LDI
The work to be done to improve oversight of the investment strategy

Greenwashing
With an increased focus on ESG, greenwashing can be a danger to schemes

Solvency II
Will new Solvency II proposals help insurers cope with the increasing number of buyouts?

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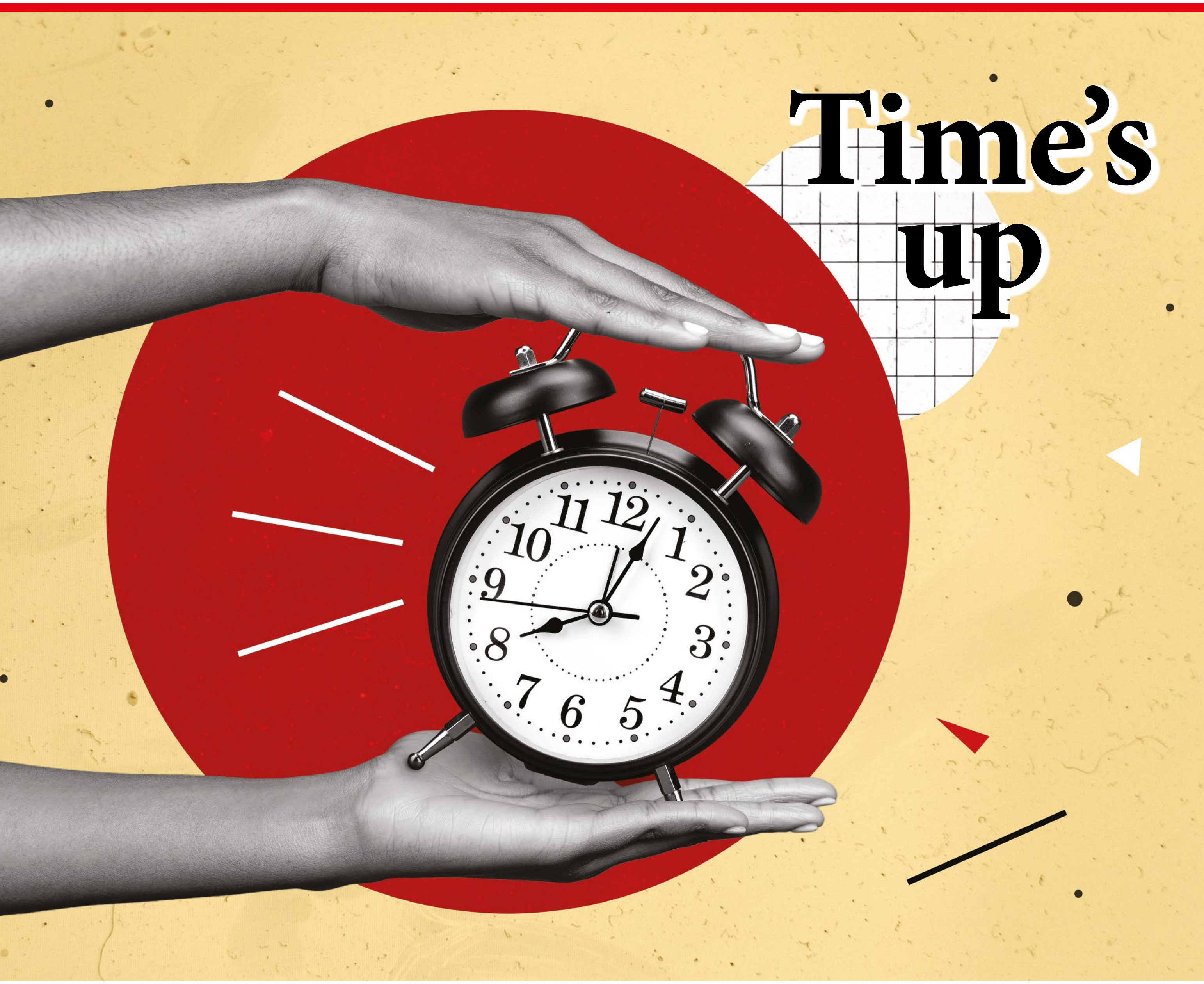
January 2023

PENSIONS*Age*

The leading pensions magazine

SCAMS FOCUS 2023: *The different types of pension scams, how the cost-of-living crisis may increase the prevalence of scams, and the impact of scams for both the member and the pensions industry are explored in the first of Pensions Age's year-long series on the subject*



Time's up

Are auto-enrolment reforms on the horizon for 2023?

INSIDE: Trustee Guide 2023

Editorial Comment

2nd Floor, 5 Maidstone Buildings Mews, London. SE1 1GN

It's a new dawn, it's a new day, it's a new consultation. This seems to be the mantra at the start of every new year for anyone involved in pensions. As soon as that last firework fizzles out in the early hours of New Year's Day, and that Prosecco buzz starts to wear off, it's likely to be feelings of anxiety rather than anticipation that set in, as looking ahead into the future of pensions more often than not means staring into the face of more regulation, more change, and more uncertainty.

When I asked several pension trustees last month what would be on their wish lists for 2023 *[see our trustee guide feature on pages 46-47]* 'more resource' and 'less change' were, unsurprisingly, the most common requests, but one particularly pertinent answer was a request for 'more time'. As a busy mother of three, a feeling that there aren't enough hours in the day is something I can certainly resonate with but, unfortunately, more time is the one thing no government department, Pensions Minister or even optimistic new King can provide, no matter how nicely we ask for it.

"I have been involved in pensions for almost 20 years and I genuinely feel that the sector is in one of the best places it has ever been"

So let's take a few moments to stop the proverbial clock and, given the theme of this month's issue is 'taking stock', let's take a look at what's ahead of us in 2023, and think about why we should approach the new year with positivity rather than panic.

Yes there is a lot on the agenda, as our 'looking ahead' feature on pages 28-30 outlines – dashboards preparation sits at the top, alongside the arrival of The Pensions Regulator's new Defined Benefit Funding Code; the ongoing work following its Single Code of Practice; plus a re-think of investment strategies and, in many cases, a lot of extra rushing around as a result of the liability-driven investment roller coaster, which last year saw many schemes closer to buyout sooner than expected.

Add to all of this the ongoing pressure on schemes to pay more attention to their environmental, social and governance obligations; while they also need to keep a keener eye on diversity and really try to understand what having a diverse workforce or pensions board truly means (it's about so much more than just hiring one or two more women and thinking that box is ticked). There's value for member and value for money also to be considered; small pots consolidation; combatting scams (which our *Pensions Age* scams awareness campaign for 2023 is trying to help tackle, see pages 34-35). Then there's potentially some long-awaited auto-enrolment reform on the horizon *[pages 69-71]*; and so much more I don't have space (or time!) to mention – and all against a backdrop of a cost-of-living crisis, high inflation and a potential capacity crunch.

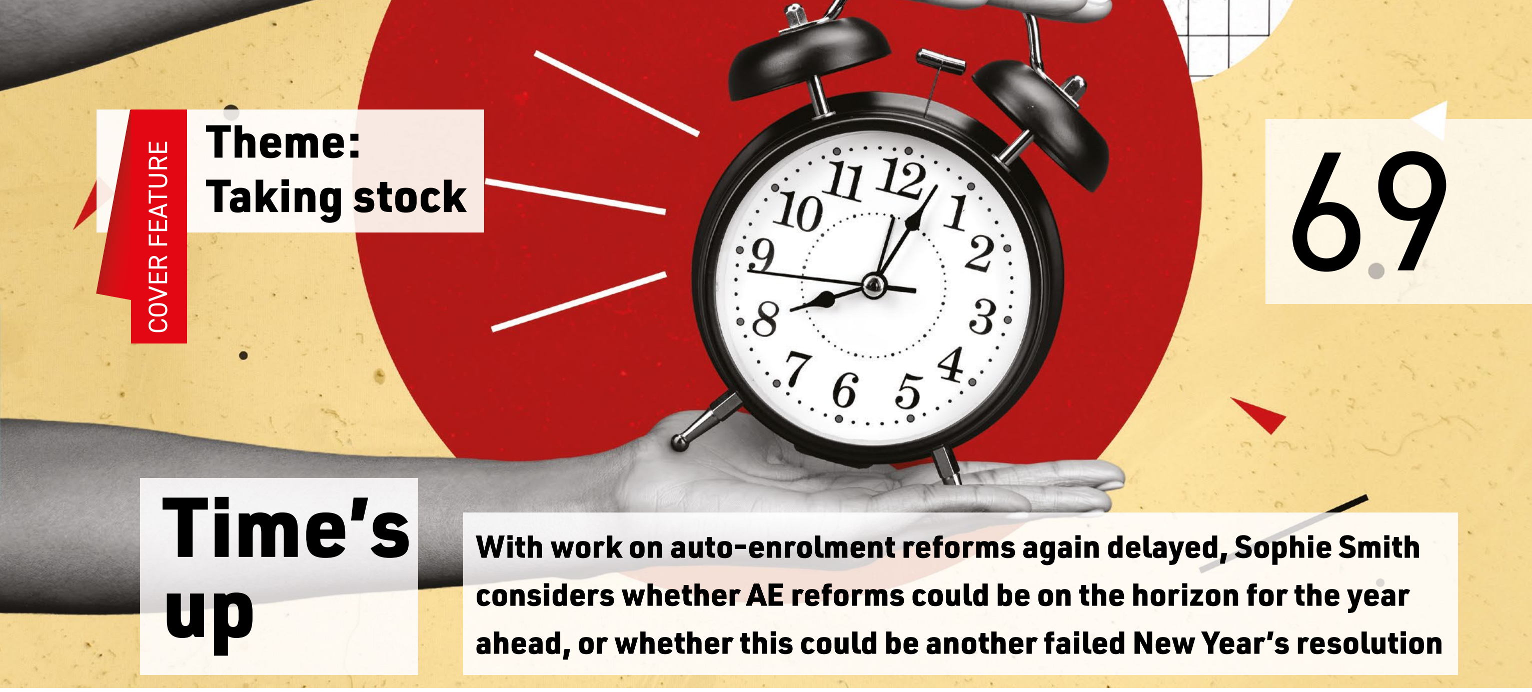
It's exhausting just thinking about it all. But while it may feel that this will all mean less time for anyone to do their jobs properly, be they trustees, consultants, lawyers, asset managers or even, dare I say, pensions journalists, all of these items on the agenda are really for the good of the industry and more importantly the member. I have been involved in pensions for almost 20 years and I genuinely feel that the sector is in one of the best places it has ever been.

Take the huge strides that have been made following the introduction of auto-enrolment 10 years ago; take the genuine innovation that we are seeing in all aspects of pension provision, from technology and communication, to investment vehicles and scheme design. Yes, more regulation might mean more hard work and late nights, but as a wise trustee kindly reminded me, it has also (on the whole) meant more professionalism and more protection for those who invest in a pensions vehicle.

And finally a word on pensions dashboards. These have been talked about for years and years at pensions events we have hosted, and while they always seemed like a pipe dream, it's hard to believe they are finally about to happen. Yes they come with ambiguity and hard work, and things will inevitably go wrong as we iron out the details, but most in the market agree they will be a positive force. Not only will they lead to cleaner and better data along the way, they will hopefully meet the long-term objectives of boosting pensions awareness, ownership and engagement.

So on that note, let's not wish for the unobtainable; but let's make the most of what we have and pat ourselves on the back for continuing to care enough to make this industry better and better every year – whatever the world throws at us. Our cover story this month is entitled *Time's Up*, but time isn't up for pensions at least – 2023 has only just begun and we are starting it busy but definitely in a stronger position than ever.

Francesca Fabrizi, Editor in Chief



COVER FEATURE

Theme: Taking stock

Time's up

With work on auto-enrolment reforms again delayed, Sophie Smith considers whether AE reforms could be on the horizon for the year ahead, or whether this could be another failed New Year's resolution

News, views & regulars

Features and columns

Continued on page 6

Features & columns

Continued from page 5

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Dateline - December 2022

Rounding up the major pensions-related news from the past month

1 December The Pensions Dashboards Programme (PDP) published its consultation on the design standards for pensions dashboards, outlining its proposals for how information should be displayed. The consultation, which runs until 16 February, proposes the design standards that qualifying pensions dashboards services (QPDS) will have to abide by when presenting users' pension information on dashboards.

Alongside this, the **Financial Conduct Authority (FCA)** launched a consultation on the proposed regulatory framework for pension dashboards operators, confirming that firms will be able to offer additional services, provided they meet "rigorous conduct standards". As part of this, the FCA outlined its intended approach to supervision and enforcement for dashboard operators, including on fees, regulatory reporting, record keeping, prudential requirements and conduct rules.

In addition to this, the FCA published final rules requiring providers of non-workplace pensions to offer consumers a default investment option and to issue a warning about the risk of inflation eroding the value of cash holdings. The rules will require providers to offer a 'default' ready-made, standardised investment option to non-advised consumers buying a non-workplace pension.

1 December The **Work and Pensions Committee** (WPC) wrote to the Pensions Minister, Laura Trott, to request further clarification around some of the recent issues raised as part of the committee's inquiry into liability-driven investment (LDI) strategies and defined benefit (DB) pensions *[see page 42 for more information on LDI developments]*.

1 December The net funding position of DB pension schemes improved to a surplus of £193bn in the year to 31 March 2022, amid the largest-ever annual fall in liabilities, the 17th annual **Pension Protection Fund** (PPF) *Purple Book* revealed.

2 December The **FCA** fined Pembrokeshire Mortgage Centre (PMC) Limited, currently in liquidation, over £2.3m for unsuitable advice to transfer out of the British Steel Pension Scheme (BSPS) and other DB pension schemes. The firm advised 420 consumers, nearly two-thirds of whom were BSPS members, on whether to transfer out of their DB scheme. Overall, 93 per cent were advised to transfer, with PMC earning over £2m in transfer and ongoing advice fees.

5 December The government launched a consultation on plans to amend **NHS** pension rules in an effort to retain staff and remove barriers for those returning from retirement, although it has not included any changes to the lifetime or annual allowance.

7 December The **WPC** wrote to the Minister for Pensions, Laura Trott, to seek updates in a number of areas, including the state pension age review, the government's GMP factsheet, and issues around the Financial Assistance Scheme.

7 December Industry experts suggested that trustee knowledge was a key issue during the recent **liquidity issues** faced by DB pension schemes, as inquiries continue following the gilt market volatility. MPs have been reassured that work is already underway to build resilience, although experts remain divided on the root cause of the recent issues.

7 December The Pensions Regulator (TPR) and the **FCA** have issued an update to their joint regulatory strategy. It emphasised the importance of a collaborative approach in the current environment and identified eight joint workstreams.

For more information on these stories, and daily breaking news from the pensions industry, visit **pensionsage.com**

9 December The **Insolvency Service** disqualified three directors from acting as directors of any company for their role in pension mis-selling, which took over £44 million from would-be investors.

12 December The **Treasury** unveiled a raft of financial service reforms, including plans to lay regulations to reform the DC pensions charge cap in early 2023, and plans to increase the pace of DC pension consolidation.

12 December The **government** published guidance on applying for a deferral of the pensions dashboards staging deadline, as the Pensions Dashboards Regulations 2022 officially came into force.

13 December The **PPF** confirmed a "significant reduction" in its levy for 2023/24 after receiving broad support for its proposed changes to the 2023/24 levy rules, with 80 per cent or more of responses supporting each proposal. Almost all (98 per cent) schemes are expected to pay less levy next year, with changes to the levy rules to cut the levy to around £200m for 2023/24, down from £620m in 2020/21 and £390m for 2022/23.

14 December The **Bank of England** (BoE) recommended that TPR, in co-ordination with the FCA and overseas regulators, takes regulatory action to ensure LDI funds remain resilient.

14 December The **FCA** announced that it is planning to review the Financial Services Compensation Scheme's (FSCS) compensation limits for pension claims.

The Pensions Regulator
Making workplace pensions work

14 December **TPR** published its draft Funding Code of Practice for DB pension schemes, alongside its consultations on the code and its proposed fast-track and twin-track regulatory approach to DB scheme funding. The new code is due to come into force from October 2023, and it will replace the current code that was introduced in 2014.

