LCP INSIGHT CLARITY ADVICE

Pensions action plan for companies

Managing the impact of Covid-19

Updated for The Pensions Regulator (TPR) latest guidance
30 March 2020

We appreciate that our corporate clients have a lot on their plate – which is why we have produced this quick action plan to help you prioritise what you need to do in relation to your company pension arrangements:

Ensuring business continuity

Ensuring business continuity - Make sure pensions continue to be paid and that your pension providers, advisors and trustees have robust plans to ensure continuity. Employers looking to furlough employees will need to think through the pensions implications.

Quantifying financial impact

Quantify financial impact - Defined Benefit (DB) plans are likely to have been negatively impacted. Those with lower interest rate hedging and material equity holdings will have been hit the hardest. This is likely to impact immediate trustee behaviour, especially if Covid-19 also has a negative long-term impact on your business. This may play out during your current or next funding valuation, or trustees may seek additional contributions, security, or to reduce risk, sooner. Note the short term flexibilities potentially available and without attracting regulatory action following the Pensions Regulator guidance on 27 March 2020. In extreme cases, some companies may want to explore if they can cease/reduce contributions immediately to help the business survive. It is also worth considering whether contingency plan triggers which may be in place are likely to be hit over the coming months.

Take investment opportunities

Take investment opportunities – After a period of substantial de-risking for many DB plans, with growth assets potentially looking cheaper, companies may wish to proactively discuss investment risks and opportunities with their trustees. New hedging opportunities may also be available given large changes in available yields.

Help employees understand impacts

Help employees understand impacts - Those with Defined Contribution (DC) pots are likely to have seen significant falls and may be very concerned that this will drastically impact their future retirement. DB members are likely to feel more 'protected' from market falls but may worry about the financial health of the plan or the sponsoring company, and may wish to explore taking a transfer value. The Pensions Regulator has now said that Trustees can suspend transfer values for 3 months, and communications with members should help raise their awareness of scams.

The situation is fluid and will continue to develop further over coming weeks. We hope these suggested actions keep you focused on critical tasks, which will help the situation both for you and your pension plan. For further details of what the implications could be, please contact the partner who normally advises you.

Ensuring business continuity

Area	*Action*	*Done?*
Providers/advisers continuity	• Ensure pension providers, advisors and the trustees (and their advisors – especially pensions administration) have robust business continuity plans in place and can continue to work, invest DC contributions, and pay pensions, including from their homes.	
Internal team	• Make sure pensions manager/other internal team have business continuity plans, including being able to work from home. If there are likely to be redundancies or furloughing, ensure adequate continuity for key roles and consider any pensions implications.	
Engage with trustees	• Keep trustees abreast of the impact Covid-19 is having on business operations and outlook. Trustees are being advised to consider the impact on companies, so be prepared for this question. Promptly provide information that the trustees reasonably request. The Pensions Regulator has highlighted the importance of companies documenting the rationale for decisions made and demonstrating that any potential impact on the pensions scheme was considered.	
Transactions	• If you are currently in or entering into a business transaction, carefully consider DB pension aspects, as the current position may be very different from historic pension figures provided. A negative change in the sponsor (seller or buyer) may alter how the trustees will view the transaction, and could trigger regulatory concerns.	
Pension exercises eg member options, closure to accrual, pension consultations	• Consider stepping back to consider current financial implications. • Members are unlikely to want to engage in consultations/exercises, so consider deferring those that require member engagement. • Having said that, for some DB plans that are open to future accrual, the current financial and business impact may mean that closure to accrual should be considered quicker, and in some cases urgently. • If this fits with your employee strategy, encourage trustees to communicate retirement options to members, so members are aware when and how they can access these. • Consider appointing a financial adviser to help members make retirement and transfer decisions, and reduce the risks of them being victims of scams or making poor decisions in stressful times.	

Keep trustees abreast of the impact Covid-19 is having on business operations and outlook. Trustees are being advised to consider the impact on companies, so be prepared for this question.

Quantifying financial impact

Area	*Action*	*Done?*
Impact on DB plan deficit/ funding level	• Keep abreast of your funding position. Conditions remain volatile and you will want to ensure you have the most accurate information available. Online tools such as LCP Visualise can provide the latest funding and accounting positions. • Trustees may have concerns if the funding level has fallen significantly or if the company's financial strength/outlook (called covenant) is negatively impacted. Engage with the trustees proactively and provide them with information they reasonably request. • If you are currently mid-valuation process (eg if valuation date was at the end of 2019) or it's during 2020, then your need to engage and take action to agree an appropriate response will be more of a priority. In some cases this may lead to companies looking to reduce current cash contributions or to defer valuation discussions until later in the year. • The Pensions Regulator has emphasized that post valuation experience does not need to be reflected by Trustees. • Consider if there are any forms of alternative covenant support that you could provide trustees – eg contingent assets such as parent guarantee, charge over a property or cash in an escrow etc. This may help them to become less risk averse in other areas.	
Developments in funding requirements	• Look out for communications from the Pensions Regulator about pension scheme funding in the current environment, including the upcoming 2020 Annual Funding Statement. The Pensions Regulator guidance gave some breathing space to employers who need it for example via a 3 month contribution deferral or a 3 month extension to the period for agreeing ongoing valuations. • Consider the impact of, and consider responding to, the Pensions Regulator's ongoing consultation on a new tougher funding regime.	
Cashflow to DB plan	• In more extreme cases, some companies may need to consider whether seeking a contribution reduction/holiday would be helpful (the Pensions Regulator saying that up to 3 months where appropriate will not attract any regulatory action) – this may be possible in some circumstances, particularly if liquidity constraints are threatening short term business viability. • If so, you will need to engage appropriately with trustees, consider other aspects of the business (eg dividends would normally need to be reduced or to stop) and whether you need to involve the Pensions Regulator. • It may be easier to do this if other non-cash protections are provided to the DB plan such as charge over a property or other contingent assets. • Consider whether any contingency plans agreed with the trustees might trigger, eg due to a credit rating downgrade. • Existing regulatory requirements, along with new requirements in the Pension Schemes Bill, mean that companies will need to tread carefully in this area to ensure 'contribution notice' triggers are not breached.	
Accounting for DB plan	• Monitor your pension accounting position. There is likely to have been a material balance sheet impact. As corporate bond spreads have widened, the impact is likely to be less than for funding, and in many cases may be positive. For some companies, this should be kept under review for banking covenants and distributable reserve monitoring. • If your year end is March or June, consider accounting options available to mitigate the impact of falling asset values (eg using LCP's Treasury discount rate).	
Mortality assumptions	• Current assumptions will be based on data before Covid-19 became a pandemic. Looking ahead, consider whether a change in assumptions would be material to your funding or accounting positions.	
The DC default investment strategy	• Keep an eye on how the default investment strategy has done. This will be where most employees are invested and will be experiencing returns. • Ask the trustees or your provider for updates on risk and return of the strategies to check that the lifestyling has helped protect employees closer to retirement.	

