, medium and long term

2. **Scenario analysis:** analyse at least two climate-related scenarios at least annually

3. **Risk management:** adopt and maintain, on ongoing basis, processes for identifying, assessing and managing climate-related risks

4. **Metrics:**
   - Obtain data on emissions and other characteristics of investments which they wish to quantify from asset managers / investee firms
   - Calculate and publish at least one emissions-based and one non-emissions based metric from a range in statutory guidance

5. **Targets:** Set at least one target for one of metrics they choose to publish

# Climate consultation: disclosure and compliance

- Publish TCFD report on own or scheme sponsor’s website
- Reference TCFD reporting from annual report
- Notify members of TCFD reporting via annual benefit statement
  - DB schemes only have to add link where already required to issue benefit statement
- tPR scheme return to include link to TCFD report, SIP, implementation statement and excerpts from chair’s statement
- Mandatory penalty for complete failure to publish a TCFD report (min £2,500)
- Other penalties subject to tPR discretion

# Improving DC member outcomes

# Improving member outcomes for members of DC schemes

- Consultation and draft guidance issued 11 September 2020
- Regulations expected in force 5 October 2021
- Follows consultation "Investment Innovation and Future Consolidation" in February 2019
- Reminder: call for evidence on elements of charge cap summer 2020; DWP intends to report towards end of 2020

# New disclosure requirements from 5 October 2021

## All OPSs:

- must report total value of scheme assets at previous year end in scheme return

## All relevant schemes:

- Report net return on investments for default and member selected funds (from 2015, if possible) in chair’s statement
- Publish return on investments information on publicly available website

# New value for members assessment from 5 October 2021

**Applies to "specified schemes"**

- Relevant scheme
- Asset value less than £100m at previous scheme year end; and
- Operating for at least three years at end of previous scheme year

**Must complete prescribed value for members assessment annually**

- Report in chair's statement
- Report overall outcome in scheme return

# New value for members assessment (cont)

**Where assessment shows scheme not present value for members:**

- Trustees must take immediate steps to wind up and consolidate into larger scheme; and
- Report proposed approach to tPR in scheme return

**Exceptionally, trustees may have “solid reason” to believe can make required improvements cost effectively & efficiently, instead of wind up**

- Must assess, time, skills, capacity & costs of improvement
- When considering consolidation, may factor in costs of wind up; exit charges; and guarantees which would be lost

# Reporting to CMA

# Reporting to CMA

- Trustees must submit a compliance statement to the CMA by 7 January 2021
    - CMA published standard form statement. Does not need to contain a lot of detail, but must state which parts of the Order the trustees have complied with and over what period

- Applies if subject to requirement to set objectives for investment consultants and/or to run competitive tender for fiduciary manager

# Brexit and pensions

*Katharine Howe*
Senior Associate, London
*Pensions*

# Brexit timeline - reminder

**31 Jan 2020**

- UK left the EU
- Entered transitional period

**1 July 2020**

- UK did not ask to extend transition period by this deadline

**31 Dec 2020**

- Unless extension otherwise agreed, transition period ends
- With or without trade deal

EU law continues to apply in the transition period

Negotiations ongoing

# Brexit in 2020

| | EU Membership Before 31 January 2020 | Under Withdrawal Agreement: Transition period 31 January → 31 December 2020 | Under Withdrawal Agreement: Northern Ireland Protocol From December 2020 until future relationship agreement comes into force – Northern Ireland | Under Withdrawal Agreement: Northern Ireland Protocol From December 2020 until future relationship agreement comes into force – Great Britain |
|---|---|---|---|---|
| **Influence in EU decision-making** | ✓ | ✗ | ✗ | ✗ |
| **No tariffs on goods** | ✓ | ✓ | ✓ | ✗ |
| **No non-tariff barriers to trade in goods** | ✓ | ✓ | ✓ | ✗ |
| **Borderless trade in services** | ✓ | ✓ | ✗ | ✗ |
| **No divergence in applicable law** | ✓ | ✓ | ✓ | ✗ |
| **Free movement of people** | ✓ | ✓ | ✗ (common travel area still applies) | ✗ |
| **Financial contribution to EU budget** | ✓ | ✓ | ✗ | ✗ |
| **CJEU (and other EU agency) jurisdiction in UK** | ✓ | ✓ | ✓ | ✗ |
| **Commencement of new trade deals** | ✗ | ✓ | ✓ (cannot prejudice relevant EU rules) | ✓ |

