May 2023

In Sight

This Quarter's Round-up

Regular Features

Pensions Tax Changes

In a surprise move, the Chancellor announced significant improvements in both the lifetime allowance and annual allowance provisions in the Spring Budget.

The government's broad intention is to encourage older workers to delay retirement, but in general these changes will provide significant additional scope for tax-efficient pension savings.

Continued on next page

The main pensions measures were effective from 6 April 2023:

- The **lifetime allowance** (LTA) is the maximum amount of tax-free pension savings an individual can build up over a lifetime. It is currently £1,073,100 but is being abolished in two stages: from 6 April 2023 no LTA charge will arise, and the LTA itself will be removed from 6 April 2024. For 2023/24, administrators will still need to operate LTA checks when calculating and paying benefits.
- Where a lump sum would have triggered the 55% LTA charge, tax will instead apply at the recipient's marginal rate of income tax.
- Members with various protections against the current level of LTA will be able to accrue new pension benefits, join new arrangements or transfer without losing this protection (provided they had applied for the protection before 15 March 2023).
- The **maximum tax-free lump sum** available when a member takes their benefits (the 'pensions commencement lump sum') is frozen at £268,275 (25% of the current LTA) for those without protections. Individuals who have a protected right to take a higher lump sum will keep this.
- The **annual allowance** increased from £40,000 to £60,000. This is the maximum amount of pensions savings an individual can make each year with tax relief without incurring a tax charge.
- The **tapered annual allowance** reduces the annual allowance for high earners. The minimum level has increased from £4,000 to £10,000, and the income threshold at which the taper starts has increased to £260,000. The effect of this is that individuals have their annual allowance reduced by £1 for every £2 of 'adjusted income' more than £260,000, down to a minimum of £10,000.
- The **money purchase annual allowance** increased from £4,000 to £10,000. This applies where a member has flexibly accessed money purchase pension benefits.

The 6 April 2023 measures are being introduced via the Finance (No. 2 Bill) 2022-23, with the abolition of the LTA from 6 April 2024 legislated for in a future Finance Bill.

HMRC has issued Pension Schemes Newsletter 148 to summarise the Budget changes and a Lifetime allowance newsletter aimed at administrators. We expect further guidance to be issued, in particular on more detailed aspects of the removal of the LTA from 6 April 2024.

The Labour Party has indicated that the LTA abolition would be reversed if it came into power at the next general election.

Action

There are a number of practical issues for trustees and employers to consider, and there is likely to be an increase in member queries.

Trustees should liaise with their advisers and administrators to ensure they understand the changes and what actions are needed. In the short term, the changes should be communicated to employees so that they can review their pension savings.

Employers may wish to review their pension arrangements in light of the improved pensions tax position.

Climate Change and ESG

Climate Change and ESG Compliance

The Pensions Regulator (TPR) has published a blog to explain why it is putting extra emphasis on compliance with environmental, social and governance (ESG) and climate change reporting duties in 2023 and what is being asked of trustees. This builds on its campaign launched in February.

Currently, trustees of schemes with at least 100 members are required to publish a statement of investment principles (SIP) containing information about the scheme's investment policies, including consideration of financially material ESG and climate factors and of members' views on non-financial matters. They must also publish an implementation statement (IS) each year showing how the principles in the SIP have been implemented. As mentioned below, larger schemes, must also publish an annual TCFD report. Website addresses for all these documents must be included in the scheme return that is submitted to TPR.

TPR is analysing scheme return data, to check that SIPs, ISs and TCFD reports are being published as required. Initial analysis of the 2022 DC scheme return data highlighted that a number of schemes did not provide valid website addresses for their SIPs and ISs.

In the summer there will be a review of a cross-section of SIPs and ISs, with the outcome being shared to highlight good practice.

TPR warns that enforcement action may be taken against trustees if they fail to publish their SIP and/or IS.

Action

Trustees should ensure that, if appropriate, they have published their SIP, IS and TCFD report online, and that they include the correct URL in their scheme return.

Review of TCFD Reports

TPR has published the results of its first review of a selection of pension schemes' annual climate-related disclosures, with a view to sharing emerging good practice and areas for improvement.

