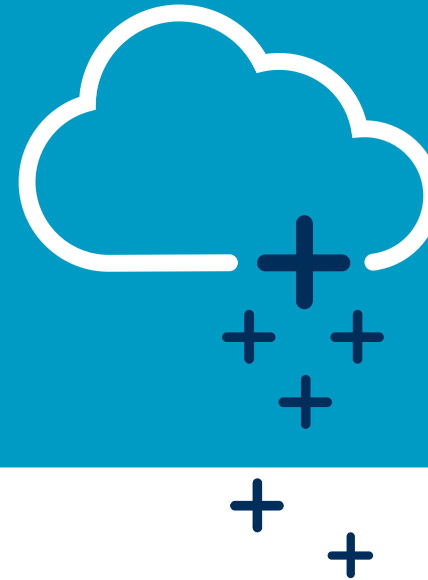
LCP DC update

Welcome to LCP's latest quarterly DC update, in which you will find our views on key developments in the DC arena over the last three months, together with any actions and issues heading your way.

November 2021



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1. Policy developments

Budget announcements confirm (another) consultation into the charge cap and a top-up for net-pay scheme members

In his Autumn Budget, the Chancellor confirmed that the Treasury will launch another consultation to end the 0.75 per cent ceiling on annual management fees on DC schemes, with the hope that relaxing charges on management fees will encourage more DC schemes to invest in illiquid assets, such as infrastructure and renewable energy. Read more about our view here.

The Chancellor also announced that for the tax-year 2024/25 onwards, workers in 'net pay arrangement' schemes will be able to claim a top-up roughly equivalent to the tax relief they would have enjoyed, had they been in a 'relief at source' scheme. The Treasury estimates that this will affect around 1.2m workers, predominantly women, and will benefit them by an average of around £53 per year. Read more on Steve Webb's view that this fix will be "messy, belated and likely to be ineffective" here.

Treasury clarifies the increase to Normal Minimum Pension Age ("NMPA")

The Treasury has also responded to its consultation in February 2021 on how it intends to increase the NMPA from 55 to 57 on 6 April 2028, including the new protections against this increase that it intends to introduce. The draft legislation and accompanying documents have now been published. Little appears to have changed following the consultation, but there are two key new easements relating to the new protection regime, compared to the original policy proposals. You can find out more here.

Policy developments (continued)

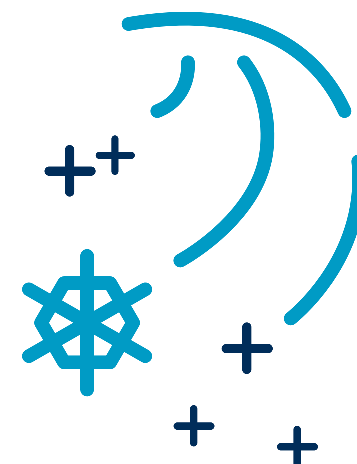
New TPR powers brought into force

Regulations introduced on 1 October by TPR provide it with additional powers over scheme sponsors and other parties, including controversial new criminal offences. A list of the additional powers can be found here.

"Good headway" made on small pots solution

The Small Pots Co-ordination Group (convened in March 2021 by the PLSA and ABI) has launched its first report into solving the small DC pots problem. The success of auto-enrolment has meant that the number of deferred pension pots is likely to increase significantly, with a figure of 27m such pots in Master Trust schemes alone predicted by 2035.

This creates challenges both for members in not only keeping track of legacy pension pots but also ensuring that their value is not defoliated by providers' administrative charges. You can find out more here.



Long-term investment

Government calls on institutional investors to boost the UK's long-term growth

In an open letter to industry, the Government has challenged the UK's institutional investors – and specifically trustees and managers of DB and DC pension funds – to ignite an "Investment Big Bang" by investing a greater proportion of their capital in long-term UK assets.

