STEPHENSON HARWOOD
pensions law group

Snapshot

October 2022

Overview

- Pension issues from the 'mini budget'
  The government has suggested it will remove certain performance fees from the occupational DC charge cap and that, as part of a deregulatory package for UK financial services, the government will replace Solvency II Regulations with "rules tailor made for the UK".

- All change for RPI – court declares change of RPI to CPIH lawful
  The trustees of five pension funds brought judicial review challenges against the decision by the then-Chancellor (and the UK Statistics Authority (**UKSA**)) that Retail Prices Index (**RPI**) should be aligned with **CPIH** (the Consumer Prices Index including owner occupiers' housing costs). The High Court rejected the challenges and determined that the process by which the decision was reached, and the decision itself, was not unlawful. RPI is therefore set to be changed from February 2030 to be aligned with CPIH. The government will also not provide compensation as a result of the change.

- PASA guidance on administration transfer exit agreements
  The PASA Exit Agreements Working Group has published guidance on administration transfer Exit Agreements. This has been prompted by concerns expressed by PASA's members in relation to the transfer of pensions administration services between administrators. Scheme trustees and administrators need to be proactive and check their current administration contract to see if there are contractually agreed terms on exit, even if a transfer of administration services is not currently being considered.

- The Pensions Regulator's expectations of trustees and sponsoring employers when refinancing in the current climate
  The Pensions Regulator (**TPR**) has issued a number of factors that sponsors and trustees should take into account when refinancing is being considered in this current economic climate.

- TPR responds on employment status guidance
  New guidance published at the end of July, brings together employment status case law into one place for businesses and individuals to access. It is intended to help workers by improving their understanding of what rights they are entitled to at work, enabling them to have informed discussions with their employer and take steps to claim or enforce them where necessary. The guidance also clarifies the rights of gig economy workers.

  In a letter to the Chair of the Work and Pensions Select Committee dated 1 September 2022, TPR has responded to a question as to whether the guidance will help TPR determine whether the worker test is met, in order to enforce pension rights and, if so, how.

- Mrs G (CAS-75166-S3Y9): increased award against employer who did not engage with Pensions Ombudsman
  In this case the Pensions Ombudsman increased the award given for distress and inconvenience, partly due to the employer's lack of engagement with the Pensions Ombudsman during the complaint.

Further information

Pension issues from the 'mini budget'

Removal of performance fees from occupational DC charge cap:

The government also revealed that they were bringing forward draft regulations to remove "well-designed performance fees" from the occupational DC pension charge cap. The rationale is to ensure savers can benefit from higher potential investment returns while providing funding to help unlock investment into the UK's most innovative businesses and assets. The charge cap currently prevents DC plans applying annual charges of more than 0.75% on members' pots.

It is unclear when the changes might be made and how "well-designed performance fees" will be defined. It is also unclear how much this might change the institutional investment landscape, given pensions trustees have a duty to act in their members' best financial interests and costs are only one factor in determining financial value.

Solvency II:

Expected later this autumn, as part of a deregulatory package for UK financial services, the government will replace Solvency II Regulations with "rules tailor made for the UK". Solvency II is an EU Directive that came into force on 1 January 2016, which sets out regulatory requirements for insurance firms, including those involved in de-risking pensions schemes. It sets requirements around financial resources, governance and accountability, risk assessment and management, supervision, reporting and public disclosure.

The replacement package is expected to make it easier for insurers to:

- use longevity reinsurance,
- invest in a wider asset base;
- calculate more favourable investment default reserves; and
- reduce their risk capital percentages.

Any planned watering down of the requirements could potentially introduce new risks which insurers will need to manage. However, it may also improve buy in/buy out pricing and capacity within the market.

All change for RPI – court declares change of RPI to CPIH lawful

The composition of the RPI is set to change from February 2030. RPI index values will be calculated using the same methods and data sources that are used to calculate the CPIH. This would likely result in RPI being lower by an average of 1% per annum. Pension schemes (in particular, defined benefit schemes) are expected to be affected in two ways:

1. a reduction in the value of any RPI linked assets; and
2. a reduction in any liabilities linked to RPI (for example indexation and revaluation calculated on the basis of RPI).

Given that many defined benefit pension schemes are invested in RPI-linked gilts, the proposed change could have a detrimental impact on the funding position of a number of schemes. A large number of pension schemes with CPI linked liabilities will have RPI linked assets. For these schemes, their funding position will be negatively affected as the value of their assets will fall while the level of their liabilities will not change.

The trustees of five pension funds brought judicial review challenges against the decision by the then-Chancellor (and the UK Statistics Authority (**UKSA**)) that (i) RPI should be aligned with CPIH; and (ii) that no compensation was payable as a result of such change. The High Court rejected the challenges and determined that the process by which the decision was reached, and the decision itself, was not unlawful. The High Court also held that compensation did not have to be paid.

RPI is therefore set to be change from February 2030 to be aligned with CPIH. The government will also not provide compensation as a result of the change. For more information on the case, please see our briefing on the topic here.

PASA guidance on administration transfer exit agreements

The PASA Exit Agreements Working Group has published guidance on administration transfer Exit Agreements. This has been prompted by concerns expressed by PASA's members in relation to the transfer of pensions administration services between administrators. In particular, members have highlighted the need to address the following common issues with the ceding administrator:

- delays in attending handover meetings and providing data and records, which restricts the time available for the new administrator to validate and map records to their administration platform and test the programming of benefit calculations;
- unreasonable charges for completing the transfer of services or the imposition of "out of scope" services not made clear at the outset; and
- deterioration in the service provided during the notice period.