16 December More than 60 people who transferred over £10m from occupational pensions into "inappropriate" Qualifying Recognised Overseas Pension Scheme (QROPS) investment funds won a **High Court** appeal to have their case heard in the UK. The 62 investors from the UK claim that they received negligent financial advice in 2014 and transferred more than £10m from DB pension schemes to QROPS investment funds administered by Castle Trust Management Services. Represented by High Street Solicitors, the investors were initially unable to sue Castle Trust Management Services, a QROPS administrator based in Gibraltar, after a High Court ruling in 2021 deemed the Courts of England and Wales did not have jurisdiction to deal with the complaints. However, following an appeal in October 2022, the decision was overturned in November 2022.
While the total loss is still to be determined by an actuary, the minimum losses were £10.2m, which is the total amount transferred from DB schemes into the QROPS. Castle Trust Management Services has until 25 January 2023 to file its defence.

21 December The **Department for Work and Pensions** (DWP) published its departmental review of the PPF, recommending that the lifeboat reassess its working relationship with the DWP, including on any potential legislative changes needed around the PPF annual levy, and suggesting that PPF consider seeking authorisation from the FCA.

31 December The pensions ombudsman and Pension Protection Fund ombudsman, **Anthony Arter**, was awarded a Commander of the Order of the British Empire (CBE) for his services to the pensions industry and charity. Redington co-founder, Dawid Konotey-Ahulu, was also awarded a CBE for his services to diversity and inclusion, while former IA chair, Keith Skeoch, was awarded a Knight Bachelor.

News focus

TPR launches consultation on long-awaited DB Funding Code

The Pensions Regulator has published the draft DB Funding Code and accompanying consultations. The pensions industry has broadly welcomed the draft code, although concerns are emerging around a potential mis-match between the regulator and the Department for Work and Pensions' regulations

The Pensions Regulator (TPR) has published its draft Funding Code of Practice for defined benefit (DB) pension schemes, alongside consultations on the code and its proposed fast-track and twin-track regulatory approach.

The new code, which is expected to come into force from October 2023, aims to support trustees, sponsoring employers and their advisers to manage their DB pension schemes. It will replace the current code, introduced in 2014.

However, as the code is forward looking, only schemes with valuation dates on or after commencement will be affected, with TPR confirming that trustees currently working on a valuation should continue using the current code.

In the code, TPR stressed that schemes are expected to set a long-term objective and a journey plan to get there, and that it expects schemes to reduce reliance on their sponsoring employer as they reach maturity.

In particular, the code outlined the regulator's key expectations for trustees to set a plan as to how they will achieve low dependency on the employer, setting a journey plan to reach that point, assessing the employer covenant as a key underpin for the level of risk that is supportable on that journey, and setting funding assumptions consistently with those plans. It also outlines expectations for assessing reasonable affordability when determining the appropriateness of recovery plans, and on open schemes, allowing for future accrual where they can justify this.

Commenting on the updates, TPR executive director of regulatory policy, advice and analysis, David Fairs, stated: "In line with DWP's draft regulations, our draft code is clear that all DB schemes should have the necessary long-term funding approach to ensure savers have the best chance of receiving the benefits they expect.

"We want to provide schemes with the continued flexibility around funding to suit their circumstances, while requiring trustees to think carefully about risk management to improve security for their members.

"We have worked hard to ensure the draft code's principles reflect the 127 responses we received to our first consultation on the code, the clarity we now have on the draft regulations, and our modelling and analysis."

Alongside the core DB Funding Code, TPR launched a second consultation on its fast-track and a twin-track regulatory approach, which is designed to help TPR filter out the estimated half of schemes that will require minimal engagement.

Under the new system, trustees following fast track will be asked to evidence how their scheme meets three criteria: Surrounding technical provisions, an investment stress test and prescribed recovery period.

The bespoke approach, meanwhile, will be available for those unable to meet fast-track criteria and, according to the regulator, may also be more appropriate for schemes following a more complex funding and investment path.

The consultation explained that TPR's approach has evolved since its initial consultation, in light of the draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023, industry feedback via consultation responses, as well as further modelling and analysis.

In particular, TPR noted that although

the fast-track approach was initially expected to be embedded in the code of practice, this separation is expected to provide greater flexibility to change fast track without requiring an amendment to the code of practice.

This decision has already been praised by industry experts, as ECPA chair, Karina Brookes, and PwC head of pensions funding and transformation, John Dunn, both welcomed the decision to de-link fast track and bespoke, and to keep fast-track filters separate from the code, respectively.

Yet other areas have remained consistent. For instance, although TPR acknowledged that market conditions have materially changed since the last consultation, it argued that the discount rate for fast track represented an "appropriate long-term target", and has therefore remained unchanged.

However, the consultation does include a section on system risk, and how the draft code may acknowledge this, highlighting the risks around liability-driven investment (LDI), after "events in 2022 highlighted the potential systemic risks from the use of leveraged LDI".

TPR stated: "Schemes that are planning to use or are using LDI may be in a better position to evidence that they can meet our expectations, as this will reduce funding volatility from changes in interest rates and inflation expectations.

"Similarly, our proposals for fast track in relation to the stress test included some specific allowance for leveraged LDI. For the fast-track stress test, only a relatively small level of leverage has been factored in. For an immature scheme we have used an example portfolio with around 60 per cent growth, 15 per cent corporate bonds and 25 per cent gilts and using 2x leverage."

TPR also confirmed that, overall, the level of leverage assumed throughout fast track is "materially lower than current market norms, even after LDI de-leveraging seen from September 2022".

"Improved governance and operational processes, lower leverage in matching assets, and higher levels of liquid collateral will mean that schemes are much more resilient to significant increases in gilt yields," it stated.

"We want to provide schemes with the continued flexibility around funding to suit their circumstances"

Although TPR suggested that more information on the level of leverage and collateral is needed to help monitor and control this risk further, it argued that it is not likely that the expectations in the code will increase or exacerbate these risks.

The pensions industry has broadly welcomed TPR's draft DB Funding Code, although some have questioned whether the level of regulation is proportionate amid healthy DB funding levels.

Isio head of research and development, Iain McLellan, said while the flexibility would be welcomed, it begged the question of why so much detailed regulation was needed if it will have little impact.

Adding to this, Barnett Waddingham partner, Paul Houghton, warned that while many schemes are well-positioned, a "lingering lack of flexibility in the overall regime" was concerning, and may lead to increased costs and hinder innovation.

This was echoed by Association of Consulting Actuaries chair, Steven Taylor, who called for "less prescription in DWP's final regulations, to ensure that TPR's vision for scheme-specific bespoke funding is viable in practice."

TPR also provided a recent update on the DB landscape, with industry experts highlighting the regulator's data as evidence of a 'terminal decline' in private sector DB schemes.

The figures revealed that the number of active members in private sector DB and hybrid pension schemes has fallen 62.6 per cent in the past decade, with only 9 per cent of schemes still open to new members. It also showed that are 785,744 active private sector DB and hybrid scheme memberships in the UK as of March 2022, representing a 13.6 per cent year-on-year fall.

However, TPR's figures revealed a very different picture for the public sector, as the data showed that there were around 6.83 million active members in public sector DB schemes in 2021/22, down from 7.48 million in 2020/21.

This is in line with further insight into the DB landscape from the Pensions Protection Fund (PPF), which revealed that, for the first time, there are now more schemes providing no form of accrual of benefits than those that do, with 51 per cent of schemes closed to new members and new benefit accrual.

It also showed that the net funding position of defined benefit (DB) pension schemes improved to a surplus of £193bn in the year to 31 March 2022, amid the largest-ever annual fall in liabilities.

The PPF's *Purple Book* revealed that the aggregate funding ratio increased to 113.1 per cent from 102.8 per cent the previous year, primarily as a result of gilt market volatility driving down liability values, alongside large increases in equity values.

Written by Sophie Smith and Jack Gray

Regulator pushes back as LDI inquiries continue following market volatility

Parliamentary inquiries into the recent issues around liability-driven investment (LDI) and DB pension schemes have continued, although experts remain divided on the root causes of the issues, while the regulator rejected claims that it placed pressure on schemes to adopt LDI strategies. The Bank of England has also outlined recommendations around LDI going forward as part of its Financial Stability Report

The Pensions Regulator (TPR) chief executive, Charles Counsell, has rejected claims that the regulator put pressure on DB pension schemes to adopt liability-driven investments (LDI) when they didn't feel it was appropriate.

Speaking at a session at the Work and Pensions Committee (WPC) on DB schemes with LDI, WPC chair, Stephen Timms, explained that the committee had heard from some schemes that felt TPR had placed huge pressure on them to adopt LDI when it was not appropriate, also highlighting concerns raised to the committee that such pressure could increase with TPR's additional powers and penalties.

In response, Counsell said that he was not sure that he recognised the complaint.

"We don't put huge pressure on schemes or advisers," he said, continuing: "What we do is encourage them to manage the risks that they have got within their own individual scheme.

"It's important to state that the underlying basis is scheme specific. I don't recognise that we've put them under pressure. What we do is set out clear guidance and we expect them to take into account that guidance when they are looking at their specific circumstances.

"If we feel that schemes are not following the guidance we may well encourage them more strongly, but broadly we are expecting them to take their decisions that are appropriate for the particular circumstances of the scheme."

However, Counsell acknowledged that there were lessons to be learnt, explaining that whilst TPR had believed it had a reasonably robust response in place, "it's clear that the level of collateral wasn't sufficient for what happened".

He continued: "Sometimes you have to take judgements as a regulator about how hard you push pension schemes.

"Quite often we are accused of putting too much burden on our regulated community, and you have to take a view of how much is adequate and how much is too much."

He added that the regulator did not foresee the speed of the rise in gilt yields that happened at the end of September, recognising that, as a result of this experience, TPR will need to change the way the system works and look to ensure a more robust system.

"I think it's fair to say that we weren't collecting systematic data around this before this happened and, in retrospect, perhaps we should have, and going forward we will be," he noted. "How we will do that we haven't yet determined, but we are working on that at the moment."

Later in the session, Counsell also revisited the idea of regulating professional trustees, stating that TPR, for some time, has believed that pension schemes should have a professional trustee sitting on their board, but the reality was that the capacity of the professional trustee market did not match the number of schemes.

Pressed further as to whether he was recommending such a process, Counsell added: "I'm being slightly cautious about going that far because I realise there's a lot to do to get there, but I think there is a strong case for it."

Industry experts had previously suggested that trustee knowledge was a key issue in the recent liquidity issues, with Dalriada Trustees director, David Fogarty, telling the WPC that the cause of these issues was a "combination of things", including trustee board understanding as to what certain products are, the extent of leverage and what would happen if certain events happened.

Fogarty also argued that while TPR has met its statutory duty, "there is a reasonably strong argument for trustees to be regulated, to lift the bar in terms of the capability and understanding", querying whether there is currently a full understanding of the guidance being issued by TPR.

However, Barnett Waddingham partner and head of investment consulting, Rod Goodyer, warned that "not everybody can be brought up to the same level of understanding" on such complex issues, also stressing the need to maintain a diversity of thought.

"You'll have a diversity of skills across the trustee board in a whole range of areas, one of them might have legal skills, some of them might have finance skills, and you don't want to lose that diversity of thought within trustee boards," he continued. "There probably is also a challenge that not everybody can be brought up to the same level of understanding on the most complex issues facing trustees, of which investment is only one."

Broader disagreements over the root cause of the recent issues have also continued, with industry experts sharing mixed views when the WPC asked about recent concerns raised around hidden leverage, with experts clarifying that details can typically be found in the public domain via, for instance, statement of investment principles.

The WPC also asked about previous comments from the Bank of England (BofE) that suggested the recent issues were due to poorly managed leverage, with the panel only "partially" agreeing.

"I don't agree that that was the primary cause," Insight Investment CEO, Abdallah Nauphal, stated, arguing that the issue "was a confluence of factors that came together that created this very unique event".

"We need to recognise how jittery the markets were with regard to the long-term outlook for the fiscal position of the UK, at a time when the BofE was ready to start unwinding quantitative easing (QE)," he stated, explaining that the market turned from "jittery to panic" based on rumours and the subsequent confirmation of the mini-Budget.

"There is a clear need for urgent and robust measures to fill regulatory and supervisory gaps to reduce risks to UK financial stability, and to improve governance"

Moving on from the root causes of the recent issues, the BofE has recently outlined recommendations for the future as part of its *Financial Stability Report*.

In particular, it recommended that TPR, in co-ordination with the Financial Conduct Authority (FCA) and overseas regulators, take regulatory action to ensure LDI funds remain resilient.

In its report, the BoE's Financial Policy Committee (FPC) called for regulatory action as an interim measure to improve LDI funds' resilience to the higher level of interest rates that they can now withstand, and DB pension trustees and advisers ensure these levels are met in their LDI arrangements.

Following this, the FPC said that regulators should set out appropriate steady-state minimum levels of resilience for LDI funds, including on operational and governance processes, and risks associated with different fund structures and market concentration.

Additionally, the FPC called for further steps to be taken to ensure regulatory and supervisory gaps are filled, in order to strengthen the resilience of the sector.

It welcomed TPR's recent guidance as a first step in maintaining financial and operational resilience, also welcoming the recent statements by the FCA and overseas regulators.

"This episode demonstrated that levels of resilience across LDI funds to the speed and scale of moves in gilt yields were insufficient, and that buffers were too low and less usable in practice than expected, particularly given the concentrated nature of the positions held in the long-dated gilt market," the report stated.

"While it might not be reasonable to expect market participants to insure against the most extreme market outcomes, it is important that shortcomings are identified and action taken to ensure financial stability risks can be avoided in future.

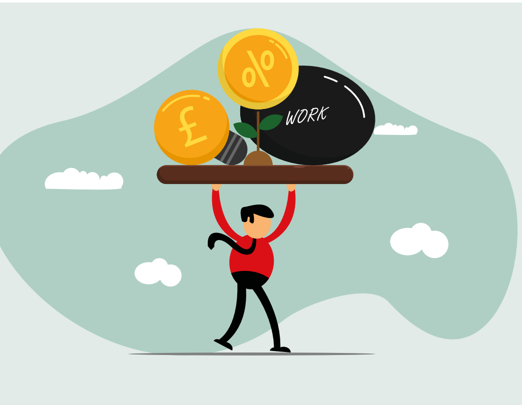
"There is a clear need for urgent and robust measures to fill regulatory and supervisory gaps to reduce risks to UK financial stability, and to improve governance and investor understanding."

Commenting in response to the FPC's recommendation in a WPC hearing, Counsell said: "We welcome the statement that the FPC made. What we have done is put in measures that are resilient for now, but we need to think about what the longer-term measures might be.

"Our intent is therefore to look at what those measures might be and our intent is to do that via a funding statement in April of next year.

"What we need to look at longer term is what happens if interest rates go up, if interest rates go down, and what levels of collateral should be in place. So, we will be looking at those medium- to longer-term implications."

Written by Jack Gray and Sophie Smith



TPR and FCA update joint regulatory statement

The Pensions Regulator and the Financial Conduct Authority (FCA) have issued an update to their joint regulatory strategy, in light of a "changing pensions landscape". The FCA has also taken enforcement action in relation to the British Steel Pension Scheme, and revealed plans to review compensation limits for pension claims

The Pensions Regulator (TPR) and the Financial Conduct Authority (FCA) have issued an update to their joint regulatory strategy, emphasising the importance of a collaborative approach in the current environment.

The update identified eight joint workstreams: Productive finance, value for money, a regulatory framework for effective stewardship, pension scams strategy, defined benefit (DB) transfer advice, DB schemes and transfer activity, pensions dashboards and supporting consumer decision-making throughout the pensions consumer journey.

TPR and FCA highlighted the eight joint workstreams as demonstration of a "fundamental shift" in recent years in the working relationship between the FCA and TPR where the two are now working "hand-in-hand".

The update also divided the ongoing work between the regulators into three parts: The joint assessment of risk and harms, such as the work to tackle pension scams through the Pension Scams Action Group; joined-up working on cross-sector initiatives such as pensions dashboards and value for money; and joint communications around DB transfer concerns.