# Implications of Brexit for pension schemes

- Significant ongoing implications for covenant, funding and investments

- Legal implications:
    - Overseas payments
        - Insurance arrangements
        - State pensions
    - Data protection
    - Investments
    - PPF entry
    - Cross border schemes

# Brexit – Overseas payments – Insurance arrangements

- Payments from trustees to members living in the EEA still possible
  - Delays or additional charges possible
  - Benefits under **buy-ins** or **insured death in service arrangements** still payable

- **Buy-outs:** UK insurers prohibited from issuing individual policies to members living in EEA. Ways to mitigate this:
  - Issue policy to trustees to assign to overseas member (also ensures FSCS protection)
  - Require member to have UK bank account
  - Insurer set up EEA subsidiaries
  - EIOPA has recommended that member state regulators should not enforce strictly

- **Reinsurance** pricing might increase

# Brexit – Overseas payments – State pensions

- State pensions still paid

- **Triple lock uprating**
    - If moved to EEA before 31 Dec 2020 or move to Ireland, uprating guaranteed
    - If move to EEA after 31 Dec 2020, uprating depends on deal agreed

# Brexit – Data protection

## Data flow from UK to EU & outside

- Personal data can still be transferred to a data processor in the EEA (provided data processing agreement in place)
- Personal data can't be transferred to country outside EEA, unless:
  - Standard Contractual Clauses (SCC) used and conduct mini adequacy assessment (due to Schrems II decision)
  - adequacy findings in place (but Schrems II invalidated US Privacy Shield)

## Data flow from EU to UK

- It is <u>unlikely</u> EU will make finding of adequacy in respect of UK by end of transition period, which would mean personal data could flow freely from EU to UK
- If no finding of adequacy, personal data can only flow from EU to UK if:
  - appropriate safeguards in place, eg SCC plus mini adequacy assessment
  - one GDPR exceptions applies

# Brexit - Investments

- **Pensions EU Exit Regulations** don't change where pension scheme assets must be invested
    - Following lobbying, regulations provide that assets must be predominantly invested in the same way as currently - on a UK, EU or overseas regulated market

- Post-Brexit, UK investment advisers and managers may be more restricted in carrying out activities in the EU and vice versa

- **EU Disclosure Regulation** on sustainability-related disclosures unlikely to apply in the UK after transition period

# Brexit – PPF entry

- EU insolvency proceedings not automatically recognised for PPF entry purposes
    - Need to have qualifying insolvency event
    - But the UK courts will have the power to wind-up companies incorporated overseas
    - And trustees can notify PPF that an EEA credit institution is unlikely to continue as a going concern

# Brexit – Cross border schemes

## UK based cross-border scheme

- Only 40 schemes
- Existing schemes will no longer be "cross-border"
- Will need to check with relevant member states whether EU employers can continue to participate
  - Eg Belgium would not allow
- No need to register as "cross-border" if EU employer participates after 31 Dec 2020

## UK employer participating in EU based cross-border scheme

- May only continue paying into scheme if:
  - established under trust;
  - UK-based trustee or representative; and
  - relevant member state will accept contributions from UK employer
- Scheme must continue to meet non-UK qualifying criteria to be used for auto-enrolment

# GMP equalisation: where are we?

*Duncan Buchanan*
Partner, London
*Pensions*

# The Courts

**October 2018:**

- Must equalise for the effects of GMPs relating to the period 17 May 1990 – 5 April 1997
- Various methods approved (B, C2 and D2)
- Need to correct for the past as well as for the future
- Time limits

**May 2020:**

- Liability for past (unequalised) transfers out
- Top up or residual pension (how calculate)
- Time limits