The reporting requirements were developed from the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD) and came into force from 1 October 2021 for the largest schemes. TCFD reporting is currently mandatory for schemes with relevant assets exceeding £1 billion, and for authorised master trusts and CDC schemes.

Having reviewed 71 TCFD reports, TPR found that almost all reports were published on time, and that they showed an encouraging level of trustee engagement with the new requirements. Some reports included helpful non-technical summaries for members.

TPR has highlighted several common issues that it asks trustees to consider when producing their next report:

- a lack of sufficient background information on the scheme can make disclosures difficult to interpret;
- for schemes with more than one DB section or popular DC arrangement, disclosures of strategy, scenario analysis and metrics activities should be provided at the appropriate level (in line with the DWP's statutory guidance); and
- accessibility issues should be considered, to ensure members and others can easily find and print online reports.

TPR indicated that it would be unlikely to issue fines in relation to the first wave of reports (other than for failure to publish online in time, or for not taking reasonable steps to comply). But it reminds trustees that it has discretion to issue penalties of up to £5,000 per individual trustee and £50,000 per corporate trustee where there has been a failure to comply with these requirements.

Government Plans for DC Schemes

The government recently announced a package of measures for defined contribution (DC) pension schemes — including new regulations relating to the DC charge cap and investment disclosures, and consultations on value for money and small pots. None of the measures are entirely new; they were simply released under one banner about creating fairer, more predictable, and better-run pensions.

New Disclosures and DC Charge Cap Changes

Following several consultations, the government has confirmed that it is proceeding with legislation intended to encourage trust-based DC schemes to invest in a broader range of assets. New regulations have been made and statutory guidance has been finalised.

The **charge cap**, which applies to default funds in DC schemes used for auto-enrolment, is seen as a barrier to trustees considering investment in certain illiquid assets. Therefore, from 6 April 2023, trustees can exclude specified performance-based fees from their charge cap calculations. Trustees must calculate and disclose any such performance-based fees that members incur in their annual chair's statement, as they already do for other costs and charges. They must also take any performance-based fees into account in the value for members assessment.

From 1 October 2023, trustees of schemes with DC benefits (unless the only DC benefits are AVCs) will also be required to **disclose and explain**:

- their policy on illiquid investments, within their default fund statement of investment principles (SIP).
- the default fund asset allocation (split between eight asset classes and shown separately for different ages), within their annual chair's statement.

Actions and Deadlines

Those schemes that opt to exclude specific performance-based fees from the charge cap calculations will need to disclose this in the chair's statement in relation to the first scheme year that ends after 6 April 2023. This information must also be published online.

All schemes in scope must comply with the disclose and explain requirements. The information on asset allocations must be included in the chair's statement for the first scheme year that ends after 1 October 2023. It must be updated annually and published online alongside other relevant parts of the chair's statement.

The policy on illiquid investments must be included when the default SIP is first updated after 1 October 2023, or by 1 October 2024 at the latest.

Value for Money (VFM) Framework

A joint consultation on a common VFM framework to apply across all workplace DC schemes has been launched by the Department for Work and Pensions (DWP), the Pensions Regulator (TPR) and the Financial Conduct Authority (FCA). Taking account of industry views from a previous TPR/FCA discussion paper, it will impact both trust-based and contract-based schemes.

Under the proposals, workplace DC schemes will be required to disclose, assess, and compare the VFM their scheme provides, shifting the focus from member-borne costs towards a more holistic assessment of overall value. The aim is for greater transparency and standardisation of reporting across the DC pensions market, to improve comparability and competition between schemes. This would allow trustees and Independent Governance Committees (IGCs) to make more informed investment and governance decisions and employers to better compare value and performance between schemes.

The proposed framework will look across key elements of VFM (investment performance, costs and charges, and quality of services), with schemes having to disclose key metrics and service standards. Trustees and IGCs would be required to conclude whether the scheme is:

1. VFM
2. Not currently VFM but could be with certain identified improvements
3. Not VFM

This is designed to build on and eventually replace the annual prescribed assessment that trustees of smaller schemes (with assets of less than £100 million) have been required to complete since October 2021. The DWP is considering whether TPR should have new powers to enforce wind-up and consolidation where a scheme is consistently not offering value.

