TUC

trustee network

member trustee news

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TPR consults on updated guidance on DB funding

The Pensions Regulator published for consultation (which closed on 7 Feb) a package of documents on the funding of defined benefit schemes, including a draft revised code of practice and a draft regulatory strategy. The new code of practice is expected to be in force by July 2014; schemes completing valuations before then are encouraged to bear in mind the messages in the revised code.

TPR's press release billed the package as "striking a balance between sponsoring employers' pension funding obligations and their ability to invest in sustainable business growth". The consultation sets out how the Regulator intends to balance its new objective (contained in the Pensions Bill 2013) to minimise the impact on an employers' sustainable growth, with its existing DB funding objectives.

Welcome

More than 90 people attended the TUC's Member Trustee Network Conference in November, with, as always, very positive feedback. Comments from attendees included, "I thought that the breakout sessions were of a very good standard this year" and "Enjoyed in particular the work done by Hilary Salt and Con Keating". There's more on the conference on p7.

Many of the themes for 2014 look to be the same that made 2013 such a busy year: a consultation from TPR on DB funding; continued work on auto-enrolment; a focus on stewardship, and increasing concern as to whether DC schemes are fit for purpose. And 2014 may be the year when the decumulation stage of DC pensions finally gets the attention it deserves.

Both the industry and the minister have been expressing doubts as to whether the annuities market works properly, or indeed if annuities remain the appropriate way of turning pension savings into retirement income. Even without auto-enrolment, the number of those with DC pensions reaching retirement age is set to grow rapidly, following the trend to close DB schemes from the 1990s onwards, and it's doubtful that the market, as currently constituted, will provide good value to many of those with small or medium pots. Let's hope for some genuinely new thinking on this issue.

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The content of the consultation also reflects how TPR's approach to DB funding has evolved over the last eight years in light of its experience in managing the risks in DB schemes.

The consultation includes a revised draft funding code of practice that provides practical guidance to help pension trustees meet the requirements of scheme funding legislation, together with a draft regulatory strategy and funding policy setting out the Regulator's approach. Stephen Soper, the Regulator's interim chief executive, said, "Investing in sustainable business growth is central to being able to provide a long-term future for any business and its pension plan. The best support for a DB pension is a strong employer and effective trustees working together to manage and balance the risks to their business and scheme. Our revised code of practice emphasises the importance of pension trustees and employers working collaboratively to establish viable, long-term funding plans. We place a strong focus on education and enablement to help schemes to achieve appropriate outcomes. The needs of employers and schemes can be reconciled in the vast majority of cases through good working relationships without the need for our involvement."

The code proposes that trustees must balance the need to act in the interests of their members with the needs of the sponsoring employer. In particular the draft code sets out the need to allow the employer to invest in the growth of their business so that long-term support to the scheme can be provided, but any funding shortfall (on an appropriate funding target) should be paid off as "quickly as the employer can reasonably afford".

The code also requires trustees to adopt an integrated approach to risk management with regard to scheme funding, with the risks faced by schemes falling broadly into three main areas: employer covenant, investment and funding. Trustees should understand and manage these risks and be "comfortable with the extent to which they can be underwritten by the employer over an appropriate period of time".

TPR intends to drop its current funding 'triggers', such as the length of a recovery plan, for investigation of particular schemes and to replace them with a 'suite of risk indicators'. These will include an assessment of the scheme's funding position against a 'Balanced Funding Outcome' (BFO) indicator, appropriate to the covenant strength and scheme maturity.

Once the code has come into effect, TPR intends to produce further guidance and to update its Trustee Toolkit.