Alongside this call for engagement, the letter recognises the need for the Government to remove the current obstacles that makes it challenging for DC schemes to make long-term illiquid investments in the UK and flags some of the measures already agreed, including the new Infrastructure Bank, the forthcoming reform to the cap on fees in DC funds, acceleration of pension consolidation options and the UK's first Green Gilt. You can find out more here.

DC schemes encouraged to invest in long-term assets

The Productive Finance Working Group has published a series of recommendations to facilitate greater investment in longer term, less liquid assets by DC schemes.

The Group is advocating this approach because it claims that "One way of potentially achieving higher returns, net of cost, is by investing in longer-term, less liquid assets, managed appropriately and as part of a diversified portfolio". In its report, the Group sets out recommendations in four areas:

1. Shifting the focus to long-term value for DC pension scheme members;
2. Building scale in the DC market;
3. A new approach to liquidity management; and
4. Widening investment in less liquid assets.

This is an ambitious agenda, but with official buy in at the highest levels, it does seem that much of this has the potential to be delivered. Once the barriers are removed we will then need to see to what extent DC schemes are able to change their investment outlook to take on longer-term less liquid assets.

Policy developments (continued)

Invest like a DC scheme with Mark Thompson

In this sixth episode of LCP's "Invest like a..." mini-series we speak to Mark Thompson, investment committee member on numerous DC schemes: the discussion covers topics such as investment philosophy, providing options for a vast DC pension membership base and the structure of a good DC scheme.

FCA finalises rules for value for money in workplace pension schemes and pathway investments

The FCA has published its final rules about how Independent Governance Committees ("IGCs") and Governance Advisory Arrangements ("GAAs") in the group workplace sector (i.e. GPPs and Stakeholder schemes) should compare the value of providers' pension products and services and promote best value for scheme members. This follows its consultation last year about defining value for money and the three key elements to take into account (costs and charges, investment performance and quality of service).

The final rules are largely the same as those outlined in the consultation draft but, following feedback, the rules now allow IGCs some flexibility to determine how best to conduct the costs and charges comparison. The new rules also require IGCs to compare their provider's offerings with similar propositions in the market as part of the assessment. The rules took effect from 4 October 2021 and provider firms and IGCs have until 30 September 2022 to publish their next reports.

FCA and TPR consult on driving further value for money in DC schemes

The FCA and TPR are proposing a new framework through which value for money during the accumulation (or 'growth') phase can be assessed for contract-based or occupational schemes.

The framework requires 'backward-looking' disclosures on investment performance, customer service, scheme oversight (including data and communications) and costs and charges. The intention is that this will allow trustees and governance committees to compare their scheme's costs and charges, investment performance and service standards with similar offerings from other providers – and by doing so assess where their scheme stands on a comparative performance basis.

It is hoped that this will help drive future improvements in value through lower costs and charges, improved risk-adjusted investment performance and higher standards of services.

You can read more here.

Consultation closes on 10 December 2021 and a feedback statement setting out next steps is promised for 2022. The FCA intends to consider the assessment of value for money in DC pensions in the decumulation (or 'de-risking' phase) after it has conducted a post-implementation review of investment pathways.

The "headline" cost of tax relief to the Exchequer increases once more

Statistics published by HMRC for the tax years 2018/19 and 2019/20 reveal that the estimated cost of tax relief on pension contributions is projected to rise over a two year period by £4.4bn to £41.3bn, from the most recent year previously published (2017/18). This continues an upwards trend seen over recent years. The increase is spread across both occupational and personal pension schemes.

Other statistics published by HMRC at the same time show that the highly complex pension tax system is catching more and more people through annual and lifetime allowance charges.

Over £45 billion has been withdrawn from pensions flexibly since the 2015 freedoms were introduced (which must mean a growing number of individuals are becoming subject to the money purchase annual allowance measure). £9.6 billion was withdrawn in 2020 to 2021, a slight decrease year-on-year from £9.8 billion withdrawn throughout 2019 to 2020.