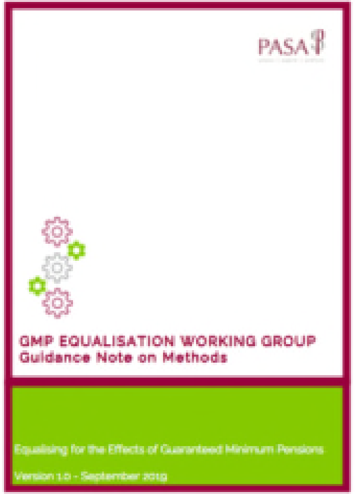
**October 2020:**

- Judge has asked for an additional hearing to discuss transfers

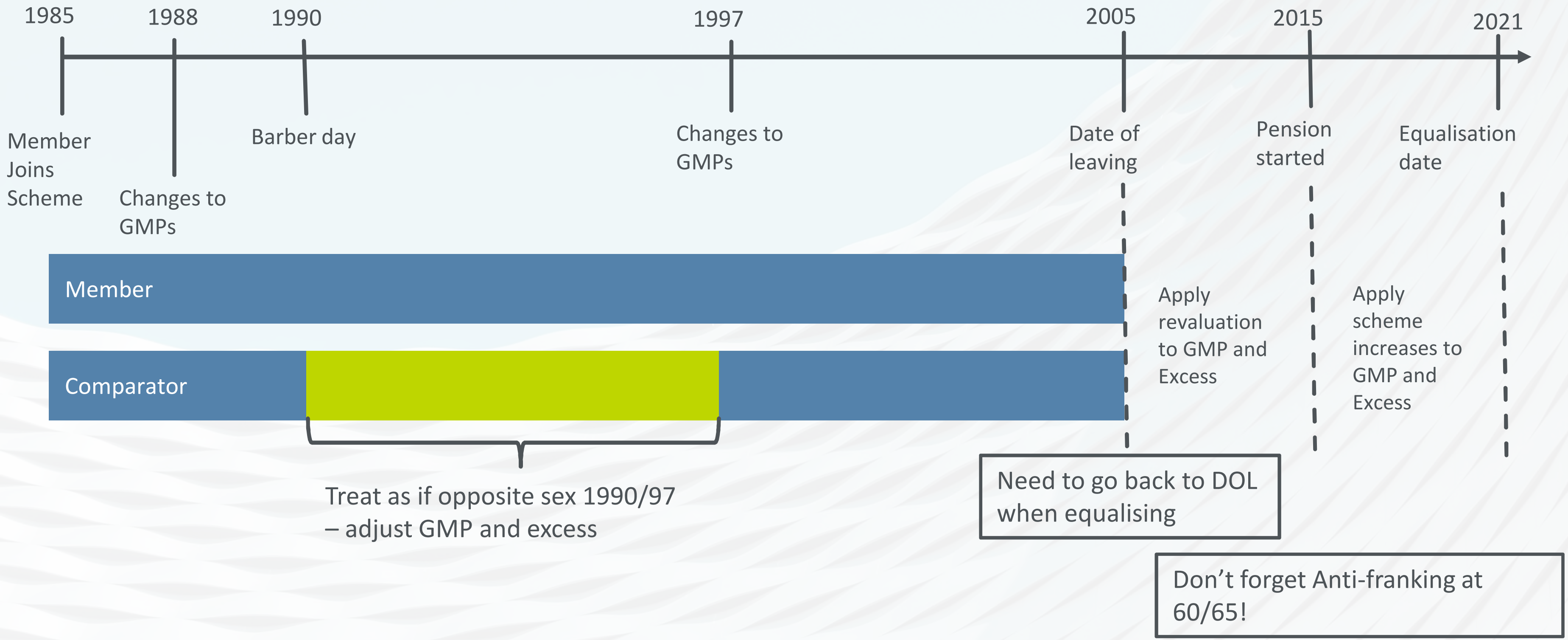
# GMP Equalisation Working Group

- **Guidance on Methods** issued in September 2019
- **Guidance on Data** issued July 2020
- **Guidance on Communications** issued in August 202(
- **Guidance on tax** being prepared

www.pasa-uk.com/guidance/gmp-equalisation/



# Data issues - constructing the comparator



# Industry guidance on Data

Four “calculation solutions” suggested to reconstruct member record and construct comparator:

1. **Reconstruction:** “gold standard” recalculate member’s pension and comparators from full suite of data

2. **Roll back:** take existing pension and wind it back to start then construct comparator and wind forwards

3. **Formulaic:** take existing pension and swap members post 1990 GMP for comparator’s and adjust excess

4. **Broad brush:** last resort for where total lack of data

# Industry Guidance on Communications

- Designed to help smaller schemes but useful for all
- Covers early planning stages for GMP Equalisation
- Additional guidance to follow
- Plain English communications

# Tax issues

- Issues for schemes are:
  - Lifetime Allowance – need to recalculate to reflect any uplift
  - Annual Allowance – for deferred members (conversion only)
  - Members with LTA protections – is protection lost on equalisation
  - Deferred member carve out where GMP is converted
  - Trivial commutation and small lump sum payments