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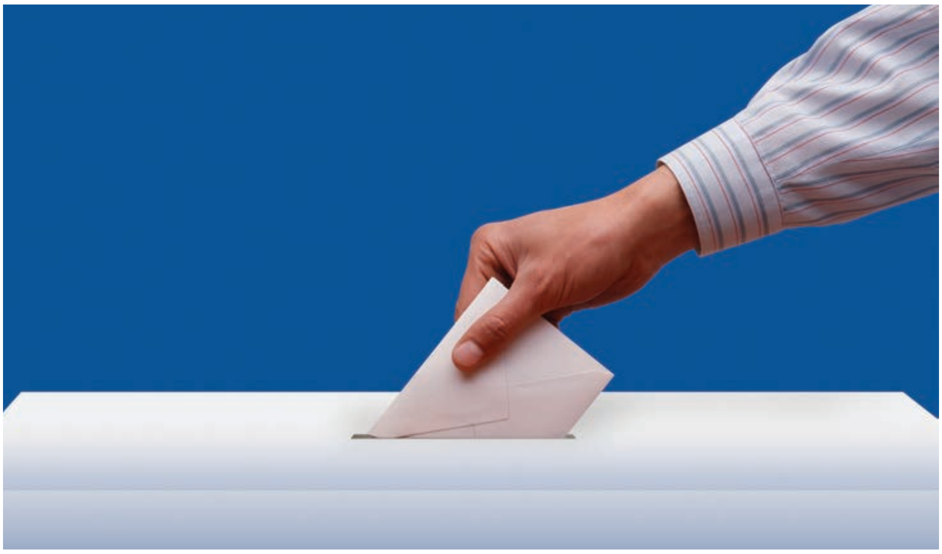
Stewardship update



The TUC's eleventh annual Fund Manager Voting Survey, published in November, showed that pay remained the biggest focus for investor concern. The survey includes many of the key votes that occurred during the so called 'shareholder spring' of 2012. There is evidence that some asset managers were more willing to vote against management over remuneration issues last year. There was also an overall reduction in the proportion of abstentions. However, "oppose" votes increased, suggesting a tougher approach on the part of some investors. Many asset managers continued to support managers on most issues most of the time. At one end of the spectrum, two respondents voted in favour of more than 85 per cent of management resolutions.

There is also possible evidence that overseas ownership of UK companies is affecting shareholder voting patterns. Barclays' remuneration report was opposed by the large majority of survey respondents, who include most of the UK's major institutional investors. Yet the company won the vote relatively easily at its AGM. This might suggest that the votes of overseas shareholders were a significant factor.

Almost all respondents now disclose some level of voting data. However, there continue to be variations in the nature of disclosure that make comparative analysis difficult. For example, some investors only disclose votes against and abstentions, which is a long way from providing a clear picture of what goes on at company AGMs.

TUC General Secretary Frances O'Grady said: "For corporate Britain to be more accountable, more needs to be known about the way investors vote. Shareholders need to be prepared to challenge proposals from the boardroom more frequently. Shareholders who fail to make use of their voting and engagement rights fuel the argument for other stakeholders to play a role in corporate governance. Clients need to know that their fund managers are using their investments in a way that reflects their wishes and that's difficult if it's hard finding out what they are up to."

The call for more transparency was echoed by the Financial Reporting Council (FRC) in their annual review of the Corporate Governance and Stewardship Codes. The FRC found that there has been an uptake in signatories to the Stewardship Code – now standing at almost 300 – with signs of better engagement with large companies by investment managers. Baroness Hogg, FRC Chairman said: "Companies and investors need to demonstrate that there is substance behind their statements of good intent. Investors need to aspire to the same level of transparency as they themselves expect of the companies in which they invest. Many statements on the Stewardship Code give little insight into investors' actual practices." The FRC is considering mechanisms for ensuring that statements are complete and up to date, and possible sanctions if they are not.

A new report from ShareAction (formerly FairPensions) makes the case for greater communication and consultation with scheme members about stewardship activity. The report, *Our Money, Our Business*, funded by the Nuffield Foundation, is accompanied by a best-practice guide. This highlights the UK schemes that are leading the way, including the Environment Agency Pension Fund's Responsible Investment Review and the Pensions Trust's member survey on ethical investment. The report and guide can both be found on the ShareAction website **http://www.shareaction.org/our-money-our-business**

In other work on corporate governance, the TUC has published two research reports on workers on the board, including the European experience of worker involvement in corporate governance. Both can be found on the TUC website at **http://www.tuc.org.uk/economic-issues/corporate-governance/workers-company-boards-makes-sound-economic-sense-says-tuc**

Trustees' investment duties under consultation

In follow up action to the Kay review on the workings of the UK equity markets, published in summer 2012, the Law Commission has been consulting on the Fiduciary Duties of Investment Intermediaries, seeking views on whether it is a trustee's duty to take into account ethical factors when making investment decisions. Trustees are under a statutory duty to exercise investment powers in the best interests of scheme beneficiaries. The concern was whether the law is unclear as to whether this requires trustees to maximise financial return over a short timescale and to what extent trustees should consider the environmental and social consequences of their decisions. The Commission's consultation paper asked:

- Is the law right to allow trustees to consider ethical issues only in limited circumstances?
- Are the legal obligations on trustees conducive to investment strategies in the best interests of the ultimate beneficiaries? And if not, what specifically needs to be changed?

