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How the SoS package is made

The Pensions Regulator has published information about the statements of strategy that trustees of private sector defined benefit (DB) schemes will soon be required to produce with their actuarial valuations. It seems that, in many cases, less info will have to be provided than initial proposals had foreboded.

The details have been published in the form of an interim response to the consultation exercise that the Regulator ran from 5 March to 16 April 2024. The purpose of the interim response is to allow trustees to plan ahead and make progress with valuations. A full response about the consultation will be given '*in the winter*'. The first statements won't be submitted until spring 2025, when a new digital service is launched.

The meat of the matter

Under reforms to the funding legislation, due to take effect for valuations with dates on and after 22 September 2024, the trustees of a DB scheme will be required to formulate a *funding and investment strategy* (FIS)—a long-term plan for providing the scheme's benefits. The trustees must set out their FIS and various supplementary matters in a *statement of strategy* (SoS) that they will have to send to the Regulator, which has discretion over the form in which SoS are submitted, and the level of detail that they must contain.

Preparation, review or revision of SoS will generally occur as part of the usual valuation cycle. The Regulator will operate a two-lane system for assessing compliance. Valuations that meet relatively prescriptive 'Fast Track' conditions are likely to receive minimal regulatory scrutiny. Those trustees who cannot, or do not wish to meet the Fast Track requirements will be able take a more flexible 'Bespoke' route, whilst accepting that the Regulator will take a closer look at their valuations.

The new SoS recipe

The Regulator has published four SoS templates with the interim response (plus a reference list of all of the data that might be required). Each template is relevant to one of the permutations of Fast Track or Bespoke

compliance and whether the valuation date is before or after the scheme reaches '*significant maturity*'. Although the cosmetic presentation of the SoS variants is likely to be different when the new online portal (see below) goes live, the Regulator says there will be no changes to the information required, which should give trustees the confidence to plan ahead.

There was widespread agreement, among respondents to the consultation exercise, that the information that Regulator proposed to capture was excessive, disproportionately burdensome, and did not make sufficient allowance for individual scheme characteristics and circumstances. In response, the Regulator has streamlined the templates by cutting unnecessary narrative, included more opportunities for trustees to explain their own situations in free text, and accommodated schemes with particular features, such as cash balance benefits and remaining open to accrual.

Other changes include the following:

- The Regulator has adopted a single definition of 'small scheme', having initially proposed to apply one of two definitions, depending on context. It captures schemes with no more than 200 members, but doesn't count death-benefit- and DC-benefit-only members, nor people whose benefits have been fully bought in and excluded from valuation liabilities. The Regulator thinks that about half of all schemes will fall within the new definition, and will consequently benefit from reduced information requirements.
- Schemes considered 'low-risk' won't need to submit detailed covenant information. This category covers fully bought-in Fast Track schemes, and those that are in surplus on a low-dependency funding basis after the application of a stress test.
- Trustees will be able to describe their long-term objectives in their own words, rather than being forced to pick from a list (the options were originally buy-out, run-off, move to a superfund or alternative consolidator).
- The Regulator has reduced the cash-flow information that it will require schemes to submit, and removed the requirement altogether for small schemes and those using the Fast Track.
- The templates will allow for a greater range of possible discount-rate and yield-curve methodologies (with, in the latter case, the opportunity to explain other approaches). Only 40 (not 100) years' forward yields will be required.
- The Regulator has simplified the information it requires about the notional investment allocation, and how trustees expect it to evolve over the period until the scheme reaches significant maturity (they'll also have the opportunity to explain their approach). The templates now accommodate schemes that have specific target interest rates and inflation-hedging ratios. There's no requirement to submit currency-hedging information.
- There's more flexibility about the framing of covenant information. Trustees of multi-employer schemes will be able to aggregate covenant data, where appropriate (and explain their approach). The templates now make allowance for un-segregated, non-associated multi-employer (NAME) schemes to summarise their assessment of supportable risk, rather than submitting the cash-flow information expected for other schemes.

Serving up the SoS

A new online system for submission of SoS, actuarial funding valuations, and (where applicable) schedules of contributions and recovery plans is scheduled to go live in the of spring of 2025. Trustees with valuation dates on or after 22 September 2024 won't be expected to submit valuation documentation or SoS until the new system is available. (Documentation associated with valuations at earlier dates should be submitted using the existing Exchange facility.)