2. Governance updates

TPR publishes its interim response to the Code of Practice re-write consultation

TPR has published an interim response to the consultation on its new 'unifed' Code of Practice. This provides background on the responses received and the steps that need to be taken before issuing the final Code. You can read more about each of the key issues here.

Given the work that will be needed to complete the review of the comments received and make adjustments as necessary, TPR does not expect to lay the new Code before Parliament until Spring 2022, which means that it is unlikely to become effective before Summer 2022. There is also the possibility that some of the content from the Pension Schemes Act 2021 may now also find its way into the first edition of the new Code.

While this means that Trustees can put a Code of Practice review on the backburner for now, we recommend a review is added to the business plans for Quarter 3, or 4 2022 when the new Code is in effect.

3. Climate change - what's new?

FRC publishes the successful signatories to the UK Stewardship Code

The Financial Reporting Council ("FRC") has published a list of the 125 applicants which have successfully met the high standards necessary to be signatories to the UK Stewardship Code. These currently represent c£20 trillion of assets under management, comprising 90 asset managers, 23 asset owners and 12 service providers.

We expect that the high standards that need to be met in order to be included on this list – and the individual feedback provided to those who did not fully meet them at this first assessment – will continue to drive improvements in stewardship across the UK investment industry.

And we are of course delighted to report that LCP made the list!

LCP commits to Net Zero from 2021

LCP has announced that it is committing to becoming operationally Net Zero by 2021, as part of the firm's wider commitment to helping clients, stakeholders and communities build towards a more sustainable future, as well as advancing its own ongoing organisational sustainability. Read more about this here.

Pension scheme voting rights – the Taskforce reports

A report by the Taskforce on Pension Scheme Voting Implementation, which was set up in December 2020 to address problems about the proxy voting by asset managers of equity shares owned by pension schemes, has been published by the DWP.

The 24 recommendations in the report include:

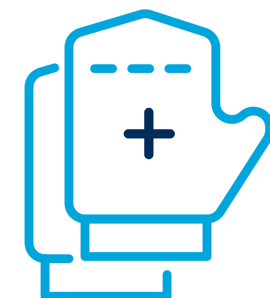
- Trustees should either set a voting policy of their own, or explicitly accept responsibility for those policies exercised on their behalf by their asset managers;
- All asset managers should offer pooled fund investors the opportunity to set an "expression of wish" as to how votes are exercised on their behalf, regardless of how they invest; and
- The FCA should clarify that there is no breach of fund rules in acting on an expression of wish, and set expectations of asset managers for better disclosure of voting policies, more granular and comparable reporting of how votes are cast, and more comprehensive explanations for those votes.

The Taskforce also asks the Government, regulators and industry to sign up to four "Key Principles for Voting", covering expressions of wish, "form over substance" in respect of the nature of relationships, transparency over voting entitlements in products, and co-operation in the voting chain.

SPP launches primer on ESG

The Society of Pension Professionals ("SPP") has published a short and readable Environmental Social and Governance Guide, which is aimed at trustees of small and medium schemes to help them begin to manage ESG integration effectively.

The guide provides step-by-step guidance for trustees on their approach to ESG integration, focusing on how the scheme's investments are held, trustees' legal obligations and a suggested high-level framework for trustees to adopt.



Climate change - what's new? (continued)

MPs call on the Government to show global leadership on pensions and climate change

The results of the Work and Pensions Committee's inquiry into the risks for pension schemes posed by climate change and the role they can play in meeting emission reduction targets have been published, ahead of the COP26 UN Conference in November. The main findings and recommendations of the inquiry launched in April (see Pensions Bulletin 2021/19) are grouped under three headings – reporting standards, scheme governance, and investment and stewardship.