For contract-based pensions and others in the investment chain such as fund managers, fiduciary duties are much less certain. The consultation asked:

- Should the duties on contract-based pension providers to act in the interests of members be clarified and strengthened?
- Should pension providers be duty-bound to review the suitability of investment strategies over time? And if so, how often should they do this?
- Does the regulation of investment consultants and custodians need to be reviewed?

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The Law Commission's "tentative view" is that the legal duties placed on trustees to act in the best interests of beneficiaries are satisfactory, but considered that duties placed on providers of workplace contract-based pensions are "unduly uncertain". The paper also notes a number of pressures on trustees which discourage long-term investment strategies (such as the statutory funding objective and the need to show any deficit in an employer's accounts).

The Commission proposes to issue its report with recommendations to the government by June 2014. The consultation document can be found at **http://lawcommission.justice.gov.uk/consultations/fiduciary_duties.htm.**

In other follow-up action to the Kay review, an Investor Forum for Collective Engagement is to be set up, to increase engagement between companies and investors. The forum is to be operational by June 2014 and will also invite foreign investors, such as sovereign wealth funds, to participate in 'engagement action groups'. The forum is supported by NAPF, the Association of British Insurers and the Investment Management Association.

DC code of practice now in force

TPR's new Code of Practice on DC arrangements came into effect in late November. The Code applies to all trust-based DC arrangements, including money purchase AVC arrangements in DB schemes. Trustees also need to be aware of Code of Practice 5, covering the late payment of contributions. This was revised in September 2013 to include a number of new requirements, such as requiring trustees to check and reconcile the amounts received and invested using a risk-based process.

Andrew Warwick-Thompson, TPR DC director, said: "From today, we expect DC trustees to assess their scheme against the standards set out in the DC code. Our aim is to protect retirement savers and to ensure their money is invested in good quality schemes that are well-run in the members' best interests. Schemes that fall short of these standards may incur enforcement action."

Trustees will need to make time to assess their scheme against the new requirements. The output should ideally be a 'comply or explain' governance statement, which should be made available to members and employers, e.g. as part of the annual report and accounts. TPR has published a template statement for trustees to use. Areas for review will include the following:

- strategic review of the value for money provided by their scheme – a model process is set out for doing so, which involves collecting and analysing information about all types of costs and benefits of scheme membership and then benchmarking against other similar schemes
- retirement processes, including what assistance or advice is available to members
- investment objectives (including for AVC arrangements) should be documented in the Statement of Investment Principles (SIP)
- review of the protection available to members including in relation to third party providers
- arrangements for prompt investment of contributions and other processes, e.g. switches.

The new Code and associated guidance can be found on the TPR website at **http://www.thepensionsregulator.gov.uk/dc-pensions.aspx**

Further pressure on trustees has come from the Financial Services Consumer Panel which has urged the Financial Conduct Authority to create requirements for employers and trustees of workplace schemes to provide non-advice annuity services for members. This would include enhanced annuity quotations, ensuring product suitability, and explaining clearly the fee and commission practices across the market. The paper also urges government to reform the tax rules on small pots and to introduce a national default annuities service with a similar public service obligation as applies to NEST.

TUC welcomes DWP consultation paper on defined ambition pensions

The TUC broadly welcomed the consultation paper on defined ambition pensions, *Reshaping Workplace Pensions for Future Generations,* published by the DWP in November.

TUC Head of Campaigns and Communications, Nigel Stanley, emphasised the need for improvements in DC schemes: “In particular we think that sharing risk between members in well-governed and large-scale collective DC schemes can make members’ savings work harder and deliver better retirement income. Getting scale and member-aligned governance will require government to take a strong lead as this will represent a real challenge to the many existing schemes run for profit”. But the TUC remains sceptical that deregulating DB pensions will change employer behaviour. It is particularly opposed to abolishing indexation as that just means pensioners getting poorer every year.