Overall, we're glad to see that TPR has taken on board feedback on the original proposals, streamlining the templates and scaling back some of the detail. Noting that an increasing number of DB schemes are well-funded and relatively low risk, the concessions for those in surplus and on Fast Track are particularly welcome. Trustees and sponsors will need to familiarise themselves with the new compliance requirements, but at least now they have the certainty to meaningfully prepare to write up plans in the format required.

PPF targets £100m of levies, again

The Pension Protection Fund (PPF) proposes to collect £100m via its levies in 2025/26, the same levy estimate as for 2024/25. To keep the amount raised to that level and distribute the burden widely and in a way that reflects risk, it is adjusting some of the factors that go into the levy calculation.

Rationale

The falling number of defined benefit schemes, and the improvement in the funding ratios of those that remain mean that, without changes to the levy calculation, the number of schemes paying risk-based levies would fall by 40%.

In the absence of changes to the fixed levy parameters, the levy estimate would fall to £55m. Legislative restrictions in place since the PPF's inception limit the proportionate increase that can be made from one year to the next (they also mean that the risk-based element of the levies must comprise at least 80% of the total). As levies reduce, therefore, the scope to increase them in subsequent years also reduces: at the extreme, a reduction to zero would inhibit subsequent reintroduction forever. In the absence of legal change, the PPF is hesitant to reduce levies below £100m, the level that it thinks is the minimum necessary to enable it to resume raising sufficient levies to recover from any economic shocks.

The PPF hopes that the Government will amend its governing legislation to give it enough flexibility and confidence to reduce the levies further, even to zero if appropriate, in future. However, with a change of Government and the launch of a review of the pension system, it believes that there is some uncertainty over the timing of the necessary amendments. The PPF has rejected calls for it to switch off the levies in the meantime, for fear that it would be unable to easily turn them back on at the required level if the need re-arises—although it considers that necessity to be remote.

Changing to stay the same

The PPF wants to distribute the £100m levies over as large a pool of schemes as possible, doing so in a way that means higher-risk schemes pay more. This is achieved by increasing the asset – liability stresses (both 'naturally', to capture the interest-rate volatility of 2022, and less naturally to broadly double the 'shock' from one standard deviation to two) and then reducing the risk-based levy scaling factor (from 0.40 to 0.35). The scheme-based component of the levies, effectively a cross subsidy benefitting the highest- risk schemes, has been

increased by 20% (from 0.000015 to 0.000018). The stress-factor changes add £55m, whilst the adjustments to the other parameters together remove £10m, such that the otherwise-£55m levy estimate gets back to £100m.

The PPF has made limited changes to its insolvency-risk assumptions, noting early indications that the rate of insolvencies may be reaching its peak. It has also decided that it should apply the most up-to-date valuation assumptions to the calculation of the levies, having chosen not to do so for levy year 2024/25 (in the interest of minimizing the number of changes being made at one time).

Implications for levy payers

The PPF believes that around 63% of the schemes that pay risk-based levies would experience a decrease in that aspect of their levy bill. Of the remaining 37%, for which the risk-based levy is expected to increase, 5% should expect an increase of no more than 0.01% of liabilities (that's £50,000 for a £500m scheme) and none should have an increase of more than 0.07% (£350,000 for a £500m scheme). The cap on the risk-based levy would be maintained at 0.25% of liabilities.

As a result of the change to the scheme-based component, it is thought that 72% of schemes will see their 2025/26 levy total grow somewhat, compared to 2024/25's. The increase in the scheme-based levy is expected to be slight, though, leading the PPF to say that it expects that it will generally be '*broadly the same*' as in 2024/25, and adding that total levies will be lower for more than 95% of schemes than they were in 2023/24 (when the levy estimate was £200m).

Larger schemes would be able to certify recovery-plan and special contributions using the simplified ('*Option Beta*') approach. As well as being simpler, this should also reduce levies more than the approach that is currently open to them ('*Option Alpha*'). The PPF also proposes to make it easier for fully bought-in schemes to apply to have their levies waived.

Consultation arrangements

The consultation period runs from 12 September to 23 October 2024. Respondents can choose between making a full submission, or a quicker, less-detailed response.

Let's hope that the Government finds some time soon to reform the primary legislation, so that the PPF can stop raising £100m a year that it doesn't need.