In a subsequent blog, TPR clarified its approach and what it hopes to achieve on VFM.

The consultation closed on 27 March 2023. The detail of what would be calculated and disclosed will be addressed in further consultations on regulations for trust-based schemes and on FCA rules for contract-based schemes. There is no timescale for implementing this regime.

Deferred Small Pots Call for Evidence

The government has issued a call for evidence on addressing the challenge of deferred small pots, with possible solutions for how these could be consolidated. In part because of the success of auto-enrolment, individuals are likely to have several deferred pots (to which contributions have ceased) from previous employments. The government wants to gather evidence about the scale and characteristics of the growth in the number of such pots. This builds on the investigations of the Small Pots Cross-Industry Co-Ordination Group, which did the groundwork on the issues involved but identified that a more detailed analysis was required.

The DWP's focus is now on two large-scale automated consolidation solutions:

- **Default consolidator** — eligible pots would automatically be transferred to a small pot consolidator.
- **Pot follows member** — when a member changes jobs, eligible pots would automatically be transferred to their new employer's scheme.

In both cases, individuals would have the opportunity to opt out should they wish.

Solutions will be considered against five key criteria (which include improving member outcomes and engagement, and minimising complexity and administrative burdens for employers). Several key questions need to be considered, such as what is 'small', should there be a minimum pot size for consolidation to happen (the government suggests possible limits: £1,000, £2,500, £5,000 and £10,000), and at what point should a pot be considered to be deferred.

The call for evidence closed on 27 March. There are no firm proposals yet; the responses will help inform the development of an approach that will be consulted on in due course.

Engagement With Members

Alongside the above consultations, the DWP released research on Understanding member engagement with workplace pensions. This found that barriers to engagement with pensions included detachment, fear, and complacency. Although participants did not actively seek information about their pension, they recognised the importance of information they were sent. Letters and other printed information about pensions were seen as being important and were more likely to be engaged with than emails. The research also identified some ways to improve engagement.

LDI Developments

The Pensions Regulator has published new guidance setting out further practical steps trustees should take to manage risks when using leveraged liability driven investments (LDI). This follows the gilt market volatility of last autumn, on which we reported in the February edition of In Sight.

In the guidance, the Regulator clarifies that it expects trustees to only invest in leveraged LDI arrangements that have put in place an appropriately sized buffer. This must include an operational buffer specific to the LDI arrangement to manage day-to-day volatility, in addition to the 250 basis points (bps) minimum buffer to provide resilience in times of market stress. The FCA has published related guidance for LDI managers.

Prior to this, further evidence had been given to parliamentary committees and actions proposed to reduce the risk of similar disruption in future.

In February, the House of Lords' Industry and Regulators Committee criticised the use of leveraged LDI strategies by DB pension schemes, stating that they worsened the financial turmoil following the September 2022 mini-Budget. In a letter to the Economic Secretary to the Treasury and the pensions minister, the Committee outlined the findings of its scrutiny work and called in particular for regulators to introduce greater control and oversight of the use of borrowing in LDI strategies.

The Bank of England has also given oral evidence to the Work and Pensions Committee, explaining that it is working with the Pensions Regulator and LDI fund regulators to decide on the appropriate 'steady-state' response. The Bank's Financial Policy Committee had recommended that the Pensions Regulator specify minimum levels of resilience for LDI funds as soon as possible, suggesting that these funds should be resilient to a yield shock of around 250bps as a minimum, in addition to the resilience required to manage other risks.

Action

Schemes with LDI investments should discuss the latest guidance on LDI with their investment consultants.