Nigel Stanley explored the issues further in a ToUChstone blog posting here: **http://touchstoneblog.org.uk/2013/11/defining-our-pension-ambitions**

Slides from the TUC’s Member Trustee Network Conference workshop on the topic of defined ambitions can be found on the TUC website.

Auto-enrolment update

A new report *VfM: Assessing value for money in defined contribution default funds* from the Pensions Institute of Cass Business School, sets out recommendations to ensure member-VfM does not suffer as a result of market forces. The report found that while cheapest is not necessarily best, there is no link between the cost of membership and member outcomes: higher charges are not linked to potential outperformance. The report can be found at **http://www.pensions-institute.org/reports.html**. The TUC supports a cap on DC charges.

Research sponsored by NEST has found that the recession may have encouraged a trend to greater personal responsibility for planning for retirement. The survey found a shift in attitudes that has affected how people manage their money day-to-day and how they think about their future. Fewer people are confident about what they have set aside for retirement compared with two years ago and a large majority are worried that they won’t have enough. Sixty-one per cent of people agree that it is a good idea for people to be enrolled into a workplace pension scheme. Those enrolled who had not opted out mostly gave a positive reason – that it was time to start saving for retirement, or that it made financial sense because the employer contributes. Only 13 per cent said they were too busy to opt out.

Commenting on the findings, TUC General Secretary Frances O’Grady said: “This is further evidence that auto-enrolment is turning out to be a huge policy success. Opt-out rates look set to remain lower than expected even as it spreads to smaller employers. And with growing evidence that people’s attitudes have been permanently shifted by the crash, the time is right to start a debate on how best to increase contributions to ensure that the new system delivers decent retirement incomes.”

More than two million workers have begun saving into a workplace pensions scheme as a result of auto-enrolment, according to figures released in mid December. So far more than 3,500 employers have signed up. This year will see a leap in the number of firms involved, with tens of thousands of medium-sized employers reaching their staging date. There is updated guidance for trustees on their auto-enrolment duties on TPR’s website at **http://www.thepensionsregulator.gov.uk/trustees/automatic-enrolment-the-role-of-trustees.aspx**

However, the TUC has reacted with dismay to the announcement in December that the salary threshold for auto-enrolment is to be raised to £10,000, pointing out that this will mean that most part-time workers, whose average salary (according to figures from the ONS) is under £9,000, will be excluded.

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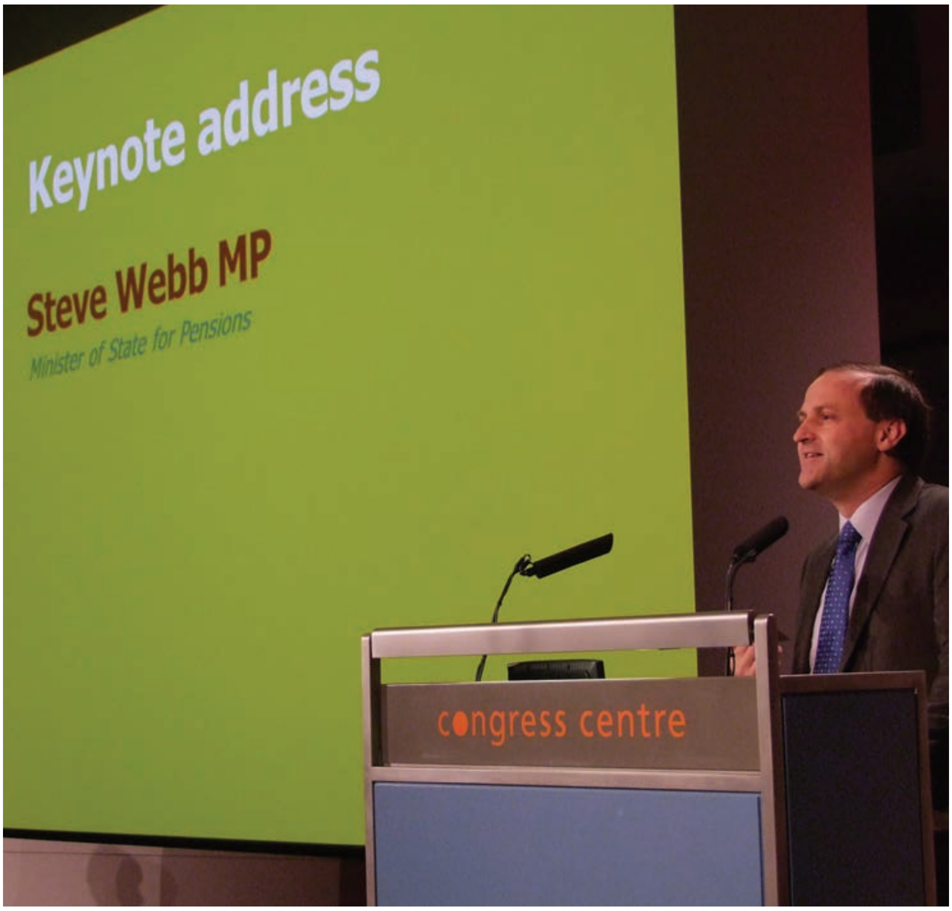