Questions for the pensions review

His Majesty's Treasury, the Department for Work and Pensions and the Ministry of Housing, Communities and Local Government called for evidence to feed into the first phase of the Government's pensions review. It asked questions about, for example,

- the risks and opportunities of further defined-contribution (DC) scheme consolidation
- the future of single-employer DC trusts
- the future roles of master trusts versus group personal pensions, and their respective governance models
- barriers to consolidation
- how successful the Local Government Pension Scheme (LGPS) has been
- the roles of different stakeholders as drivers of cost competition, and the effect on asset allocation
- the case for encouraging return-seeking via a wider range of asset classes
- the potential for consolidation to contribute to UK growth
- the factors underlying changes in investment behaviour
- whether there is a case for nudging schemes toward higher allocations in particular asset classes, and for encouraging the LGPS to invest in local communities, and if so what are the options and their relative prospects.

The call for evidence closed on 25 September 2024. The conclusions from the first phase of the pensions review are expected to influence the contents of the forthcoming Pension Schemes Bill.

Regulator parses DB funding data

The Pensions Regulator has published an *Occupational Defined Benefit Scheme Funding Analysis 2024*, covering 'tranche 17' valuations (those with effective dates falling within the period from 22 September 2021 to 21 September 2022). The main findings, as reported by the Regulator, are that:

- 47% of the schemes were in surplus, compared with 32% for tranche 14 (the last time the same cohort went through the triennial valuation process);
- the average (mean) ratio of assets to technical provisions was 97% (the median was 99%); and
- the average recovery-plan length was 4.7 years (median 3.9 years), whereas for tranche 14 valuations it was 6.2 years (median 5.2 years).

Making short work of Ombudsman cases

The Pensions Ombudsman has published a blog post about his plans for 'expedited determinations'. It's one way in which he hopes to make greater inroads into the growing list of complaints.

The Ombudsman has several mechanisms intended to facilitate informal resolution of disputes, including an early resolution service and caseworkers and adjudicators who investigate complaints and provide the parties with considered opinions. One of the problems that the Ombudsman encounters is that members can always reject such attempts, and push for a formal determination, regardless of the merits of their case.

Expedited determinations appear to involve a triage or case-management process, designed to identify and deal with applications that have no chance of success. If anyone disagrees with the caseworker's initial view, that party will be able to ask for it to be referred directly to an Ombudsman for a final decision, skipping the adjudication stage. The Pensions Ombudsman hopes that it will reduce the time some customers wait for a resolution by as much as 18 months.

How the Regulator will enforce dashboards compliance

The Pensions Regulator has published a pensions dashboards enforcement policy. It says that it will take a risk-based approach, focusing on behaviors and breaches that pose the greatest risk to savers' abilities to receive a complete and accurate picture of their pensions. Notably, it explicitly recognizes that dashboards represent '*a huge challenge for industry*', and suggests that its approach will generally be to help trustees and providers to comply—although it will not shy away from stricter measures when it spots '*wilful or reckless non-compliance*').

The Regulator says that it will, in particular, concentrate on:

- connection compliance (where breaches will include failure to connect by the connection deadline, to have regard to the connection guidance, and to remain connected)
- schemes that are failing to match people to their pensions or making mismatches that result in provision of information to the wrong person
- provision of inaccurate or out-of-date information
- ensuring that schemes keep clear audit trails showing how they have been monitoring progress, and records of compliance (as set out in the MaPS reporting standard) and the actions taken to resolve issues
- monitoring and identifying the risk of non-compliance using multiple sources.

The appendix to the enforcement policy contains useful scenarios showing how the Regulator may use its powers in various situations.

The enforcement policy was announced by a blog, Act now on pensions so we don't have to which emphasizes the importance of having accurate and complete data. It says that the Regulator will be 'engaging with hundreds of schemes this autumn, asking them to account for how they are measuring and improving their data', with the threat of regulatory action where trustees are failing to meet its expectations.

The Regulator's response to the consultation exercise on the draft policy has also been published.