"On areas of joint strategic interest – recognising our different frameworks – where appropriate we will consider from the outset how we will work jointly, whether through consultations, communications, supervisory approaches or new regulations, developed in partnership with the DWP," the update continued. "It is only by working seamlessly together as one regulatory family, in collaboration with industry, that we can deliver the consistent regulation and outcomes that the public expect."

Although the regulators acknowledged that they cannot directly address adequacy concerns, the update emphasised that TPR and FCA are committed to working with all stakeholders, including government, to support savers to achieve good outcomes.

"We have been hit with a global pandemic, faced war tragically returning to Europe and seen the return of high inflation and higher interest rates and a cost-of-living crisis"

The update also suggested that this co-ordinated action is particularly important in the current macroeconomic environment, warning that the challenges of the ongoing cost-of-living crisis could change saver behaviour, with some potentially reducing contributions.

In a blog post, TPR chair, Sarah Smart, emphasised that although the past four years saw an increase in retirement savings, "we have been hit with a global pandemic, faced war tragically returning to Europe and seen the return of high inflation and higher interest rates and a cost-of-living crisis".

In related news, the FCA has also provided an update on ongoing enforcement action in relation to the British Steel Pension Scheme (BSPS), revealing that it has fined Pembrokeshire Mortgage Centre (PMC) Limited, currently in liquidation, £2.35m for unsuitable advice to transfer out of the BSPS and other DB pension schemes.

The firm advised 420 consumers, nearly two-thirds of whom were BSPS members, on whether to transfer out of their DB scheme. Overall, 93 per cent were advised to transfer, with PMC earning over £2m in transfer and ongoing advice fees. Based on this, the FCA estimated that PMC gave unsuitable advice in 60 per cent of cases, even higher than BSPS as a whole.

The FCA is also continuing to progress around 30 ongoing enforcement investigations into firms and individuals relating wholly or partly to BSPS advice, all of which are at a "very advanced stage", while some are in litigation.

Alongside this, the FCA has announced plans to review the Financial Services Compensation Scheme's (FSCS) compensation limits for pension claims.

Any proposed changes to the compensation rules are expected to be consulted on during 2023/24, with a view to confirming any changes by the end of that financial year.

Written by Sophie Smith and Jack Gray

Govt consults on 'major' NHS Pension reforms

The Department of Health and Social Care has launched a consultation on 'major' changes to the NHS Pension Scheme, in an attempt to address the NHS backlog and ease waiting times by retaining existing staff, and allowing retired staff to return to work

The government has launched a consultation on plans to amend NHS pension rules in an effort to retain staff and remove barriers for those returning staff, although it has not announced any changes to the lifetime or annual allowance.

The consultation from the Department of Health and Social Care (DHSC) is seeking views on new plans designed to allow retired and partially retired staff to return to work or increase their hours without having payments to their pension reduced or suspended.

As part of this, the DHSC has outlined plans to introduce a new partial retirement option to support older staff who want to work more flexibly and enable them to access part of their pension whilst continuing to contribute to their pension pot.

The proposals also look to allow staff to claim a portion or all of their pension benefits but continue working and contributing to their pension.

This includes plans to remove the limits on hours recently retired staff can work to give them better control over the hours they work in the first calendar month after returning.

The proposals also aim to fix the unintended impacts of inflation, and ensure senior clinicians aren't taxed more than is necessary, by enabling skilled and experienced staff to continue to contribute to the NHS up to and beyond retirement age.

This, in turn, is expected to mean that more clinicians are able to provide appointments, ease winter pressures and deliver care to patients, as well the retention of crucial knowledge and experience to ensure patients are receiving first class care.

In particular, the DHSC is consulting on plans to ensure senior clinicians have more headroom against the £40,000 pension tax annual allowance, in an effort to ensure that senior doctors are either less likely to receive a tax charge, or will receive a smaller tax charge, in turn reducing the likelihood of early retirement.

"The generous NHS Pension Scheme is one of the best in the country, but it's not working as it should for everyone"

The consultation will run for eight weeks, with the reforms expected to be implemented in late spring 2023.

Commenting on the proposed changes, Health and Social Secretary, Steve Barclay, stated: "The generous NHS Pension Scheme is one of the best in the country, but it's not working as it should for everyone. We need a system where our most experienced clinicians don't feel they have to reduce their workload or take early retirement because of financial worries. I also want to make it easier for staff that want to return to work to support the NHS to be able to do so without penalties."

However, British Medical Association (BMA) pensions committee chair, Dr Vishal Sharma, warned that, on the face of it, the proposed changes "appear to be too little, too late", explaining that while they implement some of the immediate mitigations that the BMA has been calling for, they fall "well short of the long-term solution that the NHS desperately needs".

He continued: "It is essential that the government addresses the anomaly of negative pension growth, which has a disproportionate impact on the public sector, due to unintended consequences of the public sector pension reforms.

"Unless addressed, this will have a huge detrimental impact on the NHS, particularly if the government follows through with its threat to impose further sub-inflationary pay awards."

Work on the NHS Pension Scheme McCloud remedy has also been progressing, as HM Treasury has shared the Treasury Directions for the Public Service Pensions and Judicial Offices Act 2022, which will allow the government to consult stakeholders ahead of the 1 October 2023 'go live' date for the McCloud remedy.

Despite initial expectations that the remedy would be delivering immediate detriment cases during 2021-22, it was recently confirmed that the McCloud remedy for the NHS Pension Scheme had been delayed, with a new 'go live' date of October 2023 confirmed following "continued delays in the production and release of a suite of Provision Definition Documents (PDD) from HM Treasury".

Written by Sophie Smith

Editorial credit: Abdul N Quraishi - Abs / Shutterstock.com

BA ends DRCs following funding improvements

British Airways has confirmed that it does not expect further contributions to the New Airways Pension Scheme (NAPS) to be required for the foreseeable future, following a "considerable" improvement in the scheme's funding level, as a result of the recent volatility. The triennial valuation supersedes the previous agreement with the trustee, which allowed the group to defer £450m deficit recovery contributions previously due in October 2020 and September 2021

British Airways (BA) has confirmed that it is not expecting to make contributions to the New Airways Pension Scheme (NAPS) for the foreseeable future, following considerable improvements in the scheme's funding level.

Its latest triennial valuation revealed an agreed technical provisions deficit of £1.65bn as of 31 March 2021, down from £2.4bn in March 2018, which was primarily attributed to the £1.3bn in contributions made by BA.

BA also revealed that the funding level of the scheme has "considerably improved" since 31 March 2021, to the extent that NAPS was in surplus on the same basis as the 2021 valuation.

According to BA, this improvement in funding was in large part due to the increase in UK government bond yields, which increased the discount rate applied to pension liabilities, alongside positive relative returns from the scheme's asset portfolio.

As a result, BA is not expecting to be required to make contributions to NAPS for the foreseeable future, thanks to its overpayment protection mechanism.

However, the company agreed to provide property assets as security, to remain in place until September 2028.

The overpayment protection mechanism, which was initially agreed at the 2018 valuation, was amended as part of the 2021 agreement, with monthly deficit contributions to be suspended if the funding ratio on a technical provisions basis reaches 100 per cent.

Should the funding ratio fall below 100 per cent, however, BA must begin making monthly contributions until funding returns to at least 100 per cent.

The schedule of these contributions will be at a rate of £50m per year up to June 2023 and increasing by £50m each year up to June 2026 and then capped at £225m per year from July 2026.

The 2021 valuation agreement also confirmed that BA will not pay a dividend in 2022 and 2023 and there will be a 50 per cent matching contribution to NAPS if any dividend is paid in 2024.

Written by Sophie Smith

NEWS IN BRIEF

Smart Pension announced its first green bonds investment with the Mirova Global Green Bond Fund. It is thought to be among one of the first master trusts to invest its default growth fund in green bonds.

Moneyhub secured a further £15m in funding from Phoenix Group. This funding completed Moneyhub's £55m largest fundraise to date, totalling £55m, following the £35m in funding announced in October from Legal & General and Lloyds Banking Group, with an additional £5m debt facility provided by Shawbrook Bank, partially subject to regulatory approval.

Digital communications agency **Landscape** has merged with creative agency **Making Giants**, after "several years" on parallel paths in the financial wellbeing, pensions and benefit communications world.

New guidance on good workforce reporting was published by the **Pensions and Lifetime Savings Association** (PLSA), Railpen, the Chartered Institute of Personnel and Development (CIPD), the High Pay Centre and Board Intelligence, in an effort to "assist companies looking to improve their reporting, and support investors in their engagements with portfolio companies".

The **Pensions Management Institute** formed a new partnership with the Chartered Institute of Payroll Professionals (CIPP). The agreement aims to support membership growth and deliver enhanced value to members of both organisations and will run for an initial trail period of one year from 1 January 2023.

Arthur J. Gallagher & Co has agreed to acquire the partnership interests of BCHR Holdings, **Buck**, for a gross consideration of $660m (£543m), subject to regulatory approval. The acquisition is expected to close during the first half of 2023.

Diary: January 2023 and beyond

ABI Annual Conference 2023
21 February 2023
155 Bishopsgate, London

The ABI Annual Conference 2023 will explore the value and contribution of the insurance sector to society at large, against the current backdrop of economic and political turbulence. The sessions at the conference will explore the impacts of the digital and data revolution for the sector and how the sector must respond to changing customer demand.

For more information, visit:
https://www.abi.org.uk/events/abi-conference-hub/

Pensions Age Awards 2023
21 March 2023
Great Room, Grosvenor House, Park Lane, London

The Pensions Age Awards, celebrating their 10th successful year, aim to reward the pension schemes and the pension providers across the UK that have proved themselves worthy of recognition in these increasingly challenging economic times The awards are open to any UK pension scheme or provider firm that serves UK pension schemes.

For more information, visit:
https://www. pensionsage.com/awards

PLSA Investment Conference
6-8 June 2023
EICC, Edinburgh

The Pensions and Lifetime Savings Association's (PLSA) Investment Conference returns to Edinburgh in 2023. The conference is where CIOs, trustees, investment board members, pension managers, finance professionals and their advisers gain insight on the major trends and events affecting UK investors and markets, bringing the UK pensions investment chain together.

For more information, visit:
https://www. plsa.co.uk/Events/Conferences/Investment-Conference

European Pensions Awards
6 July 2023
London Marriott Hotel

The European Pensions Awards were launched to give recognition to and honour the investment firms, consultancies and pension providers across Europe that have set the professional standards in order to best serve European pension funds over the past year. The awards are free to enter and open to any pension fund or firm which serves European pension funds.

For more information, visit:
https://www.europeanpensions.net/awards/

Visit www.pensionsage.com for more diary listings

Month in numbers

£209.3m

The Department for Work and Pensions (DWP) has repaid a total of £209.3m to individuals impacted by historical state pension underpayments as of 31 October 2022, having identifed 31,817 people who were affected by the issue. The problems affected married women whose husbands reached pensionsable age before 2008, as well as widows and those over 80, who were unkowingly entitled to an "enhanced pension" that could have improved their pension by up to 60 per cent.

15%

More than one in seven (15 per cent) pensioners over the age of 65 have unretired as a response to the current cost-of-living crisis, according to research from Standard Life.

8.6 million

More than 8.6 million people from 'under-pensioned' groups are now missing out on workforce pensions saving, research from Now Pensions found.

VIEW FROM THE SPP: Income solutions for the new retirement

The Covid pandemic caused many people to re-evaluate their work/life balance and may change the way that people retire. Nearly 400,000 50-59 year olds left the UK labour force after the pandemic. Among these people, the most important factor when considering returning to work is flexible working hours.

For many in their late 50s and 60s, partial retirement may be attractive, combining part-time paid work with more leisure time. Hybrid retirement income solutions – which offer flexible access to savings combined with secure income – could support this. Members would have the ability to drawdown their savings flexibly in the early years of retirement when there is more variability in work and spending, while also having a guaranteed income, such as an annuity, to provide security and longevity insurance.

Whilst annuities have in recent times often been perceived as 'bad value', annuity rates have seen a sharp increase over the past year in line with rising bond yields. This may lead to greater improved perceptions of value, especially if the annuity is combined with flexible access to remaining savings in a hybrid strategy.

Whilst the days of compulsory annuitisation are behind us, perhaps guaranteed income still has a place in solutions to support the new retirement.

SPP DC committee member, Olivia Kennedy

THE SOCIETY OF PENSION PROFESSIONALS
making pensions work

Appointments, moves and mandates


Tegs Harding

Legal & General has appointed Tegs Harding as a new trustee and chair of the L&G Mastertrust Investment Committee. Harding is a professional trustee at Independent Trustee Services (ITS), and has more than 15 years' experience in the finance industry. She is also a qualified actuary, and member of the Association of Professional Pension Trustees (APPT) Committee on Responsible Investment and Climate Change. Harding replaces BESTrustees Limited's Catherine Redmond, who has stepped down from her role on the board, and her position as Investment Committee chair, after serving the L&G Mastertrust as a trustee for the past three years.

SEI has announced the appointment of Natalie Winterfrost as the new trustee director for the SEI Master Trust. Previously Law Debenture director, Winterfrost has more than 25 years' experience in investment consulting and asset management, and has helped large pension schemes address complex investment issues, including environmental, social, and governance (ESG) and Task Force on Climate-related Financial Disclosures (TCFD). The role will see Winterfrost working collaboratively with the existing trustee board, with her role described as "fundamental" in helping SEI improve the retirement outcomes for its membership. Winterfrost commented: "I look forward to leveraging my investment and asset management experience to bring enhanced value and focus to delivering better retirement outcomes for the SEI Master Trust's members."


Philip Parkinson

Mercer has appointed Philip Parkinson as its new investments and retirement leader in the UK, subject to approval from the Financial Conduct Authority. Parkinson will oversee Mercer UK's Investments and Retirement business strategy across DB pensions, DC pensions, and other growing segments such as Financial Institutions and Endowments and Foundations. He has held various roles during his time at Mercer, most recently leading the DC segment of Mercer's UK Wealth business, including both consulting and product solutions. He takes over the role from Benoit Hudon, who will concentrate on his role as president and CEO of Mercer UK.


Alexis Parrish

Isio has announced the appointment of Alexis Parrish into the newly created role of head of benefits technology.
Parrish brings over 20 years' experience to the role and joins the team from KPMG, where she led its benefits consultancy and technology business for eight years.
The news also follows the appointment of Steve Robinson as a partner into its Insurance and Risk Settlement team. Robinson previously held senior positions at Aviva and Scottish Widows, most recently as financial and insurance risk director. In his new role, he will work closely with Isio head of insurance, Nick Johnson, on developing Isio's existing offering.


Nausicaa Delfas

The Pensions Regulator (TPR) has announced the appointment of Nausicaa Delfas as its next chief executive. Delfas, who will start in the role at the end of March 2023, joins the regulator from her current role as the Financial Conduct Authority executive director of governance. In her new role, she will lead TPR as it looks to implement a raft of initiatives designed to improve outcomes for savers, including pensions dashboards and the new Defined Benefit Funding Code. In addition to this, the regulator highlighted ongoing work around value for money, ensuring automatic enrolment continues to be a success, and tackling criminal activity as key focuses for Delfas in her new role. Delfas will take over the role from Charles Counsell who previously announced he would not be seeking a second term.
The appointment was welcomed by TPR chair, Sarah Smart, who commented: "I am thrilled to appoint Nausicaa Delfas to the role at a time when the pace of change in the pension industry shows no sign of slowing. Nausicaa has a proven track record of delivering transformational change, and her background in governance will be vital as we ensure those who deliver pension savings are meeting the challenges of new legislation, and as we continue to improve our effectiveness by becoming a more data and technology-led organisation. I am confident Nausicaa will put value for money, equality and diversity and a determination to tackle wrongdoing at the core of her priorities to help us fulfil our commitment to protect savers and develop as an organisation fit for the future."