Automatic Enrolment Changes Planned

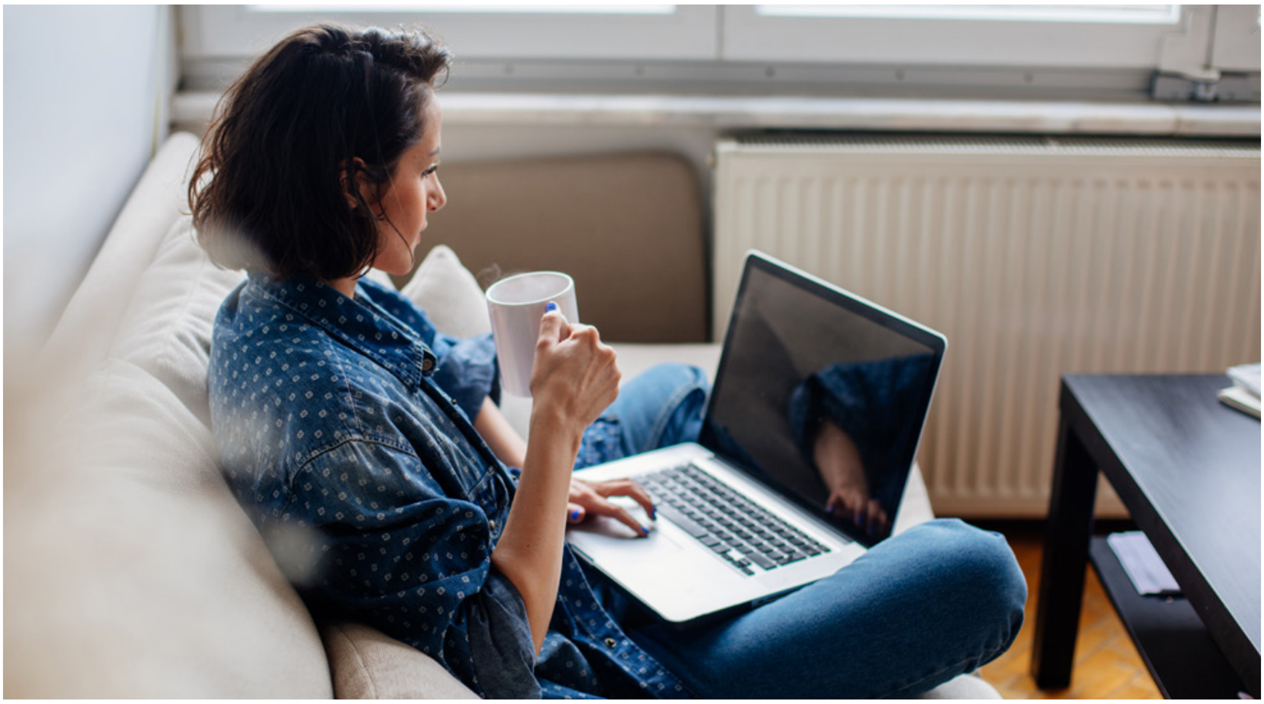
The government has given its support to a Private Member's bill that proposes to extend automatic enrolment by:

- reducing the lower age limit at which eligible workers must be auto-enrolled from 22 to 18; and
- removing the lower qualifying earnings threshold so that minimum contributions to defined contribution (DC) arrangements are calculated from the first pound earned.

This is in line with proposals within the government's 2017 review of automatic enrolment, which it intended to introduce in the mid-2020s.

Private Members' bills do not usually become law, which was the case when this Bill was first introduced to Parliament last year. However, now that it has government support, it is more likely to proceed.

There is no timetable for the changes to come into effect; the Secretary of State would be given powers to make implementing regulations following consultation. The government plans to launch a consultation in the autumn on the implementation approach and timetable.



Extra Time Needed for Pensions Dashboards

The government has announced that additional time is needed to deliver pensions dashboards. The Pensions Dashboards Programme (PDP), responsible for delivering dashboards, requires extra time to ensure that the infrastructure is safe, secure, and works for both pension schemes and the end users of the service.

The government says that the framework remains fit for purpose and dashboards are still going ahead, the only thing that is going to change is the connection deadlines. It intends to provide a further update before Parliament's summer recess that begins on 20 July 2023.