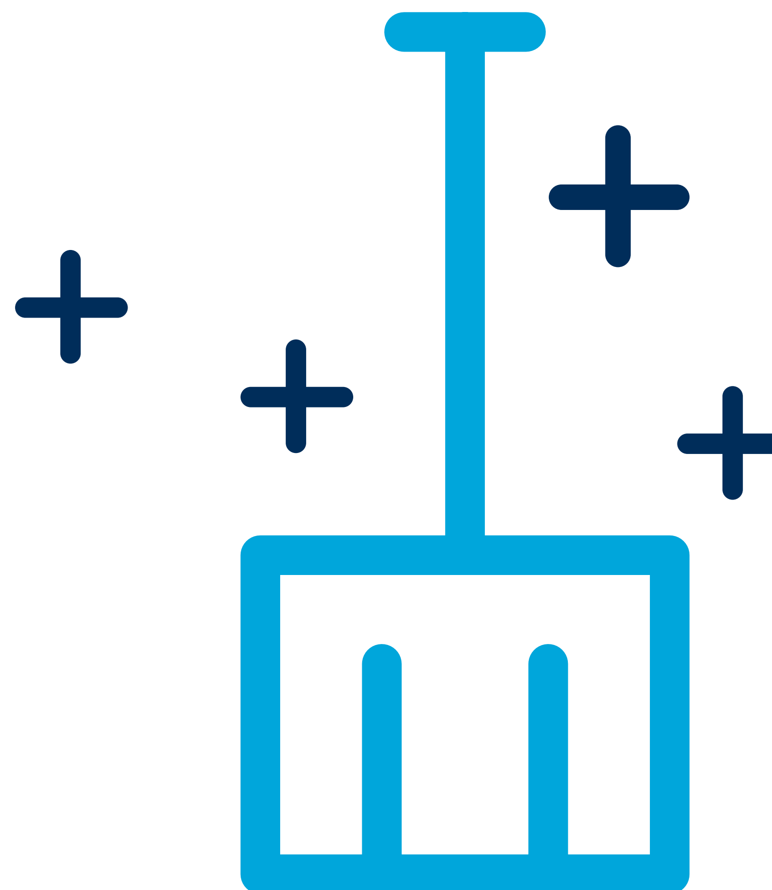
The tip of the iceberg: how UK institutional investors are responding to climate risks

The IPCC's sixth climate change report, published in August 2021, provided a clear statement on the realities and risks of climate change. But what could the Government's policy response to this mean for investors looking to manage risks and fulfil fiduciary duties, and where do the opportunities exist?

In our latest report, we carried out the first ever comprehensive climate risk profiling of a large dataset of UK institutional investors.

LCP climate change insights hub

For more information on climate change visit our hub for insights and actions you can take now to make a difference, drive real change and successfully manage your sustainability challenges. Explore more here.



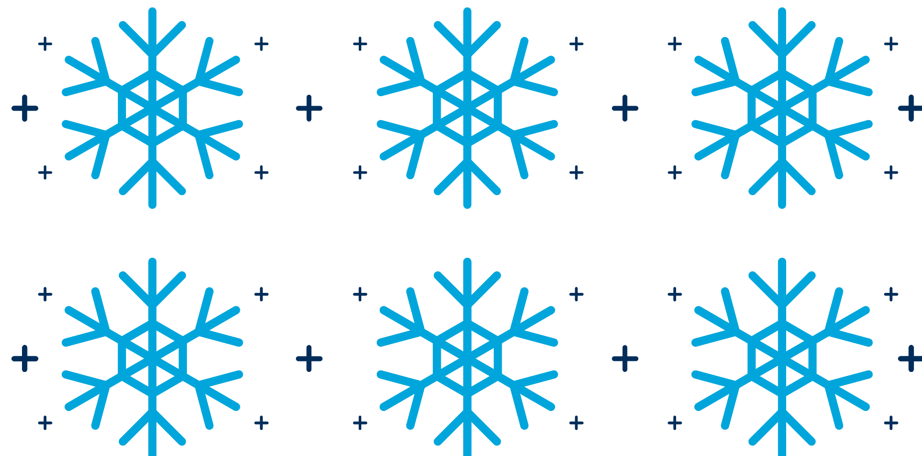
4. Rolling on the river - the right direction but still a way to go for DC

We're pleased to share with you the results of our survey that we ran to help us understand what types of DC scheme and contributions are offered, as well as the aspirations and motivations for the benefits provided. The survey was completed by 150 employers from organisations across a wide range of industry sectors, company sizes and scheme types, to help us establish what the current DC landscape looks like and what employers had to say about their schemes.