The guidance is designed to bring these issues to the forefront of administrators' and the industry's minds when transferring administration services and, therefore, support trustees and administrators to plan and manage a smooth handover of administration services. It reproduces a revised version of PASA's *Code of Conduct on Administration Provider Transfers* (the **Code**).

Changes are made to the Code from 1 January 2023 to strengthen adherence to the Code and provide clarity around the transfer of administration services process. These changes require scheme trustees and administrators to be proactive and check their current administration contract to see if there are contractually agreed terms on exit (an **Exit Agreement**). In particular, and regardless of whether or not a transfer of administration services is anticipated:

Trustees should.....

- Review the contract to be clear on the agreed terms of the Exit Agreement.
- If the contract doesn't include an Exit Agreement, consider:
  - putting one in place (trustees are more likely to secure favourable terms with an incumbent administrator rather than one whose contract has been terminated); or
  - request a copy of the administrator's policy for transferring scheme administration (Appendix 1 to the guidance contains a template policy on transferring administration services).

Administrators should.....

- For existing administration appointments, review, or put in place, a clearly stated policy on transferring schemes to a newly appointed administrator. This policy should reflect the Code and be:

  - provided to the trustees where existing contracts don't include an Exit Agreement; and/or
  - available to trustees on request as a commitment to best practice on transferring administration.
- For new administration appointments, the contract should include an Exit Agreement setting out the terms in the event of a subsequent transfer of services.

An Exit Agreement should establish clarity on:

- the terms on exit, including Service Level Agreements for provision of information and data, and the stated responsibilities of the trustees and the ceding administrator;
- scope of services covered; and
- fees, including any additional out of scope charges and the charge rates applied.

A template Exit Agreement can be found in the guidance.

The Pensions Regulator's expectations of trustees and sponsoring employers when refinancing in the current climate

TPR expects that pension trustees and sponsoring employers take into account a number of factors when refinancing in the current climate. These include:

- Interest costs and fees: The employer's ability to make pension payments could be impacted by changes in the cost of debt (interest and fees). Trustees should understand the impact of any such changes on the employer covenant.
- Debt structure: Trustees should make sure they understand the potential effects of different types of debt when an employer is seeking to switch from one type of debt to another.
- Security/ guarantees: Lenders often obtain security over assets when lending. In the case of insolvency, such security would normally rank above the trustees' claims. Trustees should ensure they understand the implications of any changes on their position on an insolvency.
- Financial covenants: Financial covenants are usually indicators of a company's financial health. When they are breached, they give debt holders the option to take action such as call in their debt or modify the terms in other ways. Trustees should be aware that a change in covenant could give power to a lender at the expense of the trustees.
- Restrictive covenants: Financing agreements may contain restrictions that limit the employer's capacity to engage in specific activities. Trustees should be mindful of such clauses, which may restrict their ability to agree appropriate funding plans or protections for the scheme.
- Counterparty: Sponsors can refinance with the same lender or a different lender. Changes in the above areas are more likely to occur where a new lender is used and trustees should be aware when new lenders are proposed.

TPR responds on employment status guidance

New guidance published at the end of July, from the Department for Business, Energy & Industrial ("**BEIS Guidance**") brings together employment status case law into one place for businesses and individuals to access. It is intended to help workers by improving their understanding of what rights they are entitled to at work, enabling them to have informed discussions with their employer and take steps to claim or enforce them where necessary. The guidance also clarifies the rights of gig economy workers.

In a letter to the Chair of the Work and Pensions Select Committee dated 1 September 2022, TPR has responded to a question as to whether the guidance will help TPR determine whether the worker test is met, in order to enforce pension rights and, if so, how. TPR notes that in this regard:

- The BEIS Guidance will be a useful document to which TPR can refer as part of its discussions with employers and during relevant enforcement proceedings, which the courts and tribunals may find persuasive;
- The BEIS Guidance however does not change the law and is not legally binding. Moreover, on any challenge by an employer of enforcement action by TPR to the First Tier Tribunal ("**FTT**") or Upper Tier Tribunal ("**UTT**") the FTT or UTT cannot directly adopt decisions of the Employment Tribunal– the FTT AND UT must form their own decisions taking into account the specific facts of the case.

The letter from TPR notes that TPR remains committed to protecting those who have non-standard employment relationships, including gig economy workers, and ensuring employers do the right thing (and it will continue to take enforcement action where appropriate to ensure savers are protected).

Mrs G (CAS-75166-S3Y9): increased award against employer who did not engage with Pensions Ombudsman

Mrs G was a member of an occupational pension scheme from October 2018 and up until July 2020 employee contributions were deducted from Mrs G's salary and paid into the Scheme, together with the corresponding employer contributions. However, Mrs G discovered that her employer had failed to make pension contributions to the scheme for the period July 2020 to May 2021, although her pay slips for this period showed that her employer had deducted a total of £1,243.07 in pension contributions.

Mrs G made a complaint to the Pensions Ombudsman and an Adjudicator provided an Opinion to which the employer did not respond.

The Ombudsman upheld Mrs G's complaint, agreeing with the Adjudicator's opinion but awarded Mrs G £1,000 for the "serious" distress and inconvenience she had experienced rather than then the £500 awarded by the Adjudicator for "significant" distress and inconvenience. This was as a result of the employer exacerbating the situation through its failure to respond to the Ombudsman's office during its investigation of the complaint. The employer was also ordered to produce and issue a schedule detailing the unpaid employee contributions deducted from Mrs G's salary, along with the corresponding employer contributions and ordered to pay the total missing contributions to the scheme. This was on top of compensation for any investment loss incurred as a result in the shortfall in the number of units Mrs G would have purchased had the contributions been paid on time.

This complaint highlights that where there is a lack of engagement with the Ombudsman's office, the Ombudsman may increase the award for non-financial injustice to reflect this.

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