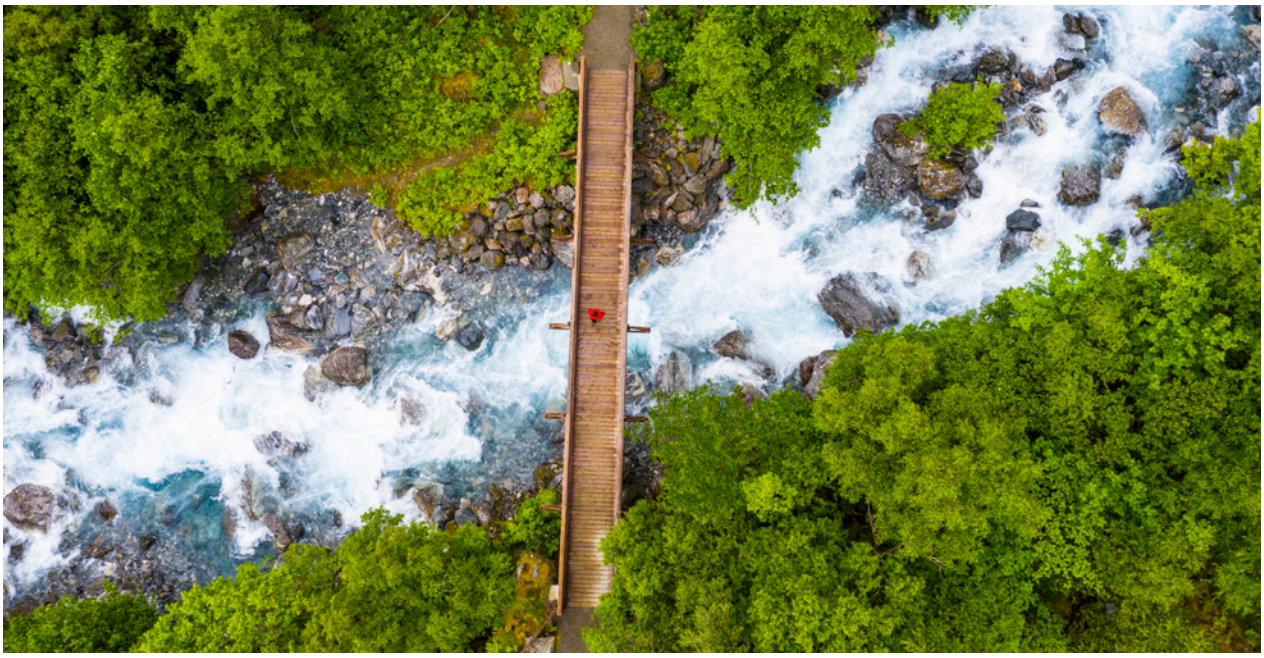
This means that the current staging timeline needs to be revised — we understand that all schemes' connection deadlines will be delayed (perhaps by around 12 months) but this has not yet been confirmed. The Department for Work and Pensions has said it will legislate at the earliest opportunity to amend the connection deadlines in its regulations. The Financial Conduct Authority has said that it will make a corresponding change to the deadlines in its dashboard rules in due course.

The PDP has subsequently published answers to some frequently asked questions, including on the cause of the delay and what providers and schemes can be doing to prepare in the meantime.

The Pensions Regulator has updated its initial pensions dashboards guidance and revised its checklist to help schemes continue with their preparations. Commenting on the announcement it says that there will be significant work involved in complying with dashboards duties and strongly advises trustees to make the most of the time available.

Action

The government, the Pensions Regulator and the PDP have all made it clear that dashboards are still going ahead. Therefore, pensions dashboards should be a standing item on trustee board agendas, and schemes should continue with their preparations until further information is given.



Pensions Regulator Update

Guidance on Improving EDI

The Regulator has published equality, diversity and inclusion (EDI) guidance for pension scheme governing bodies and for sponsoring employers. Its aim is to improve the EDI of schemes' boards.

The Regulator notes that employers have an important role in ensuring EDI is considered by their schemes, as well as having a duty to support employees who are nominated to their scheme's governing body, which is why it has provided specific guidance for employers.