Standard Life, part of Phoenix Group, has appointed Equiniti to carry out administration of both buy-in and buyout bulk purchase annuity policies.
Under the appointment, Equiniti will provide a full administration offer designed to meet the needs of both customers and trustees, including delivering self-service portal. This portal, which will use Standard Life branding, will aim to allow customers to benefit from greater flexibility in how they engage with their pension. Customers will be able to digitally access features such as a retirement modeller allowing real-time modelling of retirement options, instant indicative transfer value and access to a wide range of information to help understand their policy and make important decisions on their retirement journey. Customers will also have the option to go paperless and view all documents within the portal, although a fully staffed telephone option will also be available. The service is in the process of being implemented and is on track for an incremental roll-out for consumer use across 2023. Commenting on the appointment, Standard Life head of client service - annuities, Mark Fenlon, stated: "With Equiniti's market leading technology and substantial experience in the DB administration market, we are confident that our partnership will help us provide a customer-centric proposition that meets the needs of trustees, as well as ensuring good outcomes for customers who are at the heart of the service. We are delighted to have Equiniti on board as an administration partner to provide support in this specialist area, and we look forward to working in partnership with them to continue developing the proposition in the future."


Dan Mould

K3 Advisory has announced the appointment of Dan Mould as actuarial consultant. Based near Leeds, Mould will work with the team on delivering K3 Advisory's current buyout annuity transaction pipeline. Alongside this client work, Mould will have responsibility for developing and maintaining the firm's actuarial models, such as the newly launched small scheme index. Prior to this, he held roles at both KPMG and Isio. Commenting on the appointment, K3 managing director, Adam Davis, stated: "It is an exciting time for K3, we have a clear plan for long term growth in place and investing in first class individuals is a key part of that."


Jim Islam

People's Partnership has appointed Jim Islam as its new chair of board.
He has been part of the board since 2018 and took up his new position on 1 January 2023. A qualified actuary, he brings extensive board level leadership experience to the role, having previously held senior finance and general management roles at a number of organisations. Islam succeeds Babloo Ramamurthy, who is stepping down after nearly a decade in the role. "There is a very exciting future ahead for the organisation, and I am delighted to hand over to Jim as the new chair of People's Partnership, to continue to deliver our purpose to help people build better financial foundations for life," Ramamurthy stated.


Ziad Abou Gergi

Hargreaves Lansdown has named Ziad Abou Gergi as head of its multi-manager team. Gergi has around 20 years' experience in the multi-manager area and he had already joined Hargreaves Lansdown in December 2021. Prior to joining the Hargeaves Lansdown, he headed Barclays' high net worth multi-asset team. In his new role, Gergi will be responsible for overseeing the management of 11 multi-manager funds in the fund of managers range. Commenting on his appointment, Gergi stated: "I look forward to continue to build on our success story and strengthening our proposition for the benefit of our clients."


Dana Grey

The **Pension Protection Fund (PPF)** has appointed Dana Grey as chief risk officer. The new role will see her lead both the risk and compliance teams, having been acting as interim risk director since October 2021. Grey initially joined the PPF in 2009, most recently leading the legal and compliance team, and brings extensive knowledge and experience to the executive committee. Since joining the lifeboat, she has also been active in the PPF's diversity and inclusion efforts, having been chair of the PPF's Diversity and Inclusion Sponsorship Group and as co-lead of the Race Action Group since 2018. Grey is also co-founder of the Inspiring Women network group.

View from the AMNT: Hope for a better year

We enter the New Year with a renewed spring in our step, usually with the phrase, 'well things can't be as bad as last year' hovering on our lips. Given, as I write, the present scheduled industrial action then the phrase may have a hollow ring.

At least in the pensions industry, we start with a stable financial position following the recent market turmoil. Long-term financial planning is particularly important for pension funds and its members who need to be confident that any future shocks; and I'm sure there will be unforeseen situations, are not precipitated by poor decision making.

We have seen where poor governmental decisions lead and we have also seen where poor regulatory control can lead; with the FCA launching plans to compensate members in the British Steel Pension Fund who received poor financial advice leading to the loss of pension earnings. Also, the FCA will temporarily ban the firms that gave inappropriate advice from paying dividends or giving bonuses to directors in order to ensure they do not shift monies out before compensation is made.

The pension dashboards, to be launched this year, will provide pension members with better information, but will it lead to better decision making, or will the nature and provision of advice become the next 'unforeseen' shock?

AMNT member, Stephen Fallowell

AMNT Association of Member Nominated Trustees

View from the PLSA: Pay Your Pension Some Attention

In 2022, the unexpected collaboration of grime music and pensions arose from the industry's recognition that more should be done to address the fact that savers' confidence and understanding of their pension remains too low. Over half the public struggle to find their pension information and only 20 per cent are confident they are saving enough for retirement.

We gave grime artist, Big Zuu, 24-hours to compose a track urging listeners to Pay Your Pension Some Attention.

And the early signs are that the campaign has had some broad success that is worthy of some celebration.

In a campaign awareness survey of the public after the engagement season, 19 per cent of respondents said they could recall seeing the campaign – a very strong figure for a campaign of this scale. Of those, a staggering 91 per cent took action as a result. It means, a potential three million savers were inspired to go and pay their pension some attention.

We showed savers that learning pensions basics is easy and with small steps, like updating personal details, they can gain confidence in their pension saving.

The campaign team is already looking to next year and has identified areas where we can have an even bigger impact.

We recognise that it takes time to build a brand. Future efforts will therefore likely continue with the Pay Your Pension Some Attention brand and slogan. We will also give the industry more material and campaign assets to share through their own channels to widen the reach and breadth of activity.

PLSA director policy and advocacy, Nigel Peaple

PENSIONS AND LIFETIME SAVINGS ASSOCIATION

View from the PMI: CDC schemes

The slow pace at which collective defined contribution (CDC) schemes are developing in the United Kingdom may lead some to conclude that this scheme design has been a failed experiment. However, CDC has the potential to become the most significant change in workplace pension provision for a generation.

Currently, CDC schemes can only be used for single large employers. Whilst the Royal Mail remains the only sponsor to have formally committed to this design, rumours persist that other employers are considering their options for the future. However, a significant change would be legislation to allow CDC to move into what many regard as its natural home: The master trust sector.

A CDC master trust would allow the automatic enrolment principle of defaults to apply to all stages of membership. Currently, conventional DC schemes facilitate defaults to apply to both the induction and accumulation phases of membership. However, members are required to make life-changing decisions at the point of decumulation. CDC avoids this by providing – by default – a lifetime income at the point of retirement. CDC also offers a truly equitable approach to risk sharing in a way that is simply not possible with traditional DC.

CDC has many detractors, but it has the potential to solve many of the problems currently associated with workplace pension provision. Given this design's proven success elsewhere in Europe, it deserves to be properly considered in the UK too.

PMI director of policy and external affairs, Tim Middleton

A year in review and looking forward to 2023

Phil Brown looks back at an eventful 2022 and considers what's in store for the year ahead

With war in Europe and political turmoil and economic hardship at home, 2022 was a tough year. Pension schemes and those saving into them were buffeted by the economic impacts of the invasion of Ukraine and the economic fallout of the pandemic. As a result, schemes and savers are now grappling with both generationally high inflation and sharp falls in both bond and equity markets.

In terms of the macro-environment for DC saving, the Office for Budgetary Responsibility forecasts a fall in real household disposable income of 7 per cent over the next two years[1]. This will take household incomes back roughly to their 2013 level. As lower income households spend more of their money on essentials like food – where price increases have been particularly sharp – they will be the worst affected. The government's energy price cap on unit prices will only partially offset this.

This has yet to really pass through into pensions policy or pensions saving. So far, there have been small increases in the opt-out rate from auto-enrolment – from 7.6 per cent to 10.4 per cent between January 2020 and August 2022 – and no increases in the cessation rate[2]. Our own research shows that just 4 per cent of UK pension savers surveyed would consider stopping their pension contributions in the next 12 months. A further 4 per cent would think about reducing how much they save into their pensions over the next year. This is compared to 35 per cent who said there's a possibility they would reduce their holiday spending in the next 12 months. This may change in 2023 but, so far, pensions policy has remained surprisingly resilient. While the cost-of-living crisis has not yet affected the running of auto-enrolment, it has likely seriously affected its future. There is no plan for the implementation of the 2017 review reform package; reducing the age threshold for auto-enrolment from 22 to 18 and removing the lower earnings threshold on contributions. It's hard to see how the government can implement changes to auto-enrolment during an economic crisis of this sort. The government and the wider pensions industry can, though, use the time to prepare the ground for reform once the crisis has passed.

Dashboards project reaching its critical phase

Despite these challenges, the DC sector has made steady progress on other longstanding priorities. 2022 has been the year the DC sector began to really get to grips with pensions dashboards. The trajectory for dashboards is now set with the pensions dashboards regulations approved by parliament[3]. It's now really a case of schemes getting ready to connect to the dashboard system from April.

We expect the same sort of steady progress in 2023. DWP has signalled its intention to publish new value for money metrics that may change how DC schemes and products are judged, initially by pension professionals but ultimately by consumers. We expect a further round of discussion about how and whether deferred small pots should be consolidated. And we expect more activity on the issue of schemes investing in less-liquid assets, following the publication of the Productive Finance Working Group's guides[4] to the issue in late November. DWP has also indicated that it will consult on extending collective DC to multi-employer schemes. Lawyers and compliance teams are going to be busy.

The future remains bright

So, 2023 is set to be another challenging year. We expect to see incremental progress on longstanding pension priorities but in a tough economic and political climate. We are, though, looking forward to seeing a working pensions dashboard and, perhaps, the first attempts to consolidate small, deferred pension pots. It's through this sort of incremental progress that the UK will build better engagement with DC pensions and a healthier workplace pensions market. We remain optimistic about the UK DC sector and the long-term value of workplace pension saving.

Written by Phil Brown, director of policy and external affairs at People's Partnership – provider of The People's Pension

[1] Economic and fiscal outlook - November 2022 - Office for Budget Responsibility (obr.uk)

[2] Ten years of Automatic Enrolment in Workplace Pensions: statistics and analysis - GOV.UK (www.gov.uk) *All figures, unless otherwise stated, are from YouGov Plc. Total sample size was 2,055 adults, of whom 1,370 had a pension and/or investment for retirement. Fieldwork was undertaken between 11th - 14th November 2022. The survey was carried out online. The figures have been weighted and are representative of all UK adults (aged 18+).*

[3] The Pensions Dashboards Regulations 2022 (legislation.gov.uk)

[4] PFWG Guides – Investing in Less Liquid Assets.pdf (theia.org)

VIEW FROM TPR: Protecting savers in 2023

I'd like to start the year by welcoming Nausicaa Delfas to the role of chief executive for TPR.

Nausicaa will take the helm in April 2023 when I step down at the end of March after a four-year tenure in the role.

In our strategy we published two years ago, we put the saver at the heart of our work. I believe value for money (VfM) is integral to delivering a pension system that works for savers. A major milestone early in the year will be a joint consultation with DWP and FCA on our VfM framework.

At the end of last year we launched our second draft Defined Benefit Funding Code consultation package. Long-term funding remains a key tenet of the code, which reflects regulations from DWP and views from across industry. The industry has until 24 March to respond, which will give us just enough time to ensure the code can be in place and commence in October.

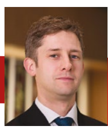
This year will also see exciting developments for pensions dashboards. Our consultation on our dashboards compliance and enforcement policy closes on 24 February so there is still time for industry to have their say. We aim to publish the final policy in spring 2023.

Promoting equality, diversity and inclusion within TPR and across the industry will remain a core priority for us in 2023, and we will continue to drive towards the delivery of our equality, diversity and inclusion strategy.

Finally, following a number of successful prosecutions in 2022, we will continue to be tough on scammers and tough on those who fail to treat savers fairly or ignore their automatic duties. We stand ready and willing to use our powers.

TPR CEO, Charles Counsell

The Pensions Regulator
Making workplace pensions work



VIEW FROM THE ABI: The Edinburgh Reforms

The Edinburgh Reforms announced in December attracted attention as a deregulatory package, but there's more to it than that. One set of announcements that pensions people should look at is the reform of retail investment disclosure.

The proposed reforms include repealing regulation on disclosure around packaged retail and insurance-based investment products (PRIIPs), and aligning this with other regulation. It also includes scrapping the requirement to tell customers if their portfolio has fallen by 10 per cent or more. Without context or reassurance, this kind of rule would do more harm than good.

Perhaps most importantly, is it consulting on a new direction for disclosure. The FCA has issued a simultaneous discussion paper alongside the Treasury consultation.

These are welcome moves and will help savers make sense of financial services. But a more flexible and innovative approach for investments could be undermined by a more rigid approach for pensions, especially when a customer sees both, on paper, on their investment platform or on their pensions dashboard's post-view services. It also raises questions about the purpose of, and audience for, various pensions disclosures. Aligned regulations, simpler communications and flexible formats are the way forward.

ABI assistant director, head of long-term savings policy, Rob Yuille

ABI

VIEW FROM THE PPI: Managing pensions policy design trade-offs

Following the 2021 publication of system design series reports, November 2022 saw the publication of the first in a series of annual reports on the PPI's *UK Pensions Framework*. Its headline finding was "the process of improving financial sustainability in the UK pension system may be compromising living standards in retirement". How has that come about?

Analysis of over 40 framework indicators showed that many of today's pension system outcomes are the product of intended and unintended consequences of structural change. Changes including the shift from defined benefit to defined contribution, and the transfer of responsibility for earnings-related saving from the state to employers, have largely come about in response to financial risks associated with population ageing and macroeconomic change. Together, their effect has been to drive a gradual pattern towards increased personal responsibility for retirement outcomes. In doing so, they reduce the cost of providing pensions, but shift market risks away from the government and employers, and onto the individual.

Changes also demonstrate a continuously evolving relationship between adequacy and sustainability in the system, and highlight the importance of policy interventions that can moderate trade-offs in a way that is deemed to be fair. Perhaps one of the most important conclusions from the work however, is the importance of building consensus across the pensions community over how to achieve them.

PENSIONS POLICY INSTITUTE
PPI

PPI research associate, Anna Brain

Royal London Asset Management (RLAM) head of sterling credit research, Martin Foden, and senior fund manager, Shalin Shah

Pension portfolios – the role of asset-backed securities

Laura Blows is joined by Royal London Asset Management (RLAM) head of sterling credit research, Martin Foden, and its senior fund manager, Shalin Shah to discuss the role of asset-backed securities (ABS) within pension fund portfolios

"Post the 2008 financial crisis, ABS is often seen as just focusing on securitisation," RLAM head of sterling credit research, Martin Foden, states. However, for RLAM, "it's absolutely about picking the best of both worlds in terms of secure corporate bonds, but also securitisation", he reveals in the *Pensions Age* podcast, *The role of asset-backed securities*.

"RLAM looks for effective security, which it is able to enforce if the issuer or company gets into trouble. It's really important you have effective covenants that interact with the security, which often gives us early warnings before default, for us to engage with the issuer and intervene to support our lending position. It's also really important that the collateral is of a high quality as well," he explains.

Also important to understand is the possibility of ESG analysis of ABS products. "The integration of ESG into ABS research and investment is no different than integration into other forms of corporate bond investing," Foden says.

"However, there are some specific characteristics of corporate bonds that make it slightly more difficult in terms of *[ESG analysis]* implementation. Coverage from third-party data providers are generally very low, because their origins tend to be in the equity market," he states.

"Our solution to that is to have a really high quality experienced in-house responsible investment team collaborating with the credit analysts and fund managers," he adds.

Discussing on the podcast whether ABS bonds are less liquid than unsecured corporate bonds, is RLAM senior fund manager, Shalin Shah, who notes no real difference between the liquidity of senior larger issue size ABS bonds and unsecured bonds.

Most ABS products are highly exposed to end consumer risk though, three consumer-led areas – autos, credit cards and mortgages – he adds.

"If you buy a typical specialist ABS fund, you may think you're getting diversification, but actually, you're very exposed to end consumer risk. This is unlike a more diversified ABS approach that we undertake, which includes a larger exposure to corporate bonds with additional security backing our claim," Shah states.

The senior securitisation structure will typically be rated AAA, meaning the AA piece will be a junior part of that capital structure. It will have a secondary claim on the assets that are being secured.

"We think that's really important to understand from a risk point of view," Foden says, "because as economic clouds are gathering and concerns around asset values are increasing, if the value of the assets you're secured on decreases, those junior pieces take those losses very, very quickly; the margin for error of going from total recovery to full loss is very, very narrow. It's only in that most senior AAA piece, which is where we choose to invest, that you have a much greater margin for error as asset values start to fall.