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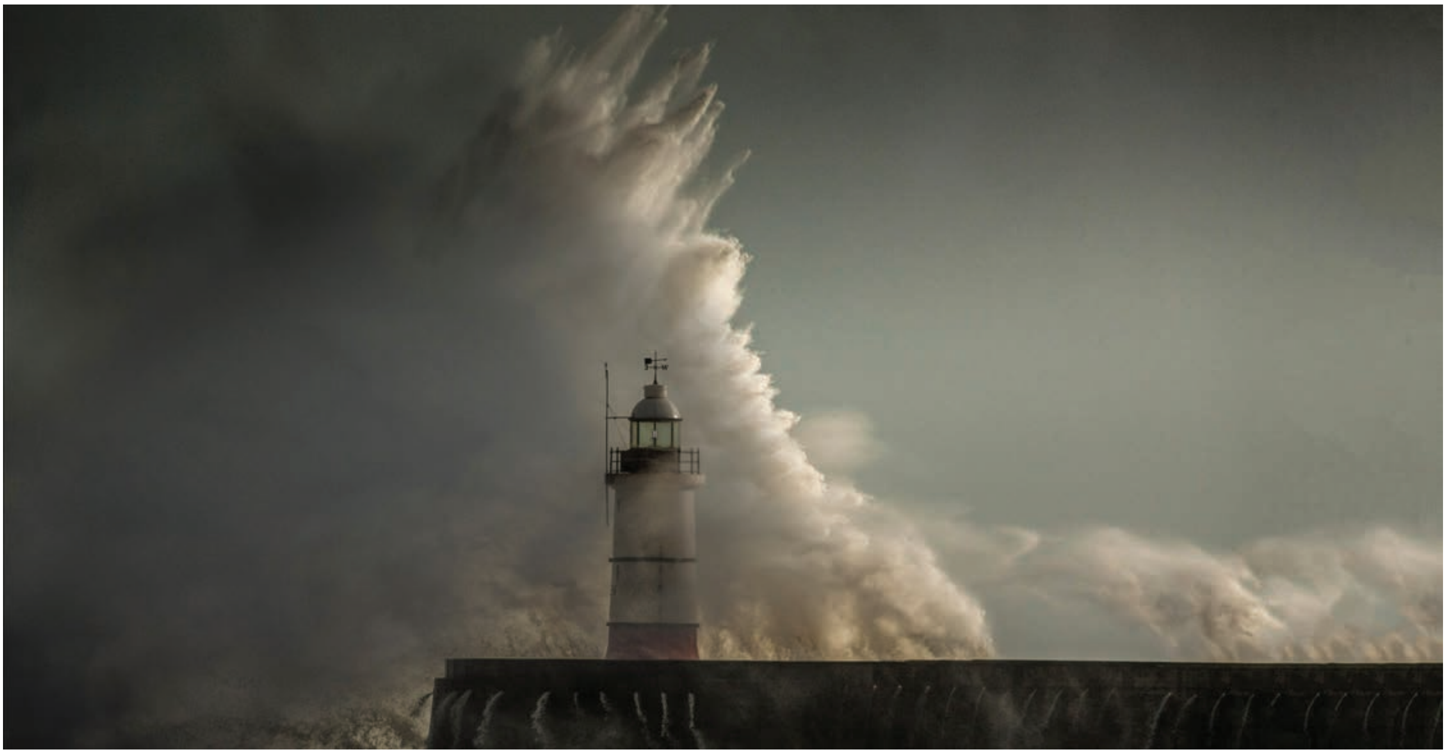
Where next for pensions policy?