We were pleased that the majority (77%) felt it was the employer's responsibility to provide sufficient income for employees to retire. However, nearly one in four (23%) organisations 'disagree' that this is the case. Furthermore, nearly one in two (46%) organisations offer a total contribution that simply meets the legal minimum requirement of 8%. And in one in four (25%) DC schemes, the employer contributes less than the minimum employee contribution. So whilst many schemes are heading in the right direction, it is clear more can be done.

"I'm delighted to see that more than 3 out of 4 employers felt that ensuring their employees have enough to retire was their responsibility, but there is still more that can be done. So, let's take control and help employees get the right retirement outcome that they deserve."

Laura Myers, LCP Partner



Rolling on the river - the right direction but still a way to go for DC schemes (continued)

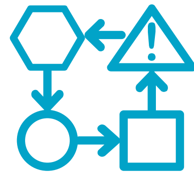
Key findings

49% of organisations do not currently have agreed metrics in place for their DC plan.

49%

Six in ten (60%) organisations make separate options available to newly hired executives and/or high earners.

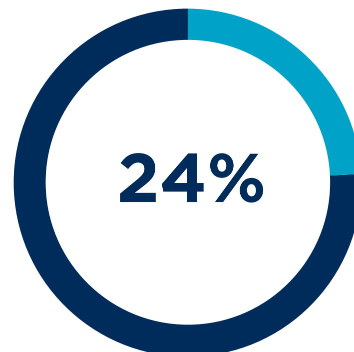
61% of respondents include ESG factors in the design of their DC scheme's default investment strategy (but that leaves nearly than 4 in 10 (39%) who don't).

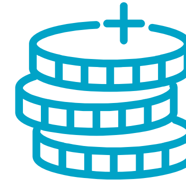


Nearly one in two (48%) organisations have reviewed the design of their DC scheme in the last two years.

48%

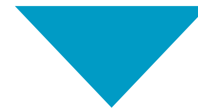
BUT fewer than 24% of organisations have conducted an employee survey in the last two years to seek views.





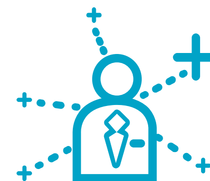
8% of pay

The average maximum employer contribution available.

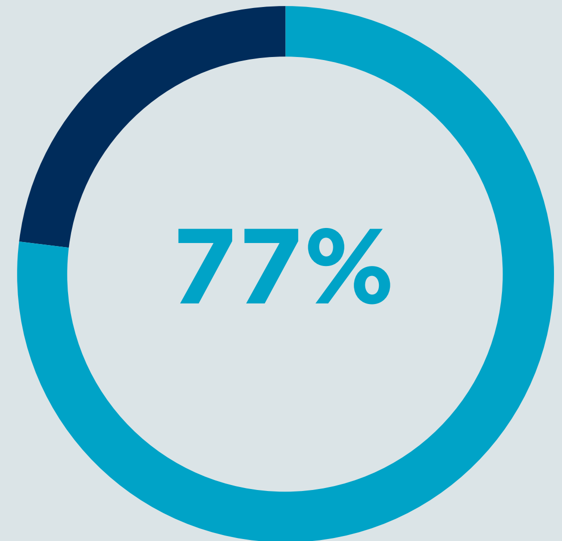


5% of pay

The average amount employees need to pay to receive the maximum contribution.



Over half (52%) supplement the regular communications issued by their scheme's pension provider with **bespoke member communications** at least once a year.