"As well as subordination, Shalin *[Shah]* talked about the concentration risk. Rating agencies often rate for 40 or 50 years in the future, whereas when an investor buys one of those junior pieces, they feel they're in a very short-dated bond.

"So, not only do you potentially have a concentrated exposure, a subordinated exposure, but also you can have a much longer exposure to that risk than you may realise," Foden explains.

However, according to Shah, there are a lot of opportunities within secured bonds, as well as securitisations.

"Many investors may just focus on senior unsecured bonds, but our experience has taught us that a senior unsecured claim on a business may turn junior.

"Therefore, when we invest, we have a much larger weight within our corporate bond funds in secured bonds, where you cannot sacrifice yield, but imbed a significant downside protection by being senior in the capital structure and looking at the specifics of the covenant," Shah says.

"By looking at the best of both worlds, really combining secured corporate funding with securitisations, you can potentially access really attractive yields at the present time, especially given the moves we've seen in spreads and underlying government bond yield," he adds.

To listen to the podcast, please visit www.pensionsage.com

Soapbox: Flying under the radar

The new year is here and with it brings a whole host of traditions, such as New Year's resolutions, accidentally saying the previous year for the first couple of months and planning for the year ahead. The pensions industry has been known for its planning, with former Secretary of State for the Department for Work and Pensions (DWP) Thérèse Coffey declaring 2023 as "the year of the trustee". In this spirit, I would like to humbly submit that 2023 should also be considered "the year of the dashboard" as much work on the long-expected pension dashboards should be completed in the coming 12 months.

Dashboards have been the most intriguing idea I have seen since joining the pensions industry a year ago and, as the completion of the dashboards draws closer, it is certainly an exciting time for the industry, but you can imagine my surprise when everyone outside the pensions industry I mentioned the concept to had no idea what I was talking about.

Although there has been a degree of ignorance when it comes to dashboards, there has also been positivity, as everyone I have explained pensions dashboards to all say the same thing: "That sounds like a great idea! How can I use it?" The fact that dashboards have been received with unanimous positivity, but complete anonymity has been incredibly disappointing, but not entirely surprising to me as I do not think this is an isolated incident.

I see this as indicative of a larger issue surrounding the pensions industry, that of modesty. Whilst modesty is, of course, a noble trait, I do believe that it works against the pensions industry in several areas such as with auto-enrolment.

When speaking with my friends who have just entered the world of work post-university for the first time, many say that they don't know whether they are contributing to their pension, due to the fact they did not make a specific effort to join a workplace pension scheme upon starting. Once the concept of auto-enrolment has been explained to them, they seem very positive about the idea and are grateful to realise they have already been contributing to their pension without even realising it.

I believe a solution to this problem would be for the pension industry to be a bit less quiet about its effective and engaging solutions and to shout its great ideas loud and proud for all to hear.

However, I would voice a quick word of caution as something else that I was told by people when I discussed with them the idea of pensions dashboards is "when can I use it?", which is, of course, a tricky question to answer. With no exact date for the public use of pension dashboards currently decided, it can be somewhat deflating to people who are so excited about the concept. This is where I would advise caution and clarify that, whilst this year could be considered the year of the dashboard, it is not only the year of the dashboard. The excitement and engagement that may be, and in my experience has been, spurred by just the concept of dashboards needs to be subsidised and supplemented by industry measures in the meantime, whilst we wait for dashboards to be properly rolled out.

Written by Tom Dunstan

VIEW FROM THE ACA: Risk management tools & LDI

I was fortunate enough recently to go before the Work and Pensions Select Committee to discuss LDI. For my part I think we can now begin to draw some conclusions on how things might evolve.

There seems little doubt that as a risk management tool, LDI has been very effective over the past decade and that, without it, the stresses on DB funding levels, scheme sponsors, and potentially on member outcomes during that period could have been severe.

But, for the industry, recent events have also been a timely reminder that risk management steps must be continually assessed to make sure they stay fit for purpose. In that light, I was pleased to see the latest statement by TPR and other regulators. This aligns well with our calls for increased collateral levels and, importantly, with measures that have already evolved naturally over recent weeks.

For government and regulators, we hope the period will also renew focus on wider systemic risks. DB schemes are among the government's largest creditor and so it is no surprise that their combined behaviours can have system-wide effects – especially if prompted by unexpectedly bold policy changes.

As schemes continue to mature, these challenges will need to be managed, but in doing so it will be vital to avoid knee-jerk reactions that could introduce new risks to the system.

ACA chair, Steven Taylor

ACA
ASSOCIATION OF CONSULTING ACTUARIES

A week in the life of: LCP partner and head of trustee consulting, Jill Ampleford

Life at LCP is never boring! I've found LCP to be a firm made up of a fantastic group of clever and caring people. I also thrive on the varied work I get, from supporting my wide range of scheme actuary clients to my role on the Pensions Leadership Group as head of trustee consulting, or the people focus my co-chair of the firm's Diversity & Inclusion Steering Group brings me. Pensions is a unique, close-knit industry, and another highlight of the job is the strong relationships I've developed with many of those I work with.

Monday

I kicked off this week with an insightful training session on inclusive leadership. Nothing beats doing these in person and there was a real spark and energy in the room as we reflected on how people can have very different perspectives on challenging matters.

The afternoon was spent in an in-person negotiation meeting for a triennial valuation. Both trustee and sponsor went through our respective positions and came up with a mutually acceptable solution. It's always good when you can find common ground and a solution all can get behind.

Tuesday

Today was a quieter day catching up on bits of work. I spent some time looking at the best and smoothest way to bring a new lead on to a client. We have such a lot of talent on our team and it's important to let others take on opportunities to shine. I also caught up with the team that is leading the move to full buyout and then wind-up for one of my clients.

I rushed back home for my children's primary school concert. Last year in primary school for my youngest and I'm making sure to make and remember all these sessions full of raw talent and energy!

Wednesday

I presented to the board our approach to diversity, equality and inclusion, and how we should evolve it further. Whilst we've made great progress, it's really important that we keep the focus on the right areas and continue moving forward.

I then had a virtual client meeting where I talked through the impact of the LDI crisis and how their strategy might evolve in light of market changes. Many of my clients are stepping back and reflecting whether they need to evolve their strategy in the light of where they have landed following the fall out of LDI – and I'm enjoying talking them through how to evolve their funding and investment strategies in the context of the covenant.

I dusted off my black-tie dress and headed to a dinner in the evening at Innholders Hall, hosted by the ACA. It was great to see so many familiar (and new) faces in a grand setting and to catch up about all things pensions (as well as what everyone was up to for Christmas!).

Thursday

A very social day with a networking breakfast and two evening events, which involved a certain amount of juggling to be at both and lots of enjoyable conversation.

During the rest of the day, I got my head down to ponder some of the bigger themes and issues such as LCP's predictions for the year ahead for an article we're planning and getting updates on some of our in-house admin and GMP equalisation projects.

Friday

I caught up with progress on one of my schemes who is evolving its approach to the member experience, including introducing a new bridging pension and IFA support.

At 1pm I dropped everything for the most important task of the day – logging into the school website to grab the chosen after school club for next term – they always fly out of the door so you have to be quick!

The week ended with a relaxing pizza with my family and then a cocktail or two with some friends. It was another end to an enjoyable week in the world of pensions.

Hard-ing work but someone has to do it

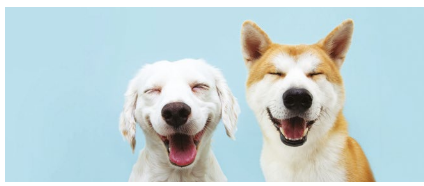
Tom Dunstan chats to Legal & General Investment Committee chair and trustee, Tegs Harding, about her love of Tolkein, her past in banking and her X-Files aspirations

What's your employment history (including jobs outside of pensions)?
I have been a professional trustee since March 2020. Before becoming a professional trustee I was an investment consultant at Mercer, giving advice to pension scheme trustees. Prior to that I was actually working for Legal & General, but this time doing a technical job doing financial modelling for the group. My first job out of university was in banking, first at Egg Banking and later at Citibank.

What's your favourite memory of working in the pensions sector?
One of the most memorable has to be the first time I did a member communication day as a trustee. I travelled down to the sponsor's offices and met with a group of members. Sitting in front of people and explaining what you are doing to look over their life savings really brings it home how important the role is. It's something I grab the opportunity to do whenever I can.

If you did not work in pensions, what sector do you think you would be in instead?
I would probably be back in the banking or insurance sectors, as I am a qualified actuary. Although I have always fancied writing for the financial press.

What was your dream job as a child?
I wanted to be a forensic pathologist, although potentially I just wanted to be Scully from *The X-Files*.



What do you do in your spare time?
I have two big dogs, who both like lots of exercise so I spend a lot of time outside with them. I like to keep moving and get outside whenever I can, so I do paddleboarding, mountain biking and obstacle races, although all of those are more for the warmer months. I'm also a climber and do a bit of aerial circus.

Do you have any hidden skills or talents?
I can do a handstand, does that count?

Is there a particular sport/ team that you follow?
I don't follow sport to be honest, although all my brothers play rugby so can sometimes be found watching them play.

If you had to choose one favourite book, which one would you recommend people read?
My favourite book will forever be *Lord of the Rings* as it is the book that made me fall in love with reading as a child. Given everyone has read that already, the book I'd recommend people read is *Nonviolent Communication* by Marshall Rosenburg.

And what film/ boxset should people see?
I'm a massive nerd when it comes to films and TV. We have been spoiled recently with the *Rings of Power* series and also *House of the Dragon*, which was excellent.

Is there any particular music/band that you enjoy?
The last gig I went to was Placebo, which is a rock band from the early 90s. I love music so tend to get to at least one gig month.

Who would be your dream dinner party guests?
Jarvis Cocker, Wim Hof, Catherine Wood, Talal Hasan and Ann Daniels.

Is there an inspirational quote/ saying that you particularly like?
The one my mum always used to say: "Kindness is free".

Written by Tom Dunstan

In association with

TCW

TCW head of fixed income ESG, Jamie Franco

Incorporating ESG into fixed income

Laura Blows is joined by TCW head of fixed income ESG, Jamie Franco, to discuss incorporating environmental, social and governance (ESG) strategies into fixed income portfolios

According to TCW head of fixed income ESG, Jamie Franco, in our *Pensions Age* podcast, *Incorporating ESG into fixed income*, when looking at ESG within fixed income there are two factors.

The first is looking at integration, she says. What are the risk factors that you need to analyse that are relevant to the price of a security?

"They will vary and differ whether you're a corporate credit or securitised or sovereigns, for instance. But there's a way that analysts, with good underwriting, understand what are the factors that affect those particular securities and including that in the investment process is really part of good due diligence."

The second, Franco continues, is how to view investments that are sustainable in these types of assets.

"So, what companies or collateral is providing a benefit to the planet or society? That's a different analytical framework that requires different data, but it's also equally possible in the fixed income space. Provided as a manager you're very clear about what you're trying to accomplish and which framework you're using, there is a way to credibly analyse a lot of these issues in the fixed income markets," she explains.

Corporate credit is one thing when analysing ESG factors, but applying ESG screens within securitised assets may be more challenging.

However, "securitised is one of my favourite sectors in fixed income because there you're really looking at what is it that's being financed, what the collateral is behind the securitisation," Franco says.

"It's very different than corporate credit where you're trying to analyse intentionality of a corporate issuer, and whether they're meeting their environmental targets. It's really about how much of this pool of assets is going towards solar panels, for instance? How do I know that this mortgage underwriter is actually financing mortgages for low-income neighbourhoods?"

Governance factors are an important part of analysing ESG risks and securitised assets, given the bankruptcy risk nature of the vehicle being financed, Franco adds. "If you don't have a good governance structure, you shouldn't be investing in the assets. Adding additional features such as understanding the environmental footprint of what you're financing both from a positive perspective and a risk mitigation perspective, along with the social characteristics, really builds out a robust research framework for securitised credit."

Analysing the carbon footprint of securitised credit is more of a challenge though, "which we are all trying to solve this problem, which is to say that it is not readily available for securitised credit" Franco says. TCW is playing its part here by recently joining the partnership for Carbon Accounting Financials, which tries to estimate emissions for different asset classes to figure out a methodology for securitised credit.

While regulation may help to overcome this issue, so too will issuers have a role to play.

"It's important to make a distinction between what is a good risk management tool and what is a values-based investment, they often get conflated. As a result of that, a lot of education is needed with clients, but we continue to see a lot of demand for different approaches across the sustainable spectrum. Looking for investments where they want to ensure they aren't financing certain companies or sectors is an approach that some clients have taken on the one hand," Franco says.

"On the other hand, you see a lot of clients looking for ways to finance more sustainably, and that means a lot of different things to them. As a manager, you need to flexibly design and provide these solution for clients."

To meet differing, and evolving, investor demand, TCW is trying to provide an ability to integrate ESG considerations that are financially material across asset classes and sectors, even ones that traditionally have been challenging to evaluate, such as private loans and securitised, Franco says. "It's critically important to the investment process, understanding the risks in our portfolios," she adds, "and whether or not we're being compensated for those risks."

TCW also aims to provide sustainable investing solutions to its clients across a range of objectives, as well as working on a robust framework for understanding the transition to a low carbon economy.

As Franco says: "We're very excited about the ability to help partner with clients to provide investment solutions in that space."

To listen to the podcast, please visit www.pensionsage.com

The year ahead: Pensions in 2023

After a year in which the word eventful feels like an understatement, it doesn't seem like the pensions industry is going to get much respite in 2023. Jack Gray investigates the key themes for the coming year

Following the events of 2022, the pensions industry will be hoping for a quieter year in 2023. However, the issues affecting the industry towards the end of the last year look likely to rumble on, with the fallout from the liabiity-driven investment (LDI) crisis ongoing. This year will also see several other key themes, including the next stages of pensions dashboards, the DB Funding Code, the need for improved DC pension adequacy, and TPR's Single Code of Practice. We look at these key issues in more detail.

LDI

"A big area of focus for DB schemes will be the lessons learned from 2022's gilt market volatility," says State Street Global Advisors head of retirement strategy, Alistair Byrne. "Schemes using LDI will consider their investment strategy, including leverage levels, collateral requirements, and stress testing."

Schemes will likely be busy this year assessing the risks of LDI investment and what role it will play in their strategies. Society of Pension Professionals president, Steve Hitchiner, notes that 2023 will see reviews of liquidity and governance requirements, but stresses a measured and consultative approach will be important to help avoid unintended consequences.

"Liquidity in the Fed hike/inflation-defined era ahead will be important," adds Man Solutions head of multi-asset solutions, Peter van Dooijeweert, "and use of leverage must be modelled sufficiently to ensure there are no unexpected collateral or margin issues. Private assets could come under more scrutiny."

Aon partner, Lynda Whitney, concurs that the LDI crisis is likely to lead to investment strategy reviews this year: "We see DB schemes in a range of investment scenarios needing to reconsider their risk and return structure when overlaid by new liquidity constraints. On risk settlement, we see schemes whose funding level has improved and are closer to buyout, but also schemes who need to reassess liquidity and may be further away from a buy-in."

Squire Patton Boggs head of pensions, Matthew Giles, states that some schemes may have to sacrifice some return-seeking assets to recalibrate their LDI to accommodate the trend towards lower leverage.

"All of this will extend their time to buyout and may mean re-opening long term funding discussions with the employer," he continues. "It could also mean that greater attention will need to be paid to compliance obligations, whilst the scheme runs on longer."

Portfolio allocations/ illiquids

The volatility following the mini-Budget and its impact on LDI, alongside the push for DC schemes to invest in more illiquids, will likely influence schemes' portfolios in the coming year, as Candriam head of UK distribution, David Morley, explains: "Scheme asset allocations have been left unbalanced as the most liquid assets were sold to meet collateral calls on LDI programmes, leaving overweights to illiquid asset classes.

"Capacity in the pension insurance market remains a constraint on the endgame ambitions of many, so it will be interesting to observe whether there will be a rebuilding of positions in more liquid risk assets. It is hard to predict strong demand for private assets from corporate DB schemes in this environment."