Take investment opportunities

Area	Action	Done?
Liquidity	• Ensure arrangements for creating liquidity to make sure pension payments remain robust. • Discuss with trustees any challenges that might arise from less liquid assets in the portfolio, eg the possibility of frozen property funds.	
Risk	• Assess whether the level of risk in the investments remains appropriate given changes in the funding position of the DB Plan and changes in the company's business. Eg could the business weather a further downturn and, if not, is some de-risking advisable?	
Insurance opportunities	• Understand how market movements will have impacted insurer pricing. Widening credit spreads may make buy-in and buy-out pricing appear more attractive for schemes holding low risk assets.	
Rebalancing	• Trustees are likely to need some support to respond quickly and decisively. Fund managers may not rebalance automatically so it will be important to agree a pragmatic approach. Not rebalancing at all is likely to mean asset allocation drifts away from strategic target. • Consider phasing any agreed re-risking switches given ongoing volatility. • Any planned asset transfers and/or triggers should be reviewed to determine if they continue to be appropriate or whether better to hold off or reset.	
Hedging & collateral	• Consider the current hedging strategy and collateral position. It may be advisable for the trustees to retain higher cash buffers given increased volatility. • Test whether other non-cash collateral assets remain sufficiently liquid and if not consider discussing mitigating action now with your trustees so your pension plan isn't a forced seller at the wrong time. • Investigate opportunities that may arise from volatility in yields and inflation expectations, to lock-in hedging at better levels. Discuss with and make proposals to the trustees as appropriate.	
New opportunities	• Evaluate with trustees/advisers the best opportunities that have been (or will be) created by the market disruption, and any changes in their long-term return expectations going forward. • Ensure your plan can take advantage as opportunities arise. Keep a fluid and open dialogue with trustees, any investment sub-committee and its advisers. Do the fund managers have sufficient flexibility to move quickly? • Don't just focus on the equity markets as the financial press tends to. Also consider credit markets, which may be more important for your plan and may present more compelling opportunities. • Complexity and illiquidity are not necessarily your enemy. You may also wish to explore with trustees dedicated 'opportunistic' funds. These may charge high fees and lock-in investors for multiple years, but may be best positioned to produce high risk-adjusted returns during periods of financial uncertainty.	

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Help employees understand impacts

Area	*Action*	*Done?*
Defined Contribution	• If you have furloughed employees under the Government scheme, minimum automatic enrolment employer pension contributions can be claimed on the wage covered by the scheme. This contribution level (3% of Qualifying Earnings) is likely to be less than many employers pay into their defined contribution pension scheme. If you are thinking about reducing pension contributions down to the minimum automatic enrolment levels you will need to seek legal advice, as there is a requirement to consult with employees for this type of change. In reducing to 3%, you may need employees to increase their contributions in order to meet AE total minimum requirements. You should consider the messaging of this change in the context of furloughing. • Members who are closer to retirement will be concerned about the possible impact on their ability to retire due to their savings having been hit. Consider working with trustees/providers to communicate to employees to help them understand that 'lifestyling' is likely to have helped, that there may be no need to immediately purchase an annuity, and point them to where they can get further information. • Members who are further from retirement may also be concerned about market falls. Care must be taken not to give advice, but communications can be considered that provide appropriate and reassuring messages about pensions being for the long term. • Higher earners may have other issues to manage depending on size of pot, any historic DB savings, and Annual Allowance thresholds. Engagement with key individuals may be helpful. Targeted communications could be provided to this group. • Ask the trustees or your provider for the opportunity to review any communications they are issuing.	
Defined Benefit	• Current working conditions may have an impact on staff retention and their retirement plans. This may be a helpful time to communicate the options available to DB members from age 55. This may support companies seeking to encourage part-time working requests and early retirements as part of their workforce planning. • Members may become more concerned about the strength of the 'guarantee' provided by the company. Expect more questions in this area. Having a response prepared may be useful, even if this is not something that is actively communicated to everyone. • Possibly driven by this concern, members may seek advice from other sources. They may be encouraged to transfer out at a time when DB valuations will be high and stock markets are low, which may or may not be in their best interest. Encourage trustees to step up scam awareness communications to safeguard employees' savings. Work with trustees to appoint a financial adviser to help members where appropriate. • Ask the trustees for the opportunity to review any communications they are issuing. The Pensions Regulator has issued warnings around pensions scams, and has stated that Trustees can suspend transfer values for 3 months.	

Want to find out more?

If you would like further information, please visit our Corporate Consulting team or contact one of the people below.

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