STEPHENSON HARWOOD

pensions law group

Snapshot

January 2023

Overview

- The Pensions Regulator publishes its draft funding code of practice
  The Pensions Regulator (**Regulator**) has now published its draft defined benefit funding code for consultation. This provides more detail for trustees on, in particular, the investments, level of risk and journey plans they need to consider when achieving their long-term funding target.

- EU PPF case law preservation?
  Certain ECJ judgments relating to the calculation of PPF benefits will not be retained. This will open the door for the PPF to move away from minimum benefit limits imposed by EU law.

- Regulating pensions and retirement income: FCA/Regulator regulatory strategy update
  In December, the Regulator and the Financial Conduct Authority (**FCA**) published an update to their joint regulatory strategy, highlighting the importance of collaboration between regulators to enhance and protect savers' outcomes. The strategy notes eight joint workstreams where the regulators are working "hand in hand".

- DC schemes: 'Member's outcomes: Why it's time for a change' - blog published by the Regulator
  A recent blog published by the Regulator encourages trustees to improve their investment decision skills and consider whether their governance structures are fit for the future investment environment.

- Pensions-related aspects of the Edinburgh Reforms
  A wide-ranging set of reforms of the financial services sector, referred to as the 'Edinburgh Reforms', were announced by the Chancellor of the Exchequer on 9 December 2022. A number of these impact pension schemes.

- Pensions Ombudsman case – trustees need to ensure sufficient due diligence before transferring out
  This case highlights the importance for trustees to undertake sufficient due diligence before undertaking a transfer out to avoid full liability for transfers that turn out to be scams.

In more detail

The Pensions Regulator publishes its draft funding code of practice

The Pension Schemes Act 2021 provided a framework for a new defined benefit funding regime. Draft regulations published last year filled in some of the detail of what would be required but the industry has been waiting for a revised code of practice from the Regulator to understand what much of this will mean in practice.

The Regulator has now provided a draft of this new code, on which they are consulting (**Draft Code**). The consultation period will close on 24 March 2023. The intention is that the Draft Code will come into force from October 2023.

Under the new regime trustees will be required to produce a funding and investment strategy which sets out how they will meet their long-term funding target. The Draft Code discusses the types of investments and level of risk available to trustees under this new approach, as well as setting out the maturity level of the scheme by which the long-term funding target will need to be met.

Trustees should start considering the impact the new approach will have on the funding of their schemes and in particular their investment portfolio. Equally, employers will need to understand what impact the long-term funding and investment strategy will have on the funding position and requirements of the scheme as well as the length of their recovery plans. More information on the Draft Code can be found in our briefing on the topic here.

EU PPF case law preservation?

The House of Commons Public Bill Committee has rejected an amendment to the Retained EU Law (Revocation and Reform) Bill that would have otherwise retained certain ECJ judgments relating to the calculation of PPF benefits in English law.

This amendment would have preserved the *Bauer* line of case law which ensured that members of insolvent schemes that had entered into the PPF received an increase to the level of benefits set by the PPF in certain cases. The PPF provides compensation at 2 different levels. Pensioners over normal retirement age receive 100% of their benefits, whereas deferred members (and pensioners under normal retirement age other than because of ill-health) receive 90% of their benefits, subject to a compensation cap. It is this second category of compensation level to which this line of case law applies.

In 2019, the *Bauer* decision stated that the PPF must ensure members do not fall below the poverty line when the employer becomes insolvent. The Hampshire case, in September 2018, held that members should not receive less than 50 per cent of their entitled pension benefits from the PPF. Finally, the Hughes case in 2021 held that members should not receive less than 50% of guaranteed benefits and that the compensation cap on deferred members should not apply.

The Minister of State for Business, Energy and Industrial Strategy has confirmed that the DWP does not intend to implement the Bauer judgment, citing is as a clear example of where an EU judgment conflicts with the UK Government's policies on UK private pensions protection schemes.

Regulating pensions and retirement income: FCA/TPR regulatory strategy update

In December, the Regulator and the FCA published an update to their joint regulatory strategy, highlighting the importance of collaboration between regulators to enhance and protect savers' outcomes.

The update noted eight joint workstreams: productive finance, value for money, a regulatory framework for effective stewardship, pension scams strategy, defined benefit (**DB**) transfer advice, DB schemes and transfer activity, pensions dashboards and supporting consumer decision-making throughout the pensions consumer journey.

The Regulator and FCA highlighted the eight joint workstreams as demonstrating a "fundamental shift" in the working relationship between the FCA and the Regulator where the two are now working "hand-in-hand".

The update divides the ongoing work between the regulators into three parts: the joint assessment of risk and harms, such as the work to tackle pension scams through the Pension Scams Action Group and intelligence sharing; joined-up working on cross-sector initiatives, such pensions dashboards and a consistent framework for assessing value for money; and communications around joint work, such as joint communications around DB transfer concerns.

The Regulator and FCA note that it is through co-ordinated action by everyone in the sector that the regulators deliver on their strategy and achieve good outcomes for pension savers now and in the future.

DC Schemes: 'Member's outcomes: Why it's time for a change' - blog published by the Regulator

A blog has been published by the Regulator in which it encourages trustees of DC schemes to improve their investment decision skills and consider whether their governance structures are fit for the future investment environment.

The Regulator addresses better governance and the need for trustees to consider better member outcomes by either transferring members' benefits to another scheme (such as by consolidating with larger scale providers) or making any improvements necessary to their own scheme to ensure it offers value.