Morley expects this lack of demand from DB schemes to be picked up by LGPS funds and DC schemes, where there is interest in building more sophisticated default portfolios.

Franklin Templeton head of UK retirement, Lee Hollingworth, agrees: "We believe that 2023 will be the year when private markets investment within workplace DC will come of age. Having reached sufficient scale, allocations to private markets will become a priority for most asset owners and large employer DC schemes.

"In addition, the regulatory focus shifting from an emphasis on cost to value should help support a more balanced approach to strategic asset allocation."

Octopus Group co-founder, Chris Hulatt, says he hopes this year will see the transition from a regulatory push factor to pull demands from DC schemes: "Doing this would surely change the pensions landscape, by providing DC schemes with a huge opportunity to invest in the asset classes that can fundamentally shape the future of our economy, such as venture capital, while driving positive financial outcomes for members."

Despite the growing calls for illiquids to play a greater role in DC schemes' asset allocations, Natixis IM head of UK DC sales and strategy, Nick Groom, notes the competitive landscape of low fees in the DC market needs to change to drive greater illiquid investment. "There are a number of initiatives to try and make this happen, for example, the ELTAF will enable private assets to find their way more easily into DC schemes," he explains. "Also removing the performance fee element from the fee cap will help open up more funds from managers that work this way, but none of this will happen unless we have a change of approach from low fee to overall value to members."

Van Dooijeweert adds that "much has been made" of the poor returns in the traditional 60/40 asset allocation, but investors may not have been expecting the severe impact on portfolio volatility of rising bond/equity correlation couples with rising bond and equity volatility.

"Correlations have been very unstable in most asset classes and have created significant challenges in management for traditional investors," he continues. "Future correlations are unknowable across bonds, equities, currencies, and commodities. Adding active management around correlation, or via trend strategies, could play a role in improving portfolio returns."

DC adequacy

The issue of DC adequacy and auto-enrolment reform looks set to take centre stage this year as people grapple with the cost-of-living crisis. More people are reaching retirement with purely DC savings, and Bryne stresses the need for the industry to provide solutions and support to help people have sustainable income in retirement.

BlackRock head of UK institutional client business, Gavin Lewis, adds that DC schemes will likely increase innovation this year, giving savers the ability to access more opportunities.

"The investment landscape in 2023 will continue to be shaped by the macro-economic forces that have led to the end of the great moderation – with savers, who depend solely on investment returns to realise their retirement goals, having to contend with increased inflation, higher interest rates and continued market volatility," he says. "This will see the structure of schemes evolve, as affordability and achieving value for money become more important. In 2023, pension adequacy – be it by gender, ethnicity, or regional distribution – will come into much sharper focus."

People's Partnership, provider of The People's Pension, director of policy, Phil Brown, adds: "The DWP has already signalled its intention to publish new value for money metrics that, if used correctly, may change how DC schemes and products are judged.

"The next 12 months will also tell us just how resilient auto-enrolment is and whether the anticipated increased financial pressures on millions of people will lead to a significant increase in the number of people who stop paying into their pension.

"The much-anticipated response from the DWP on its consultation about decumulation in DC pensions should lay out a clearer path for how savers can be supported on how to best use their pension pot."

Dashboards

One development that may help the industry in supporting greater DC pension adequacy is pensions dashboards. This year will see the mandatory onboarding of schemes in April as dashboards get prepared for launch. "The deadlines for schemes to connect to pensions dashboards will be landmark events in 2023," says TPT Retirement Solutions DC director, Philip Smith. "As many people have several DC pensions from different providers, the launch of dashboards will be fundamental to consumers fully understanding and engaging with their pensions. While consumers aren't expected to be able to fully access the dashboards until the second half of 2024, the next 12 months will be significant, especially for large schemes and master trusts."

DLA Piper partner, Matthew Swynnerton, adds that dashboards should revolutionise the way members access pension information, "hopefully ushering in an era of increased engagement and understanding".

Hitchiner stresses that for dashboards to be a trusted and transformative engagement tool, 2023 needs to see an increased focus on their successful delivery, and the industry needs clarity on deliverables and deadlines.

DB Funding Code

TPR's DB Funding Code, which is expected to be operational from September 2023, is set to be one of the biggest shake-ups to DB pensions in recent years. Whitney notes that the new code will require trustees to agree a Statement of Strategy with their employer and focus on the long term, and that investment strategy changes may need to be reviewed.

"The core principles and objectives underlying the new regime are sound, but there are concerns that the detailed requirements are too inflexible," warns Hitchiner. "This could lead to unnecessary costs for employers, reduce innovation and increase systemic risks. The industry, policymakers and TPR need to work together to ensure that the overall framework continues to provide the flexibility needed to adapt to changing economic circumstances."

Single Code of Practice/notifiable events

Alongside its DB Funding Code, schemes will need to be aware of TPR's Single Code of Practice and new notifiable events regulations this year. "A key focus of the single code is consolidation of a number of existing codes of practice, much of the content should already be familiar to trustees, however the key difference is the increased focus and scrutiny on scheme governance, which governing bodies have to ensure that they address," explains 20-20 Trustees trustee director, Angela Winchester.

"We recognise that governance arrangements should be proportionate to the size and complexity of the scheme, and we have been working to develop a pragmatic, straightforward and cost-effective solution for schemes to ensure that their governance is fit for purpose, focusing specifically on the new Effective System of Governance and Own Risk Assessment requirements."

Giles adds that compliance projects will begin or accelerate, noting there is room for proportionality and a short path to buyout may justify a "light-touch approach".

Finally, on the new notifiable events regulations, Swynnerton comments: "Depending on how the regulations are drafted, the implications for corporate activity could be significant, giving trustees a seat at the table in transactions, and bringing forward the trigger to notify, so that this occurs at the point at which 'a decision in principle' is made to proceed with the event, that is, before the event has actually occurred. The final regulations and, hopefully, the clarity they will bring are eagerly anticipated by trustees and employers alike."

Written by Jack Gray

The path ahead for pensions in 2023

Pensions Minister, Laura Trott, speaks to *Pensions Age* about her priorities and aims for the coming year

Last year was quite a year for pensions – with plenty of positives. I was extremely pleased to see out 2022 with our commitment to the biggest state pension increase in history from April, and a renewed push for pensioners to claim Pension Credit.

Throughout December 2022 we called upon pensioners across the country to check if they were entitled to this passport benefit as soon as possible, ensuring they stood the best chance to qualify for an extra £324 cost of living payment.

Dedicating my time to making sure a generation who worked their whole lives for our country are supported in their old age is something I am extremely passionate about and will continue to do throughout my time in this role.

It was also my great pleasure to step into my new role as Minister for Pensions in the autumn last year, just in time to mark a decade since the dawn of automatic enrolment.

One of the key measures on which to judge automatic enrolment is whether it is supporting people to save towards achieving the lifestyle to which they aspire in retirement.

In the 10 years since its introduction, the British people have started saving at unimaginable rates when compared to pre-automatic enrolment levels. New figures released to mark the anniversary showed the number of eligible employees participating in workplace pensions rose from 10.7 million to 20 million, an increase of 86 per cent.

In 2021 alone, these eligible workers saved £114.6 billion into their pension pots, a 40 per cent real terms increase in what they were saving in 2012.

Dubbed 'automatic enrolment 2.0' by my predecessor, the future of the policy is being supplemented by a range of measures helping people engage more with their savings. Our objective is to help savers better understand the clear benefits of paying into their retirement pots.

"My key goal is to ensure people have access to the support and information they need to make informed choices about their financial futures"

As I look forward to what we can deliver in 2023, my key goal is to ensure people have access to the support and information they need to make informed choices about their financial futures; including pensions dashboards – which will enable everyone to instantly pull together data from all of their pension pots and see how much they have saved over their lifetime – and through our ongoing work on value for money with The Pensions Regulator and the Financial Conduct Authority.

This is alongside the introduction of new user-friendly, two-page pension benefit statements to help make it easier for people to access and make sense of their pensions information to support their retirement planning. It is my hope that making pensions information easier to navigate will help boost engagement and understanding among savers.

I will also be looking to find a workable solution to tackle the issue of DC small pots, looking to find a resolution that ensures a better functioning and efficient pensions market to provide the best possible outcomes for savers.

Elsewhere in the private pensions space, I hope to forge the path ahead for collective defined contribution (CDC) pension schemes. CDC schemes have the potential to transform the UK pensions landscape, and since the introduction of the legislation in 2022, some parties have already expressed an interest in expanding CDC models, including multi-employer CDC schemes.

We have a jam-packed January and opening to the year. I am steadfast in my conviction that my role is one of the most important jobs in government and it is my ambition to continue to support our current pensioners and deliver for the record number of people across the country now saving for retirement.

Having created a generation of savers, it's time to help them maximise the value of their hard-earned retirement in later life.

Written by Minister for Pensions, Laura Trott

Summary
• The largest pension providers will be required to start feeding data to the dashboard infrastructure from August this year.
• The Pensions Dashboard Programme is engaged with providers in testing and refining of the digital framework.
• Administrators and other service providers still face challenges in enabling retirement income estimates through the dashboard.

Powering the dashboards revolution

With deadlines set and standards emerging, attention is turning to ensuring pension providers and schemes are ready to provide data to dashboards from next year. Nick Reeve explores the progress so far and the hurdles still left to negotiate

It's official: Pensions dashboards are coming. With the Financial Conduct Authority's final rules published on 1 November 2022, the regulator set out rules for pension providers governing how they must supply data to dashboards.

The implementation deadline is 31 August 2023, and a consultation is expected imminently for rules for commercial dashboard providers.

Speaking at the publication of the government's dashboard legislation in October last year, Pensions Dashboards Programme (PDP) principal, Chris Curry, stated that the development would "make a real difference to how people view their pensions savings, and how pension providers and schemes engage with their members and customers".

With just a few months left until the first window opens for providers and schemes to start connecting to the new technology's 'ecosystem', Curry added, "dashboards will soon become a reality, and government, the regulators, and industry will work together to make them a success".

But how ready are pension providers? And how realistic is the implementation timeline given the highly complex nature of the UK's pensions industry?

The state of play

The PDP is currently working with more than 20 organisations to help build the technology infrastructure that will power the dashboard, testing and refining it to ensure it is as smooth and secure as possible when it launches this year. The digital architecture is provided by Capgemini and Origo.

The first dashboard – MoneyHelper, provided by the Money and Pensions Service – is expected to be followed by commercial versions in the coming years as more providers plug into the infrastructure and more pension savers become comfortable with the concept.

For service providers – in particular administrators – the next few months will be crucial in making sure their systems are prepared and can support data exchange and cybersecurity requirements. Many firms have been working for months, if not years, to digitise their data records and improve connectivity in preparation for this, often by engaging with independent service providers (ISPs) – effectively buying in the required technology and expertise.

The data provision part of the dashboard project is well catered for in this regard, according to CTC Pensions Technology sales director, John Parker. Providers of legacy pensions are "talking confidently", he says, and working on data cleansing ready to feed that information to dashboards.

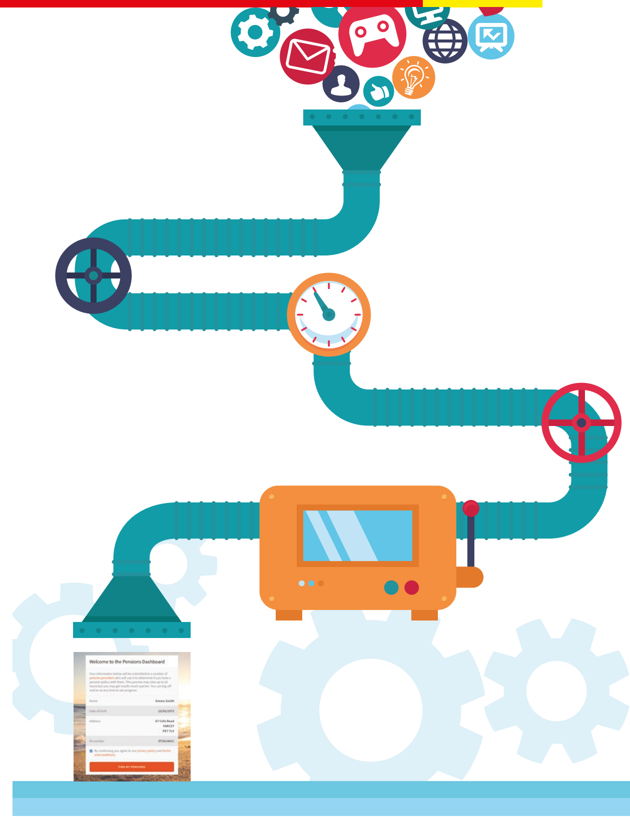
However, the functionality that dashboards are expected to provide could cause issues for some firms. This may be the case for providers of legacy pension products such as with-profits and insurance-based funds. For these, compliance with dashboard requirements may be "challenging" given their typically older technology, explains Ross Trustees senior associate, Luke Tutt.

Parker adds: "The market from administrators for ISPs who will meet data requirements looks competitive and well provided for. However, many of these do not have the calculation capability to adjust to the new estimated retirement income projections, and there is also a concern that when the smaller defined benefit schemes come on board they will be overlooked."

The PDP's website states that it is "essential" that dashboards can provide estimated retirement income information "from day one". Evidence shows that savers want and need this information, the PDP says, and without it "dashboards would lack credibility".

However, while most providers can model retirement income based on their own data, how they do this varies significantly depending on the type of benefits. This hampers comparability and threatens to undermine confidence in the dashboard project, according to some commentators. The PDP is carrying out testing and is working on data standards in an effort to address this significant issue.

This makes the quality of pensions administration more important than ever for occupational pension schemes, according to Gateley Legal pensions partner, Phil Jelley. He points out this pressure comes from the legal obligations of trustees to ensure they can supply data



to the dashboard.

For smaller schemes – those with between 100 and 999 members, due to be onboarded in 2024 and 2025 – trustees "will have to carefully consider whether they have the capabilities and resources to economically and efficiently meet the dashboard obligations, and consideration may switch to whether to outsource future administration", Jelley says.

For larger schemes that face the earlier deadline, Jelley adds that trustees "should already be well advanced in discussions with their administrators as to how dashboard compliance will be achieved".

"Such advanced planning is necessary as there may be hurdles in preparation that the trustees need to overcome, which may be both complex and time-consuming," he explains. Important areas to discuss and obtain clarification on include technology platforms, software, staff capabilities, capacity, accuracy of benefits, the potential effects of GMP equalisation, and data security.

Therefore, there is a greater urgency for boards to work towards these deadlines, with Tutt urging trustees to work "full steam towards meeting" obligations ahead of time.

"For smaller schemes with access to fewer resources, trustees should identify any potential constraints and seek early access to external help to ensure full compliance," he says.

"For those schemes with later staging dates, compliance with the pensions dashboard requirements should now be a standing item on all trustee meeting agendas. This will allow both the trustees and advisers to work together to ensure there is a plan in place for their schemes to be compliant ahead of these changes."

Meeting the deadline

The first window for mandatory connections to the dashboard's digital infrastructure opens in August 2023 for the country's largest pension funds and providers. Whether they will be ready is unclear. While the PDP's work has been underway for some time, the digitisation of pension data is a massive project for the entire industry.

"There are a range of deadlines from connection to the dashboard, addition of estimated retirement income projection and final 'go live', and these are spread across multiple waves for differing providers," explains Parker.

While the focus has rightly been on data cleansing, Parker warns that "no one is watching" the deadline for providers to be able to support estimated retirement income projections in October next year. These are changes that "no one is planning for and only about 10 per cent of current providers can handle", Parker says.

In agreement is Jelley, who says the PDP's deadlines are "more realistic for the larger pension providers" given their greater resources – although these firms also have the largest amounts of member data to prepare.

For schemes such as defined contribution master trusts, the advent of dashboards could act as "an opportunity to showcase how efficient their particular scheme is, with a possible view to the likely future consolidation of member funds which the dashboard will facilitate", Jelley continues.

Many master trusts are also less reliant on older technology, making it easier to adapt to the digital infrastructure that will power the dashboards.