Guidance on Employer-Related Investments

The Regulator has issued new guidance for trustees and employers about the restrictions on using pension scheme funds for employer-related investments (ERI). The legal position on ERI has not changed. The guidance gives a reminder that, with certain exceptions, no more than 5% of scheme assets may, at any time, be invested in ERI, and no assets may be loaned to the employer. Breaches of these rules are a criminal offence.

Review of TPR

The DWP has appointed Mary Starks to lead a review of the Pensions Regulator, in line with the expectation that public bodies are reviewed each Parliament. Starks was previously Director of Competition and Chief Economist at the Financial Conduct Authority. The review will examine how the Regulator is performing its role and where it can improve, providing greater efficiency and value to taxpayers. It aims to identify efficiency savings of more than five percent where possible. Starks has been asked to aim to deliver the report in May 2023.

Broadening CDC Provision

The DWP has been consulting on extending collective defined contribution (CDC) provision beyond single or connected employer schemes.

As a recap, CDC schemes offer employers a new pension provision option for their employees: the employer benefits from fixed-cost defined contributions, while the members can receive a targeted inflation-linked income payable for life, without having to make complex financial and investment decisions along the way. CDC schemes can also seek greater investment returns through investing in different types of assets; and they can hold these assets over a longer time horizon than savers would otherwise be able to do individually, which leads to better average outcomes for CDC members. Our paper The Dawn of a New (Pensions) Era provides further information.

In August 2022, regulations came into force allowing single and connected employers to seek authorisation to operate their own CDC scheme. The Pensions Regulator recently announced that it had authorised the first CDC scheme — the Royal Mail Collective Pension Plan.

The DWP's latest consultation considers a policy framework for multi-employer CDC whole-life schemes, including master trusts, providing accumulation and decumulation on a collective basis in one package. It discusses the changes that might be required to the existing framework for single and connected employers (including to scheme design and to the key principles that schemes must meet).

The consultation notes considerable interest in the potential for CDC decumulation-only arrangements and how these might help improve member choice and outcomes in the existing DC decumulation market. Such arrangements could provide those approaching retirement with an income product that allows them to share investment and longevity risk. While the DWP recognises the potential benefits of decumulation-only CDC arrangements, it is keen to develop its understanding of how they might work in practice and their implications and risks.

The consultation closed on 27 March. Regulations will be required to extend the existing CDC provisions if applicable following the consultation.

Action

Whether you currently operate a DC scheme, a DB scheme or both, if you would like to get a feel for whether CDC — or decumulation options for your members more generally — could be the right solution for future provision of benefits for your workforce you can access our CDC Quiz here. If you're interested in exploring CDC provision further, or in joining our CDC Interest Group, you can speak to your usual consultant or contact us at CDC.UK@aon.com

News Round-Up

State Pension Age Review

The government has published its second review of State Pension Age (SPA).

Legislation currently brings the rise from 67 to 68 into effect between 2044 and 2046 but, in its 2017 review, the government proposed that this be moved to 2037-2039. However, it has decided to make no changes at this time. Instead, it intends to have a further review within two years of the next Parliament to reconsider the rise to age 68. The government also confirmed that it is committed to the principle of providing 10 years' notice of changes to SPA.

Individuals who reach SPA on or after 6 April 2016 can boost their State Pension by paying voluntary National Insurance (NI) contributions for incomplete years in their NI record. The deadline for making these contributions for tax years 2006/07 to 2015/16 has recently been extended from 5 April 2023 to 31 July 2023. In addition, the planned increase in the rates of voluntary NI contributions has been delayed until August 2023.

WPC Inquiries

The House of Commons' Work and Pensions Committee (WPC) looks into the policies and spending of the DWP, including state pensions and how private pensions are regulated.

Inquiry on Saving for Later Life

The WPC recently completed its inquiry into pension freedoms and the protection of savers, and has published the government's response to its final report. The third and final part of the inquiry was on saving for later life, focusing on what more needs to be done to help people plan and save for their retirement. Amongst other things, the inquiry asked whether households have adequate pension savings for retirement, what advice and guidance people need, and how the government should support self-employed people to save for retirement.