The publication of guides by the Productive Finance Working Group is welcomed by the Regulator as these are aimed at supporting trustees and advisers in considering opportunities offered by illiquid assets.

Pensions-related aspects of the Edinburgh Reforms

A wide-ranging set of reforms of the financial services sector, referred to as the 'Edinburgh Reforms', were announced by the Chancellor of the Exchequer on 9 December 2022. Those that are pensions related are as follows:

- The DWP alongside the FCA and the Regulator, will consult on a new value for money framework for defined contribution (DC) schemes. This will set required metrics and standards for all schemes in areas such as investment performance, costs and charges, and quality of service.

- The DWP will draft regulations that will remove certain performance fees from the charges cap that applies in default funds in DC schemes used for auto-enrolment. This is intended to enhance investment in liquid assets.
- The government will consult on new guidance for the Local Government Pension Scheme on asset pooling.
- HM Treasury and HMRC published a joint consultation on proposals for reforming the VAT treatment of fund management services. This proposes to provide legal clarity by codifying the existing position under UK VAT law and retained EU law. This would include establishing defined criteria to determine which funds are entitled to the special investment funds exemption.

Pensions Ombudsman case – trustees need to ensure sufficient due diligence before transferring out

Mrs G complained that the Teachers' Pension (**TP**) did not conduct sufficient due diligence checks when transferring her pension benefits to the London Quantum Pension Scheme (**LQPS**), where it was invested in high risk, unregulated assets unsuited to pension fund investment.

In January 2015, Mrs G received advice from Investaco, an unregulated firm not authorised to give investment advice. They introduced her to LQPS. Gerard Associates Ltd (**Gerard**) then subsequently provided her with advice in respect of transfer. Mrs G received a transfer analysis report from Gerard which highlighted the advantages of the proceeding with the transfer and was also accompanied by a pro forma letter for Mrs G to sign agreeing that she was not taking any form of pension liberation. Mrs G completed the forms and the transfer from TP was completed on 18 Feb 2015.

In April 2015, Friends Life wrote to Mrs G flagging concerns about LQPS and confirming it was unable to proceed with the transfer of the two pensions she had with Friends Life to LQPS.

Mrs G complained to the Pensions Ombudsman (**PO**) regarding the transfer from TP to LQPS arguing that had TP flagged up similar concerns regarding the LQPS she would not have transferred her pension from TP.

TP placed heavy reliance on the fact that Mrs G had validly exercised her statutory right to transfer and therefore TP, who had been criticised in previous decisions for delay in the transfer process, wanted to proceed with the transfer within the timeframes.

The PO found that Mrs G did not, in fact, complete her application form to transfer within the 3 month statutory transfer deadline and so TP was under no obligation to proceed with the transfer. In addition, even if TP did believe it was under a statutory obligation to effect the transfer, it still had to carry out sufficient due diligence. Further, the only contact made by TP to Mrs G directly was in respect of a previous CETV request the member had made but decided not to go ahead with. That letter had contained no warning about the risk of scams or fraud.

PO noted that TP's actions showed a '*surprising lack of understanding at the time of the transfer of the Regulator's expectations to put proper processes in place to protect members, which was widely understood in the industry and is highlighted by the fact that Friends Life rejected the transfe*r'. TP prioritised processing the transfer quickly. PO found TP had sufficient time to carry out the due diligence and therefore TP's failures amounted to serious maladministration.

PO found that had TP put in place proper processes to identify transfers to potential scam arrangements and warned Mrs G of the risk of transferring her benefits from TPS to LQPS, she would have withdrawn her transfer request.

TP was ordered to reinstate Mrs G's accrued benefits in TP, adjusting for any revaluation, and pay £1,000 to reflect the 'serious distress and inconvenience' she has suffered.

This case serves as a reminder to trustees to ensure that appropriate due diligence is carried out in the context of transfers. The requirements are even more stringent now with the advent of red and amber flags, which trustees should ensure they are actively considering in response to any statutory transfer request received.

Our wider team – a closer look

Contentious pensions

Our pensions litigation practice enjoys an unrivalled position in the City, working closely with contentious trusts, regulatory and pensions advisory, ensuring that every aspect of their varied caseload is expertly addressed. Our contentious pensions team are first and foremost litigators, but they are also immersed in the pensions industry, with expert knowledge of the varied claims which arise. From defending and bringing claims for professional negligence, applying for construction and rectification applications, to dealing with regulatory and judicial review proceedings, the claims covered are extremely broad.

The team acts for a broad range of clients, including employers, trustees, pensions professionals, law firms and as a trusted advisor to in-house legal teams, in all types of claims. The team also has specific experience acting for representative beneficiaries, particularly in the context of court applications, in high profile, large scale Representative Beneficiary applications, for example having acted in this capacity in relation to the BBC and BT pension schemes.

Rare for pensions litigators, our team also has experience leading cross-border and international disputes, dealing with pension scheme claims in off-shore jurisdictions, whether connected with fraud, pension liberation or more general pensions related claims. Cases with a regulatory context (another team specialism) increasingly feature in our work, such as with investigations and sanctions, and advising our clients in respect of funding and restructuring disputes. The team have acted for large utility companies in relation to a wide range of regulatory disputes concerning pension funds, as well as on public law challenges (such as the *East Midlands Franchise* litigation against the Department of Transport).

The team is particularly well-known for defending claims against pensions professionals, as well as (uniquely) *also* acting for claimants. The team is currently acting for Mercer in the ongoing and highly complex *Honda* litigation. We also have a good deal of experience advising claimants and defendants in relation to disputes arising from investment advice; and most recently related to market volatility and the recent LDI crisis.

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