The TUC Member Trustee Network conference on 26 November reflected on a significant year for pensions, which saw the first wave of employers implement auto-enrolment. In 2013 there was also a flurry of initiatives from government, including final proposals for the single-tier state pension and abolition of contracting out; Steve Webb's ideas for 'defined ambition' pensions; and plans for both DC charges and scheme quality standards. The keynote address was from Pensions Minister Steve Webb, whose paper on defined ambition schemes is featured on page 6. Other guest speakers included Con Keating and Hilary Salt, giving between them a lively and provocative view on DB valuations. Speakers also included Andrew Vaughan from the Association of Consulting Actuaries, Shadow Minister Gregg McClymont and consultant Sarah Smart. Workshops on defined ambition, de-risking, stewardship, the DC governance gap and investment governance in the LGPS were well attended, with lots of contributions from delegates. Presentations from the 2013 conference are available online at **http://www.tuc.org.uk/economic-issues/pensions-and-retirement/member-trustees/where-next-pensions-policy**

Pensions Ombudsman cases

The Pensions Ombudsman has ruled *Bradbury v BBC* (PO 636) that the BBC had not breached its implied duty of mutual trust and confidence in seeking to impose a one per cent cap on increases in pensionable pay contractually rather than by amending scheme rules. Mr Bradbury had complained that the BBC had changed the definition of pensionable salary without consulting the trustees and had failed to make the proper changes required to the trust deeds and scheme rules. The Ombudsman ruled that the BBC had not breached its implied duties in doing so, had acted reasonably in the light of the scheme's deficit and potential future liability, Mr Bradbury was not contractually entitled to a salary increase, and the BBC had informed members of the proposed changes.

In the case of *Mrs Tuttle v the NHS Scheme* (PO 86135) the Deputy Ombudsman found that Mrs Tuttle had relied on an incorrect estimate to decide to retire early. She directed that Mrs Tuttle be compensated for the extra time that she would have spent in paid work and to ensure that her pension was that which it would have been had she retired at the later date. The NHS scheme's defence, that the estimate made clear it was only an estimate and not a guaranteed quotation, was not accepted as an adequate defence.



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Climate change is an issue for trustees, says pensions minister

Speaking at the launch in October of ShareAction's report *The Green Light Report: resilient scenarios in an uncertain world,* Pensions Minister Steve Webb warned pension funds of the risk associated with climate change. He said: "Those who at least question what the firms are doing to diversify and to mitigate the carbon implications of what they're doing may well have a competitive advantage. Simply upgrading our electricity infrastructure alone will require over £100bn of capital investment between now and 2020. These sorts of issues are not marginal or niche. They're absolutely mainstream." He added: "We particularly welcome the Law Commission's provisional conclusion that fiduciaries such as pension scheme trustees may take into account factors relevant to long-term investment performance, including environmental factors and wider systemic considerations, and indeed they should actively consider whether doing so serves the best interests of their beneficiaries."

The report on climate-conscious investment argues that pension funds have the responsibility to protect the public and their pension savings from climate risk, and aims to assist pension funds by guiding them through the financial implications of climate change and the steps they can take in light of the risks and opportunities it presents. You can download the report from **http://www.shareaction.org/greenlightreport**

» These sorts of issues are not marginal or niche. They're absolutely mainstream. «

Recommendations in the report include:

- undertake training on the financial materiality of climate risks
- develop a policy and action plan on climate risks and report regularly to members on progress being made
- require fixed income managers to demonstrate how they integrate carbon/climate risks into credit analysis
- request that investment managers support collaborative initiatives to secure greater transparency and accountability on investee companies' lobbying positions.

Meanwhile an annual global survey by Mercer of major pension asset owners has found that 100 per cent now assess their investments for climate change impacts. However, investors continue to face hurdles such as limited data available in certain asset classes as well as inadequate company disclosures.