"In my view, it isn't inevitable that a significant proportion of the pensions industry will miss the deadline," says Jelley. "Many of the larger commercial providers and third-party administrators will see this as an opportunity to showcase their services and will be keen to ensure that they can meet the dashboard obligations for themselves and their clients.

"Providers and administrators will not want the negative reputational risk of being unable to have the infrastructure in place to meet the requirements and the potential impact this may have on their business."

He highlights that schemes can apply for a deferral of up to 12 months from their initial deadline pushing to meet it would be "disproportionately burdensome or put the personal data of members at risk".

The central tenet for every stakeholder in the dashboards project is to ensure the security and credibility of the system for the benefit of end users. Parker says that, while deadlines may be pushed back and some providers may not be ready in time, "if we wait for it to be perfect then it will never happen".

Tutt concludes: "Regardless of any difficulties in schemes meeting their respective staging date, confidence in the pensions dashboard will build over time as the industry, and users, adapt to the new normal."

It seems this revolutionary development for the UK pensions industry is just a short time away from becoming a reality.

Written by Nick Reeve, a freelance journalist

The scale of the problem

In the first of *Pensions Age*'s year-long series on the subject of scams, Laura Blows explores the different types of pension scams, how the cost-of-living crisis may increase the prevalence of scams, and the impact of scams for both the member and the pensions industry

Summary

- The average loss per individual to pension scams is estimated to be around £75,000.
- There are many different styles of scams targeting retirees, including transfer scams, liberation scams, investment scams and layering scams.
- The cost-of-living crisis may increase the risk of people being vulnerable to scams.

Defrauding pensioners is not a new phenomenon. Yet ever since the freedom and choice reforms of 2015, scammers have been attracted by the siren call of significant sums of money suddenly becoming available to people who are typically not used to managing such wealth.

As pension transfers are invariably large sums of money, "it is likely that scammers would target them as the potential reward appears very high compared to consequences/risk of being caught or found out during the process", SPP Administration Committee deputy chair, Amit Shanker, suggests.

"The world has cottoned on to the massive value invested in pensions, the opaqueness of its workings and the lack of trust in providers, that scammers spotted a rich source of income, for relatively little cost and risk to them," Pension Scams Industry Group (PSIG) chair, Margaret Snowdon, explains.

The amounts obtained by scammers can be significant, with Dalriada Trustees head of technical, research and policy, John Wilson, noting that some individuals have lost seven figure sums and the average loss per individual is estimated to be around £75,000.

While Snowdon acknowledges that we don't know the scale *[of pension scams]* "and can only extrapolate from what we do know", PSIG believes that around 5 per cent of pension transfers could be scams, "which could mean over a £1 billion a year being lost to up to 10,000 people".

Methods

The methods in which scammers obtain these figures are also varied and evolving.

According to Scottish Widows senior corporate pension specialist, Robert Cochran: "More often than not, a pension scam starts with an unexpected phone call, email, or text from someone claiming to represent a financial services firm or government body, but the tactics being used are becoming increasingly sophisticated."

While "all pension scams are basically the same – scammers deceive with false claims of better outcomes and people fall for them, what varies is the approach", Snowdon says. She highlights four typical types of scams.

First, she explains, transfer scams are where someone moves their pension savings from a safe scheme to an unsafe one, where the savings can be directly stolen or squandered through charges and investment losses. These are often to international SIPPs, which are UK personal pensions, but involve overseas advice and are thereby not subject to UK financial protection if things go wrong.

Second are liberation scams, where someone transfers their savings in order to access funds earlier than the law permits and thereby incur tax penalties. This is often combined with theft and investment losses.

Then there are investment scams, which are where someone is persuaded to cash in their pension savings and invest them in unregulated or bogus vehicles.

Finally, layering scams involve someone transferring their pension to an arrangement where there are several parties quietly deducting significant fees to whittle away the funds.

At risk

With such a variety of scams available, anyone can be at risk, particularly as scammers are very convincing and appear trustworthy. "Ironically around 50 per cent of people think they would never fall for a scam, despite evidence to the contrary," Snowdon notes.

"While people of all ages need to be on their guard, the sheer value of assets held in defined contribution pensions means they will always be a target for fraudsters," AJ Bell head of retirement policy, Tom Selby, warns.

However, Snowdon states that most pension scams are against 50-something males because they tend to have more savings and are closer to pension age. "Also, a little financial sophistication gives people more courage to go for that 'once in a lifetime opportunity'," she adds.

Scammers were normally likely to target low-income areas, along with those members of society who could be considered vulnerable members of society, such as the elderly, who could be more susceptible to scams or of being confused/overwhelmed by information/pressure from scammers, Shanker notes.

"However, scammers have materials that appear genuine to members and by also using convincing adverts online a larger audience is being targeted and could fall foul of a scam," he adds.

Cost-of-living crisis

With the current cost-of-living crisis, more people may become susceptible to scammers, prompting The Pensions Regulator (TPR) to launch a strategy to educate the industry and savers on the threat of scams, prevent practices that can harm savers' retirement outcomes, and fight fraud through the prevention, disruption and punishment of criminals.

"Many more people are under financial stress and very vulnerable. They need access to cash to get by and pension savings will therefore be very attractive," Snowdon says. "Because rules on pensions access are so inflexible, people will be driven to scammers who will offer to help but will help themselves to people's savings."

In October, the Financial Conduct Authority (FCA) raised concerns that rising costs could leave people vulnerable to scams, after research found that 25 per cent of savers would consider withdrawing money from their pension earlier than planned to cover the cost of living. This has already started to occur, Cochran says. "Unfortunately, we've seen an increase in the number of pension scams taking place in the UK. Our research has found that more than one in 10 people have been targeted by a pension scam, with one in 20 of these saying the scam was successful," he notes.

"We've seen an increase in the number of pension scams taking place in the UK, as scammers use rising living costs to take advantage of people"

Consequences

The ramifications for this can be significant. Wilson notes that trustees and providers have duties to protect pension savers and "when they fail to do so, those that lose out will seek redress from those who may have transferred money without proper checks. Like with PPI, there are now claims companies specialising in this area".

Research by Wealth at Work and the PMI found that pension trustees have 'grave concerns' for their members as they approach retirement, with 92 per cent of trustees fearing they will be targeted by scammers. The pensions industry should care about scams first and foremost because it damages the welfare of customers, Selby says. "Regardless of whether scams directly involve pensions or not, it is clearly terrible if large numbers of people are defrauded of their life savings," he explains.

"There is also the risk that if people don't feel their pensions and investments are safe from scammers, they will stash their cash under the mattress or simply choose not to save for the long term at all."

Written by Laura Blows

Pensions Age 2023 scams focus

Throughout 2023, *Pensions Age* will be shining a spotlight on pension scams, delving deep into the many issues and challenges the industry faces in tackling fraudsters.

Over the year we will explore topics such as the evolving nature of scams and their psychological impact – how they manage to entice people, and the mental impact of falling victim of a scam. We will hear first-hand about the devastating consequences of losing your pension savings to a criminal and highlight the effective communication methods implemented by trustees, employees, regulators and providers to minimise this risk to their savers.

While the vital role of politics and regulation in this fight against scammers will be explored, so too will be the importance of collaboration with all parties to tackle this foe. Best practice methods of minimising fraud will be highlighted and we will talk to the experts with one-on-one interviews about how best to achieve these goals.

Finally, we will celebrate the industry's hard work and achievements in this area by showcasing success stories of protecting potential victims and prosecutions of fraudsters.

Commenting on *Pensions Age*'s scams focus, Minister for Pensions, Laura Trott, says: "One of my key priorities is to make sure savers are armed with the tools they need to catch out duplicitous fraudsters who operate online.

"These crooks will use any means necessary to get at peoples hard-earned savings, and even the savviest among us could fall victim to these sophisticated scams.

"The landmark Pension Schemes Act introduced legislation to prevent pension savers from becoming a victim of a scam and I will continue to work closely with industry leaders so we keep your savings out of their pockets.

"I am in full support of *Pensions Age*'s campaign to shine a light directly on scammers so this year we can take down more criminals who want to part us from our retirement funds."

Looking to the Left

Summary
• The Fabian Society recently released a report where it outlined several recommendations for what action a Labour government should take in relation to pensions.
• Whilst much of it was positively received, some recommendations were perceived as controversial by industry experts, such as the emphasis on guaranteeing a retirement income for life.

In light of the recent publication of a new report by the Fabian Society, Tom Dunstan examines both the report's contents and the industry's reaction to it to understand what the political pensions landscape might look like under a Labour government

Politics have, of course, always been very closely linked to the world of pensions (something last year's mini-Budget under Liz Truss made very obvious) and so the people and party in government is very important to the running of the pensions industry.

Whilst the next general election may be a while away (with the next mandatory election occurring in 2025 if it is not called before then), a recent publication has provided some insight into what attitudes a Labour government might have towards pensions and what changes they may implement if they came into power.

On the bright side

A recently released report from the Fabian Society, a centre-left thinktank, entitled *Good Pensions For All: The Left's Agenda for Private Pensions*, details perceived issues with the current pensions system and its suggested recommendations for fixing these issues.

The report outlines three key priorities that the society believes a left-wing government should provide, namely a retirement income for life available to all as the norm, support for everyone to save enough to meet their future financial needs, and fair, affordable and effective social security and tax policies.

Providing some background on the report and the reasons for the report's creation, the Fabian Society general secretary, Andrew Harrop, states that: "There aren't that many centre-left think tanks with much engagement in these sorts of pensions policy debates."

After the release of the report there has been a fair amount of industry reaction to it, much being positive.

One area of agreement was with its recommendations surrounding collective defined contribution (CDC) pension schemes.

The report included many proposals about CDC schemes, such as the introduction of legislation to enable pension providers to offer CDC decumulation-only pensions if they wish and to challenge large employers who would have once operated defined benefit (DB) pensions to establish collective pensions using the CDC model.

These proposals were met with

general positivity and enthusiasm by the pensions industry, such as from LCP partner, Steve Webb, who comments: "I think there is a strong CDC sentiment within the industry."

The report's proposals surrounding auto-enrolment and tax reform also received a positive reception from members of the industry. For instance, Webb states that "we do need to take a proper look at tax relief". However, not all recommendations in the report were received with such universal approval, such as its suggestion for providing a guaranteed pension income for life.

Lifelong guarantee

One of the main ideas the report argues for is pensions being primarily for the purpose of providing a guaranteed income for life. On this topic, the report suggests the steps that could be taken to achieve this goal, such as raising the minimum age for drawing a private pension to 60 or 62 once state pension age reaches 67 and revising pension communication requirements for people in their 50s to focus on saving more and working longer, rather than accessing pensions.

One of the biggest parts of the strategy to ensure everyone has access to a guaranteed retirement income for life is the plan to reverse the direction of recent policy and develop a framework where pension deliver incomes for life as the norm for most people. This is an idea that has been somewhat controversial in the pensions industry.

There has been positive reaction to the idea, such as from the Pensions and Lifetime Saving Association (PLSA) head of DC, master trusts and lifetime saving, Alyshia Harrington-Clark, who states: "Some of the issues that they draw out are the same ones that we found, namely that some people are making sub-optimal choices and that they risk making poor decisions that lead to them either running out of money too early or use their retirement income for something that isn't really about retirement income", giving the example of using retirement income for personal use.

However, there are some in the pensions industry who have not looked on the idea as favourably, such as Webb who voices concern that the implementation of such a framework might be seen as a rolling back of pensions freedoms.

He says: "Of all the things on the list, that would probably be the least popular one with the industry."

In addition to possibly being unpopular with the pensions industry, Webb casts doubt on the idea that the measures suggested by the Fabian Society would be introduced by a possible Labour government, stating: "Pensions freedoms is very popular and raises money for the Treasury so I think this questions the extent to which a Labour government would row back on those freedoms."

Webb also criticises the lack of clarity surrounding the report's proposal, saying: "It's not clear what they mean by an income for life being the norm for most people. Do they mean you have to have a certain amount of pot before you could do something else other than buying an annuity?"

Responding to this controversial reception on the report's guaranteed income framework, Harrop states: "I wouldn't claim that this is something that the industry is going to be 100 per cent behind."

Harrop also says that the report does point out exceptions to the suggestion of changing to a framework that provides an income for life, such as for particularly small pension pots as "in that case it does make more sense just to maybe take it as one payment". It also specifies that it is the "middle group" of pensions that are the chief concern for the paper's framework.

Coming up short

The idea of the new pension framework was not the only controversial part of the report. Harrington-Clark voices some concern about the report's suggestions on auto-enrolment, although for a different reason.

Whilst Harrington-Clark made clear that some of the reforms to auto-enrolment suggested by the report, namely reducing the age for auto-enrolment and to judge auto-enrolment on the first pound of earnings, had almost 'universal' backing from the pensions industry, she also states that "almost universally people think that we should go further than that", thereby suggesting that perhaps the report's recommendations could have done more.

This sentiment is also echoed by Webb, who states: "There's a spectrum of suggestions in the report, some of which are pretty mainstream."

Auto-enrolment was not the only area in which Harrington-Clark had an issue with the report. She clarifies that, whilst there was not a specific line of policy recommendations in the report that she disagrees, her concerns lie more with the fact that the report didn't go far enough on the concept of minimum income standards as they have, in the past, asked for "a proper, holistic and considered objective for the overall framework".

The report has certainly managed to produce some interesting conversations surrounding what direction a potential Labour government could take the pensions industry in and, although some of that conversation has been contentious and controversial, it certainly hasn't failed to pique the industry's attention.

A week is a long time in politics, so the saying goes, but just how long a time is two years? That could be a lifetime. So, whilst the Fabian Society's report does indeed ask some thoughtful questions, it is difficult to say at this stage exactly how accurately the report would reflect the realities of a new government.

Written by Tom Dunstan

The Pensions Regulator

Making workplace pensions work

Putting strategy into action

The Pensions Regulator (TPR) has emphasised that it will take action against those trustees who ignore employer-related investment rules. Sophie Smith considers the recent action taken by the regulator on employer-related investment (ERI) breaches

The Pensions Regulator (TPR) has been cracking down on pension scams over the past year, having published a new scam-fighting strategy in light of concerns that the cost-of-living crisis may leave savers vulnerable.

In this, TPR said it was primarily, although not solely, concerned with seven kinds of scams, including employer-related investment (ERI) breaches.

And the work to tackle these issues is already delivering results; two former pension scheme trustees recently received suspended sentences for making illegal loans of £236,000 from a company pension scheme to the scheme's employer, following a prosecution by TPR.

Former company directors of Eastman Staples, Andrew Kyprianou and Colin Werb, were sentenced to 16 months in jail for each offence, suspended for two years, and were also ordered to carry out 250 hours of unpaid work.

Although the pair initially pleaded not guilty, they later changed their pleas, admitting two counts of making prohibited ERI. Both defendants were also charged with providing false or misleading information to TPR contrary to section 80 of the Pensions Act 2004.

The charges relate to two loans, an initial £96,000 loan and a second £140,000 loan, paid from Eastman Machine Company Limited Superannuation Scheme to Eastman Staples Limited, contrary to section 40(5) of the Pensions Act 1995.

TPR initially challenged Werb regarding the £96,000 payment in 2018, only to be told it was being used as working capital for the business and repaid on a monthly basis with 5 per cent interest, while Werb failed to mention the £140,000 payment made earlier.

Kyprianou also told TPR the money was withdrawn from the pension scheme and paid to the company to support it in the face of the adverse effects of Brexit.

However, both Werb and Kyprianou changed their story in later interviews with TPR, stating that the payments were instead used as investments on behalf of the scheme in a disused church, with a view to potentially converting it into offices and a community space.

Despite this, TPR found that the church was not registered in the scheme's name and there was no independent evidence to support these assertions.

Furthermore, although the pair had fabricated minutes to disguise the loans as investments, investigators found communications describing earlier payments from the scheme as loans.

Since proceedings began, the defendants have sold the church and paid the proceeds of sale to the scheme, with £270,000 paid into the scheme.

TPR director of enforcement, Erica Carroll, also highlights the case as a reminder to all trustees on the rules around ERI and a warning that TPR will prosecute those who ignore them.