- HMRC guidance issued in February 2020 and in July 2020

- Guidance does not cover equalisation through GMP conversion

# What we are seeing

- Most schemes unlikely to equalise until tax position is clearer
- Ongoing schemes looking at 2021/2022 to equalise
- Schemes starting to prepare now – availability of data
- Issues about linking in with GMP reconciliation/rectification exercises
- Schemes taking steps to equalise transfer values for effects of GMPs
- Those schemes winding up are now having to equalise GMPs
- Whilst for most members adjustments are “modest” – a member of one scheme winding up is due a back payment of £15,000 (less tax)

# Recent Pensions Ombudsman determinations

*Rob Struckett*
Associate, London
*Pensions*

# Mr E (Liberty SIPP)

## Transfers: insufficient due diligence

- Mr E was member of Liberty SIPP
- Initial transfer request made in 2017
- Transfer to Dawson Scheme takes place in 2018
- Liberty argues that it carried out checks:
  - Dawson Scheme status: HMRC confirmation, not recently registered
  - No mention of access pre-55 or legal loopholes
  - No mention of unsolicited approach or pressure to complete
  - Nothing to indicate wouldn't have transferred if warned
- Ombudsman concludes Liberty failed to put in place necessary procedures to reflect the industry guidance on pension liberation fraud

**Request to transfer**

*Encloses transfer form, HMRC scheme registration certificate, screen prints, certified copy of TD&R and Letter of Authority*

**Letter of Authority**

*Adviser does not provide financial or investment advice and is not regulated by the FCA*

# Mr E (Liberty SIPP)

## Reasons for decision

### Adjudicator

- Insufficient adherence to February 2013 guidance
- No checks on employer/member connection
- No dialogue between Mr E and Liberty
- Even if Liberty had carried out a full due diligence, unlikely to have been able to state categorically that it was a scam
- But enough known risk factors that member should be contacted, given warnings and asked to explain or directed to TPAS

### Ombudsman

- Threat of scams well-known by 2017
- Red flags:
  - Type of receiving scheme (SSAS)
  - Geographically distant employer
  - Newly registered employer
  - Unregistered adviser/administrator
  - Pressured Liberty to complete transfer
- Should ask member to explain advice taken, documentation received, and pressure exerted
- Missing the point whether warnings would have dissuaded Mr E from transfer – Liberty's responsibility to give warnings and put Mr E in position to make informed decision

# Mr E (Liberty SIPP)

## Learning points

- TPR guidance elevated from best practice/guidance to a requirement
- No injustice, just maladministration
- Significant that transfer was in 2017 not 2013?
  - o Distinguish from PO-12324 where transfer made in March 2013
- Don’t delay, but do the checks!
- Assess third party administrators with rigid procedures

# Mr T (James Hay)

## Transfer delays

- Member of the Tenco Scheme
- Scheme administrator: James Hay
- Mr T requests transfer to SIPP before Brexit referendum
- Lost opportunity for financial profit by investing in stock markets post-referendum
- Intended to invest in FTSE 100 if result was to exit the EU

# Mr T (James Hay)

**24 March 2016:** Mr T contacts James Hay to request transfer

**6 May 2016:** *"must be done before 30 June"*

**10 June 2016:** *"desperately keen to be back in the market before Brexit"*; *"target is before 23rd, that's key to me"*

**23 June 2016:** Brexit referendum – Mr T complains

**July to October 2016:** cash paid out and transfers made

**Ombudsman (first instance)**

- Maladministration but no loss
- Not foreseeable or measurable
- Mr T failed to disclose specific shares
- £2k distress and inconvenience

**High Court**

- Foreseeable that delay could cause loss
- Ombudsman confused quantification and recoverability
- Ombudsman to determine date money should have been available
- Mr T to show what he would have done

**Ombudsman (second instance)**

- Transfer would have completed by 23 June
- Mr T likely to have invested full amount in FTSE 100
- Financial profit of £43k plus interest

# Mr T (James Hay)

## Learning points

- Loss of opportunity can be quantifiable
    - More difficult for trustees to argue financial loss not clear
    - Applies to other incorrect statements?
- How much investigation should trustees do?
- Balance against checking for scams
    - Clear and rigorous process with administrators
- Covid-19, more claims?

# Any questions?

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