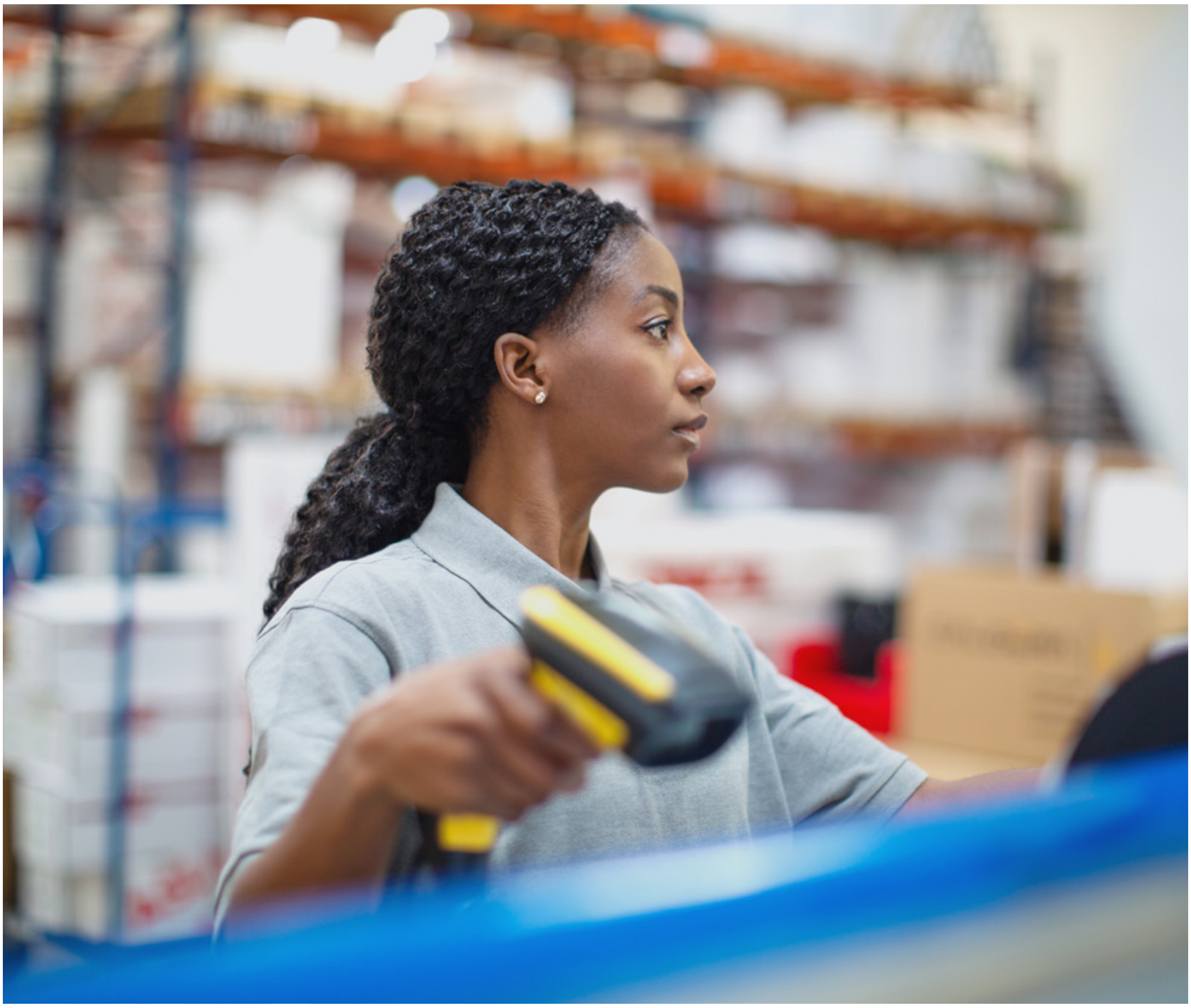
The government disagreed with a number of the WPC's recommendations, such as the call for a new consensus on what an adequate income is in retirement. However, it is working to develop a 'coherent framework for understanding the scale and challenge of the gender pension gap'. The government also said that it remains committed to implementing the 2017 automatic enrolment review reforms in the mid-2020s, although it rejected calls to share a timetable for this (but see page 6 for the Bill that has subsequently been introduced to Parliament).