More than three in four of respondents (77%) agreed in varying degrees that it is the employer's responsibility to provide sufficient income for employees to retire.

Rolling on the river - the right direction but still a way to go for DC schemes (continued)

Rolling on the river

The right direction, but still a way to go for DC schemes

LCP DC Pensions report 2021

JUMP TO INTRODUCTION

Read our report to discover more of out the results of our DC survey, what it means for your scheme and practical 'takeaways' to help you take the next steps, click here.

5. Practical guidance

PLSA updates its retirement living standards income levels

The Pensions and Lifetime Savings Association has published an updated version of its "rules of thumb", which are designed to help people understand more about the income they will need in order to lead a certain lifestyle in retirement. This is the first update since they were launched two years ago.

In the main, the standards have been updated to reflect inflation in the intervening period. However, there has also been some reflection of changing attitudes towards retirement lifestyles as a result of the Covid-19 pandemic, most notably more money for eating out, a higher personal grooming budget – and the inclusion of a Netflix subscription.

As before, there are three levels:

1. The minimum living standard ("covers all your needs, with some left over for fun") now requires an income of £10,900 pa (£10,200) for a single person and £16,700 pa (£15,700) for a couple;
2. The moderate living standard ("more financial security and flexibility") now requires an income of £20,800 pa (£20,200) for a single person and £30,600 pa (£29,100) for a couple;
3. The comfortable living standard ("more financial freedom and some luxuries") now requires an income of £33,600 pa (£33,000) for a single person and £49,700 (£47,500) pa for a couple.

Further details are provided by the PLSA here. Get in touch with one of the DC team or your usual LCP contact to understand more about how we can help you analyse your membership against these standards.

DWP consults on stronger nudges to pensions scheme members to seek pension guidance

The DWP has launched a consultation to implement a requirement that trustees ensure that scheme members are referred to "appropriate pensions guidance" and have either received or opted out of receiving it, where they are proposing to access or transfer their DC benefits. You can read more about what is included in the DWP's proposals here (the FCA's proposed rules for workplace schemes should be finalised by the end of the year).

6. Pension scams

Pension scams – Government responds to MPs' concerns

The Government has responded to the Work and Pensions Committee's call for "quick and decisive" action on pension scams with an explanation of the significant activity by Government and various bodies on this issue in recent years and an indication of what is likely to happen next.

The Committee has focused on online scams, criticising the Government's apparent "ambivalence to major sources of harm", in response to what now seems to be its firm decision not to include fraud facilitated through paid-for advertising (eg via adverts on search engines) in the Online Safety Bill. The Government promises instead a consultation later this year, by the Department for Digital, Culture, Media and Sport, on how to tackle harmful or misleading online advertising that can enable online fraud. You can read more about this here.

Whilst the cold-calling ban in itself appears to have been a success, the scammers' communication methods have simply evolved, with online advertising now being a major 'route to market'. Action is needed here, but at present , whilst the problem is acknowledged, there is no firm timescale within which to tackle it.

FCA urges potential scam victims to 'flip the context'

The FCA is urging pension savers to assess pension offers made online in the same way they would if they were approached in person in an everyday setting such as a trip to the shops or an afternoon in the pub.

In this context 'flipping' is being suggested as a result of research commissioned by the FCA from which it is reported that pension savers were:

1. Nine times more likely to accept advice from someone online than they would from a stranger met in person; and
2. Five times as likely to be interested in a free pension review from a stranger online than someone in their local pub.

The FCA also reports that in the first five months of 2021 nearly £2,250,000 has been reportedly lost to pension scams – a figure reported to Action Fraud – with the total amount lost likely to be much higher due to reluctance to report, or not realising a scam has taken place until potentially years later.

This concept is a useful one that could be repeated by pension schemes in their member communications. It is also a demonstration of how worried the FCA is about pension scams being conducted online. However, as we know from experience over recent years, it is regulatory action that is needed, which is often years in the making.