HMRC newsletters: September 2024

Pension Schemes Newsletter 162, from His Majesty's Revenue and Customs (HMRC), says that—

- regulations to fix problems with the lifetime-allowance-abolition legislation will be introduced '*as soon as Parliamentary time allows*' (having been subject to a short, informal consultation exercise);
- the Revenue is organizing a workshop for scheme administrators in early October on changes to 'real-time information' (RTI) and reporting of relevant lump sums, and invites them to register interest if they haven't done so already;
- HMRC is also looking for volunteers to user-test a feature of its online Managing Pension Schemes service (MPSS) that will allow scheme administrators and practitioners to check members' entitlement to lump sum protections and enhancements;
- relief-at-source scheme administrators need to submit outstanding returns and declarations for 2023/24 before their interim repayment claims will be paid;
- scheme administrators who haven't done so already should take the necessary steps to migrate their schemes over to the MPSS;
- the MPSS is scheduled for some maintenance and is expected to be offline from 16:00 on 11 October to 10:00 on 15 October 2024.

A September 2024 edition of HMRC's Newsletter on the Public Sector Pensions Remedy contains articles about the following:

- the *Calculate Your Public Sector Pension Adjustment* service is back online, with a list of improvements that are detailed in the Newsletter;
- a potential obligation on members to report and pay tax on any interest element of the *McCloud* remedy (there's an appendix on the subject); and
- Government plans to permit scheme administrators to offset overpaid charges on unauthorized payments against revised charges when the member's tax liability changes as a result of the remedy; to exempt interest on underpaid unauthorized payments from the scheme sanction charge; and what to do if the full amount of the overpayment can't be offset against the amount now due.

The Newsletter was later updated to include an additional appendix providing more information about the offsetting process for the unauthorized payments charge.

And Finally…

There was a moment, back a few years ago, when the all the talk seemed to be about a decline in the public's trust in experts. *AF* was reminded of that when reading a recent Tribunal judgment that explores a different question: how much trust is too much trust?

The two appellants in the case were seemingly part of a larger group of individuals involved in earlier Tribunal proceedings. They had been persuaded to set up occupational pension schemes by a company that, HMRC suspected, was involved in promoting them as part of tax-avoidance arrangements. The Revenue served information notices upon the company, which was designated as the scheme administrator for all of the schemes. No sooner were those notices received than, according to evidence led by HMRC, there was a sudden flurry of online activity that resulted in the *individuals* being named as the scheme administrators of their respective schemes in place of the company. The lawyer representing HMRC in the earlier proceedings invited the Tribunal to infer that the individuals might not in fact have made the necessary declarations themselves—everything seemed to have happened during two web-browser sessions, over the course of two days, and the individuals were later surprised to find that they were the scheme administrators—but the judge in that case didn't have to make any finding on the matter.

Either way, this led on to the events that were the subject of the recent appeal. HMRC re-issued the information notices to the newly designated individual scheme administrators. The ex-administrator company engaged another firm to advise on the information notices and correspond with HMRC on the individuals' behalf. The individuals were told that there should be no need to respond, as the schemes had been wound up. This argument was raised numerous times, even though HMRC had pointed out that the notices were issued to the individuals, not the schemes, so were unaffected by the wind ups.

The individuals were issued with £300 non-compliance fines, but were advised that no action was required by them as the adviser firm was taking the matter up with HMRC. There followed several tranches of additional penalties, which were accruing daily, initially at the rate of £30 per day of continued non-compliance, and later at £60 per day. This went on for the best part of two years, so that many thousands of pounds' worth of fines were eventually racked up by each appellant. The individuals accepted the adviser's reassurances that it was handling things, and that they didn't need to do anything.

The Tribunal judge concluded that neither of the appellants had taken reasonable care to confirm that they could rely on the advice, when a prudent taxpayer would have asked questions of it. It was, she said, '*closer to reliance on an unchecked assumption that they were being appropriately advised.*' As a result, neither appellant had a reasonable excuse for their failure to comply with the information notices, so they remained liable to pay the penalties in full.

At the Tribunal hearing, the advisers explained a year's delay in appealing by saying that they were '*eternal optimists*' and that they thought that the situation '*couldn't go on forever*'. They also said that they'd thought that if they'd appealed against the penalty notices it might look like they were accepting that the notices were valid, an explanation that the judge said was so absurd that she couldn't believe it was an accurate reflection of their position. She also commented on their '*misplaced optimism that repeating the same argument over the course of a year… will change HMRC's view*'—despite the

evidence of the steadily mounting penalties that might have indicated that the argument was having limited persuasive success.

AF suspects that a behavioural psychologist or economist could explain the appellants' over-extended trust in the advisers by reference to phenomena like the sunk-cost fallacy and escalation of commitment. However, he has filed away the judge's comment about misplaced optimism about the effectiveness of endlessly repeating the same argument, for use with his children…

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