Inquiry on Future of DB Pension Schemes

A more recent WPC inquiry considers defined benefit (DB) pension schemes, and the challenges and opportunities they pose to members, trustees, employers and the Pensions Regulator. As part of the inquiry, the WPC called for evidence on a broad range of questions, including on whether further steps should be taken to encourage DB scheme consolidation and how scheme surpluses should be treated. The deadline for submissions was 26 April 2023.

PLSA Stewardship and Voting Guidelines 2023

The Pensions and Lifetime Savings Association (PLSA) has published its Stewardship and Voting Guidelines 2023, which are designed to help schemes decide how to exercise their votes at annual general meetings. This year's update takes into account recent political and economic events and circumstances, increased awareness and interest in social issues, how companies should be reporting on climate risk and impact, and the latest gender and diversity standards that investors should take into consideration.



Preparing Data for Buy-In or Buy-Out

The Pensions Administration Standards Association has published guidance on data readiness for a buy-in or buy-out, intended to help trustees and administrators prepare for transactions with insurers. The guide covers: the consequences of holding incomplete and poor-quality data, the key data items that should be held for all members, and the actions trustees can take in advance of buy-in/out to demonstrate good governance.

Living Pension Standard Launched

The Living Wage Foundation has launched its Living Pension employer standard, to tackle low pension saving amongst low-paid workers. With the aim of meeting basic everyday needs in retirement, the standard sets a target of saving at least 12% of a worker's annual salary into a pension, of which the employer pays in at least 7%. The Living Pension accreditation is open to all accredited Living Wage Employers.

On the Horizon

Here are some key future developments affecting pensions:

Spring 2023

- Regulator's single code, to be called the General Code, due to be laid before Parliament

May 2023

- DWP committed to review transfer regulations that were introduced in November 2021

August 2023

- Schemes were due to start connecting to the dashboards ecosystem (exact date depending on scheme size and type), but government says more time is needed

October 2023

- New version of AS TM1 (that sets assumptions for SMPIs) will take effect — to be used for DC benefit statements and illustrations on pensions dashboards
- DC default arrangement disclosure requirements on illiquid assets come into force: chair's statements must disclose default fund asset allocation, and DC default SIPs must explain the trustees' policy on illiquid assets

2023

- Extension of notifiable events framework still awaited
- DWP consultation expected in the autumn on proposals to extend automatic enrolment eligibility and benefits

April 2024

- It is expected that valuations with effective dates from April 2024 will need to comply with the new scheme funding legislation and revised code of practice
- Lifetime allowance to be abolished (lifetime allowance charge ceased in April 2023)
- Low earners in net pay schemes earn top-up payments (payable from 2026/27)

Late 2024

- Subject to consultation in 2023, climate change governance and disclosure requirements may extend to smaller schemes (assets under £1 billion)

Training and Events

Dates currently scheduled for our pensions training seminars are set out below.

All London seminars will take place at The Aon Centre.

For further details, you can find a copy of our training brochure and book online at: www.aon.com/pensionstraining

Please contact us to discuss your training needs: pensionstraining.enquiries@aon.com

Pensions Training Courses	Dates
Defined Benefit — Part 1	14 June (London) 15 August and 16 August (Webinar, a.m.) 31 October (London)
Defined Benefit — Part 2	18 July (London) 12 September and 13 September (Webinar, a.m.) 5 December (London)
Defined Contribution	26 September (London)
Pension Governance Committee	17 May (Webinar, a.m.) 28 November (London, a.m.)

Other Events

Aon participates in a variety of sector-specific conferences and exhibitions as well as holding regular seminars, webinars, conferences and events focusing on key issues of client interest.

To find out more about our events, go here.

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Contact Us

If you have any questions on In Sight, please speak to your usual Aon consultant or contact:

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About

Aon plc (NYSE: AON) exists to shape decisions for the better—to protect and enrich the lives of people around the world. Our colleagues provide our clients in over 120 countries with advice and solutions that give them the clarity and confidence to make better decisions to protect and grow their business.