New pension anti-scam laws: the burden on trustees will only increase

Whilst the final form of the new anti-scams legislation for pension transfers is awaited, and is not expected until late 2021, administrators are currently (or at least, they should be!) working their way through the draft proposals and considering what changes will be needed to their processes and procedures.

Whilst there is a clear risk that this legislation will apply with very little notice, doing nothing for now is not an option. Read more about this here.

7. LCP Insight

Never the twain...

In this latest edition of our 'mini-series' of blogs on current issues facing defined DC contribution schemes, with Rebecca McKay from Trowers & Hamlins, we look at how DC members might be missing a trick when it comes to flexible retirement planning, and what their schemes can do to help.

How getting pension freedoms wrong could cost your benefit

The greater freedom around accessing pensions introduced in 2015 have been hugely popular. In the last two years alone, more than a million people aged 55 or above have accessed a pension pot in a wide variety of ways, commonly taking the full amount in cash or going into a flexible drawdown arrangement. But there has so far been very little focus on how these pension withdrawals may interact with the means-tested benefits system. Read more here.

Pension inequality a major issue when couples divorce

A new report from the University of Manchester and the Pensions Policy Institute has found that, within couples, men have substantially more private pension wealth than women, which poses particular challenges if they divorce.

The data also showed that while around 90% of couples have some pension wealth between them, in about half of couples with pensions, one partner has more than 90% of the pension wealth. Fewer than 15% of couples have pensions that are approximately equal.

The issue here is not so much the pension inequality, but that divorcing couples often fail to take into account their pension wealth when dividing their money and property, despite a long-standing mechanism that is available for them to do so. The report is accompanied by a particularly useful video which it is hoped will help divorcing couples understand the legal context for pension sharing.

LCP CARES awards

On 9 December we will be holding our 5th annual LCP CARES awards, which is our peer-to-peer recognition for those who have gone the extra mile for clients, colleagues or the wider community.

We are inviting you to help us. If you've experienced incredible service from someone at LCP over the last year, we'd love to hear about it. Whether they've made a difference to your strategic goals or just done something small to make your day better, please let us know.

You can nominate the LCP individuals (or teams) that you feel deserve an award for 'Exceptional Client Service', regardless of job title by clicking here to access our nomination form.

Stephen Budge promoted to Partner

We are pleased to announce that Stephen Budge has been promoted to Partner. Stephen joined LCP's DC team last year, bringing with him over 20 years' experience in advising clients on a variety of DC issues. He has a wealth of experience advising large DC client and Master Trusts and is the lead advisor on a number of our largest DC clients. Congratulations Stephen.

LCP named Employee Benefits and Actuarial Consultants of the Year

LCP has been crowned the winner in two categories at this year's Pension and Investment Awards (PIPA,) being recognised for its actions as a firm during the pandemic. The judges named LCP Actuarial Consultants of the year, saying that "Strong performance and Covid-related measures won the judging panel over, with LCP's consideration for colleague and client wellbeing helping it outperform the other entries in the category."

In the Employee Benefits arena, the judges said that the company's "examples of innovative activity" had made a difference in improving LCP's offering. Find out more here.

Annual conference

We are excited to invite you to LCP's first ever hybrid annual pensions conference on Thursday 25 November. This year we take a deep dive under the waves of the current regulatory changes which affect all those connected with pension schemes – trustees, sponsors and administrators.

We're looking forward to sharing our thoughts, ideas and experiences on everything pensions-related. We'll cover hot topics such as the current regulatory changes, Net Zero and strategic journey planning. We'll also be busting some myths on what you think you know about governance.

For further information on the agenda, timings and how to register, click here.

Do you enjoy hearing from our experts?

It's important to us that we deliver what you want, and don't clog up your inbox with things you don't.

Please take a moment to let us know your preferences; in return we will try our best to only send you the things that matter to you.

For further details, visit our preference centre.

Any questions?

If you would like any assistance or further information on the contents of this Update, please contact one of the team below.

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