"Despite being experienced business people and having been warned by their adviser about payments between scheme and employer, Werb and Kyprianou continued to flout laws designed to protect pension savers," she states, arguing that the duo "recklessly used money meant for their staff's retirements to prop up their company despite the risk to the scheme – and their employees' pensions".

Looking ahead, Carroll also emphasises the importance of proportionality in the regulator's approach, stressing however, that TPR will take tough action where needed, stating: "During the initial months of the global pandemic, we supported trustees and the industry with guidance, advice and regulatory flexibility. We will continue to act in a proportionate way during this current period of economic pressure, but that does not mean trustees and employers should be complacent. Legal duties remain regardless of external pressures.

"We will not be relaxing our stance on those who abuse their position of trust because circumstances are challenging. We will continue to be tough on scammers, fraudsters, criminal gangs and those who fail to treat savers fairly; we stand ready and willing to use our regulatory powers, or prosecute against those who break the law."

Written by Sophie Smith

Summary
• Attributing blame to trustees, consultants or managers for the LDI liquidity crisis could be viewed as a harsh verdict. The mini-Budget that sparked the crisis was clearly a Black Swan event.
• Nevertheless, some additional tweaks to the overall system could help avert future similar events.
• These include better regulatory oversight of 'hidden leverage' and allowing more flexibility for pension funds when posting collateral.

The blame game

With almost everyone involved with LDI getting caught out by the dramatic events following the September 2022 mini-Budget, what needs to be done to improve oversight of the investment strategy?

Speaking at a conference run by the International Swaps and Derivatives Association and the Alternative Investment Management Association on 7 November 2022, Bank of England executive director of financial stability, strategy and risk, Sarah Breeden, labelled the LDI liquidity crisis of September 2022 as the latest example in a list of "poorly managed non-bank leverage throwing a large rock into the pool of financial stability".

From Long-Term Capital Management in 1998, to the failure of Archegos in 2021, Breeden said several episodes in the past two decades have highlighted the need to take into account the potential amplifying effect of ill-handled leverage that when aggregated, can escalate into systemic risk.

Attributing the LDI emergency in wholesale fashion to substandard supervision, however, is viewed by many in the pensions industry as a rather harsh verdict, given the unprecedented nature of September's mini budget. Nevertheless, some warning signs were there. Back in July 2022, Aon and Mercer both urged DB funds to prepare for bond yield spikes that had not been seen since the early 1990s. Any such rapid rises, said the consultancies, would place huge pressure on LDI strategies.

Is anyone to blame?

Such admonitions, clearly, came too late to make any difference. Everyone along the governance chain was caught out by events, making it hard to definitively pin blame on any particular group or regulator.

One commentator, who wished to remain anonymous, explains that most schemes would have been aware of the liquidity profile of their assets and the leverage in their LDI portfolios in the run-up to the mini-Budget. What caused the challenges for most schemes was the speed of the collateral calls, which was quicker and more extreme than had been stress-tested for, so collateral buffers were being rapidly eroded.

In parallel to this, the collateral buffers that LDI managers were requiring clients to hold were also being increased. In a classic snowball effect, this meant that once schemes had met collateral calls to maintain hedging positions, they were then required to raise more capital to build up a larger buffer against future collateral calls. "So even if a scheme had been holding a buffer sufficient to withstand the extreme movement in rate rises, they would still have been required to find more assets to build up the collateral pool," explains the commentator.

In its response to a call for evidence from the Work and Pensions Committee on the crisis, the PLSA writes that its research indicates that nearly all schemes believe they had a strong understanding of risks within LDI strategies. "It is also evident that various measures put in place following the financial crisis, worked as intended; i.e. collateral calls were made, and met. Despite the extreme circumstances, our data indicates that majority of schemes feel that their governance measures coped with the stressed conditions."

"I would always caution against a knee-jerk change to regulation which takes away the ability for schemes to be able to reflect their own specific circumstances"

Decision making

Nonetheless, says the PLSA, there are clearly lessons to be learnt. "This was not a universal experience," it says in its submission, "and even for those that coped very well there will be areas for improvement".

For the PLSA, these fields include further scenario testing, enhanced liquidity reviews, and adaptations to scheme governance to act quickly in crisis.

This latter area is one that the Investment Association has also highlighted as worthy of investigation. In its written evidence to the Work and Pensions Committee, the Investment Association makes the case for further delegation to eliminate the points at which communication can breakdown or be misinterpreted. "In this specific instance, decisions around whether to maintain hedging ratios and deciding which assets to sell to raise collateral once the initial pools had been exhausted, were needed more quickly than they were sometimes forthcoming," writes the body. "Anecdotally, those schemes where greater discretion on these matters was granted to the LDI manager were able to respond more quickly to changes in market conditions. As a result, we expect that more schemes will seek to delegate more of these decisions to their LDI managers in future."

Trusting stress tests

Another one of the PLSA's recommendations, additional stress testing, has also come under scrutiny.

Addressing another investigatory panel, this time The House of Lords' Industry and Regulators Committee, on 22 November 2022, Legal and General chief executive, Sir Nigel Wilson, admitted that the insurance giant — which is set to lose some £10 million in profits as a direct result of the crisis — had never stress tested a scenario such as the one that unfolded past September.

"We will now incorporate that into our stress testing," he told the committee. "And we've already doubled the headroom that the funds have, and that's an appropriate way to behave right now. When the dust has settled, there will be, I suspect, a review of the what stress testing models *[are appropriate]*."

Also speaking to the committee, the insurer's chair, Sir John Kingman, claimed that LDI vehicles were now adequately shielded from bond market fluctuations following the actions taken in the wake of the crisis.

"We have worked with the authorities to ensure that they are extremely well insulated," he said. "It was very clear that the Bank of England's objective was at the moment at which support was withdrawn, that LDI vehicles could sustain a very violent further market reaction were it to happen again."

Now, however, he said there needed to be a debate as to where LDI strategies eventually settle in terms of protective measures. It was highly unlikely that anyone would advocate returning to the status quo pre mini-budget, but trustees would have to understand that elevating levels of protection would come at a cost. "So there's some balance to be found here," he added.

Only once that deliberation is complete however, can restructured scenario testing commence.

Hidden leverage

In the search to ascribe blame, a common feature of LDI strategies – the use of synthetic leverage through derivatives – has emerged as a clear scapegoat.

During his appearance before the Work and Pensions Committee in November, independent consultant, John Ralfe, described the component as hidden leverage, which has become a problem as LDI has evolved over the years. "Hidden leverage is undoubtedly a bad thing," he stressed. "Leverage if you are being absolutely clear what you are doing, and that means being clear to the shareholders, clear to the members, clear to The Pensions Regulator (TPR) and anybody else, may be a bad *[or a]* good thing. But hidden leverage is always a bad thing."

In a speech at the Lord Mayor's City of London Banquet on 27 October, FCA chief executive, Nikhil Rathi, admitted that hidden leverage had undoubtedly concentrated counterparty risk. "I can see the need for better regulatory and risk reporting and oversight both domestically and internationally *[for hidden leverage]* and this is something we will be focusing on with our partners," he told his audience.

Given the importance of synthetic leverage for modern-day LDI, how this could be effectively regulated is debatable. At the same time, the danger of hidden leverage may decrease. As alluded to by Wilson, most schemes will be reassessing their liquidity requirements and running more extreme stress tests. This will lead to DB funds probably taking on less leverage in the future, which for some will mean lower hedging.

Margin requirements

An arguably more tangible change could appear in relation to margin requirements.

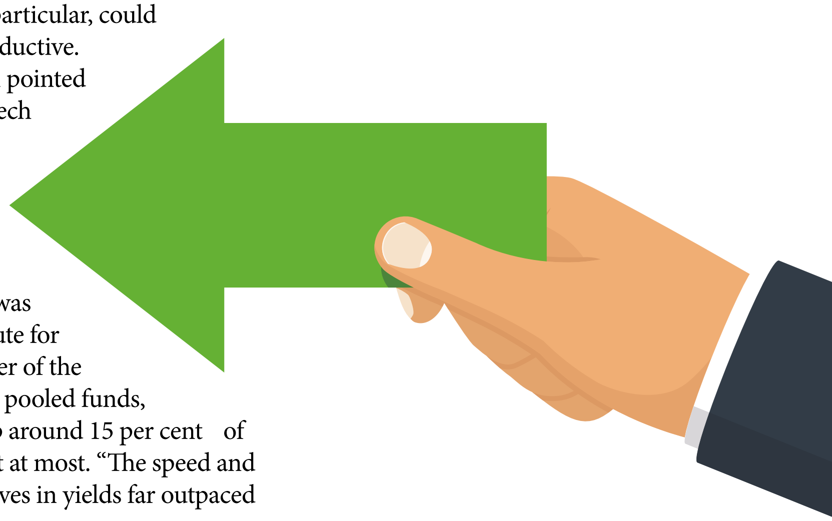
As the PLSA argues in its submission to the Work and Pensions Committee, one of the key components of the liquidity squeeze was the limited options that schemes had when posting collateral. The PLSA has suggested that regulators examine whether greater flexibility around margin requirements would have reduced market volatility and, if so, then whether they could be introduced in the future.

"This should include an assessment of whether the UK makes the 'on-shored' temporary exemption from the European Market Infrastructure Regulation permanent for UK pension funds, and associated bank capital rules, which makes this practically feasible."

Dangers of an over reaction

As is ever the case, a danger remains that increased governance, stress testing and regulation, in particular, could be counter-productive.

As Breedan pointed out in here speech at the ISDA and AIMA event in November, the LDI liquidity issue was particularly acute for one small corner of the LDI industry – pooled funds, which make up around 15 per cent of the LDI market at most. "The speed and scale of the moves in yields far outpaced the ability of the large number of pooled funds' smaller investors to provide new funds who were typically given a week, in some cases two, to rebalance their positions," she said.



Looking at improving mechanisms to further protect pooled funds could therefore be a better use of time and resources, rather than making sweeping changes across the entire LDI landscape.

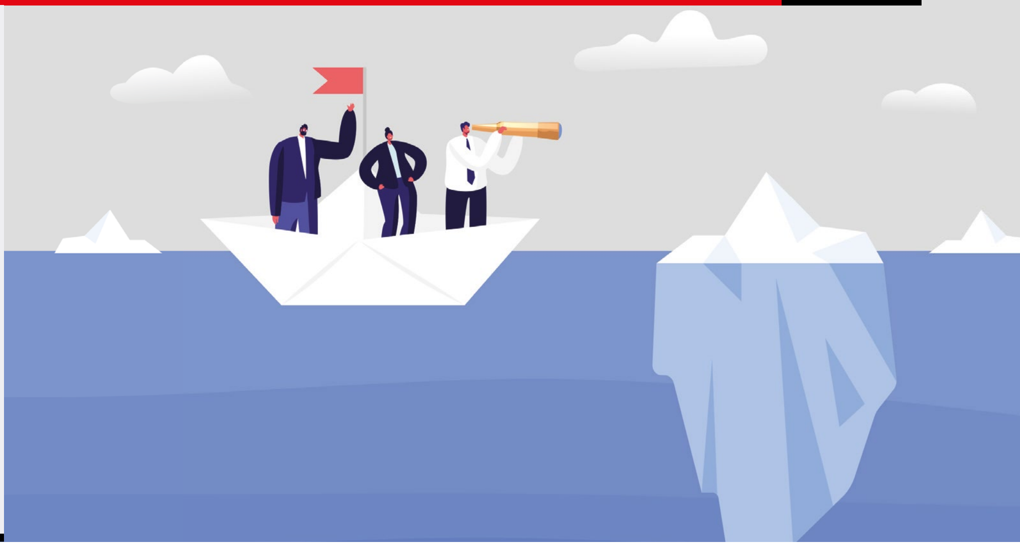
"Any governance or regulation that helps to improve member outcomes and the security of members benefits should be considered," says Hymans Robertson co-head of DB investment, Elaine Torry. "However, I would always caution against a knee-jerk change to regulation which takes away the ability for schemes to be able to reflect their own specific circumstances."

"In practice this is a well-regulated industry however, any further changes in regulation should not, as a consequence, punish schemes who have used LDI and managed their investment strategy prudently. LDI has been, and will continue to be, a useful risk management tool for defined benefit pension schemes, therefore any regulation changes should seek to support rather than diminish the use of LDI as a risk management tool in the future."

Written by Marek Handzel, a freelance journalist

Summary

- Inquiries around LDI have raised concerns around the use of derivatives to hedge liabilities, highlighting a discrepancy in the UK's transposition of the IORP I Directive.
- The Pensions Minister has recently provided further detail on the reasoning behind this discrepancy.
- Legal experts have suggested that the risk to trustees is "remote", and attention should instead be focused on the operational issues that the LDI liquidity crisis exposed.



The tip of the iceberg?

Concerns around a potential mis-selling issue have emerged as part of the inquiries around liability-driven investments (LDI), but in such a complex field, it can be hard to tell if this is a technicality, or a genuine concern for trustees. Sophie Smith reports

Inquiries into liability-driven investment (LDI) issues in DB schemes have continued over the past month, after headlines of pensions being on the brink of collapse shook the industry's standing last year.

The blame game is in full swing, as Squire Patton Boggs partner, Clifford Sims, says that there have already been rumours about potential claims against LDI managers and consultants, with pensions celebrities summoned to explain the way that LDI worked and the role of leverage in product design in various parliamentary committees.

One key issue that has been repeatedly raised as part of these hearings is over the potential use of borrowing, particularly the use of derivatives to hedge liabilities and the use of repo.

Creating a debate

This has been a growing area of focus, including in the House of Lords Industry and Regulators Committee, as Baroness Bowles of Berkhamsted argued that "there is no doubt that, economically, *[leveraged LDIs]* are borrowing", stating: "The Oxford English Dictionary defines leverage as the use of 'borrowed capital for (an investment), expecting the profits made to be greater than the interest payable'. Therefore, whether you can slide around the precise wording or not, are you not in the position of subverting the intent of the legislation?"

In response to Baroness Bowles' queries, The Pensions Regulator (TPR) investment specialist, Neil Bull, explained that while it is correct that pension schemes are not allowed to borrow money except for short-term liquidity requirements, the use of LDI focuses on two types of instrument: repos, and swaps, which are derivative instruments used by pension schemes.

"The use of derivatives is explicitly allowed in regulation 4(8) for "efficient portfolio management" and to reduce the risk," he explained.

Furthermore, Bull argued there "is a healthy debate about whether repos fall into the category of derivatives or money market instruments".

However, responding to a similar query, Financial Conduct Authority chief executive, Nikhil Rathi, said it "is clear that there was leverage and, effectively, borrowing going on in the system", stating that he would instead "wait to see what the leading opinion says on the precise technicalities of the legislation".

The devil in the detail

TPR has since written to WPC confirming that it considers borrowing as defined in the regulations to be different to the use of derivatives.

"When pension funds use leveraged LDI, they typically use swaps or 'repos' or a combination of both," TPR explained. "These derivative instruments are used in both pooled fund and segregated arrangements and allow pension funds to benefit from exposure to long dated cashflow payments.

"Regulation 4(8) of the 2005 investment regulations explicitly allows trustees to use derivative instruments. They may be used where they contribute to a reduction in risk or facilitate efficient portfolio management (including the reduction of cost or the generation of additional capital or income with an acceptable level of risk). In principle, use of derivatives in LDI funds is consistent with this provision."

TPR explained that it is not an issue that it felt required counsel on, arguing that the pensions legal profession, as a whole, has "not considered it to be a matter of significant debate".

Indeed, despite the concerns raised in the recent inquiries, Sims says that some of the critics of LDI have perhaps ignored the wholesale reform of the derivatives market that happened in the wake of the Global Financial Crisis (GFC) of 2008-9, which aimed to address systemic risks in the banking sector by introducing central clearing of trades and strengthened margin or collateral requirements.

Sims also suggests that if trustees did not have the legal power to enter into the complex financial instruments used in LDI strategies, most DB trustees would have "some serious soul-searching to do".

"The absence of a power to do something raises the spectre of acting in breach of trust and the risk of uncertainty about contractual obligations which is absolutely central to agreeing any contract, let alone a high-value investment derivative contract with millions of pounds at stake," he says.

Looking back, however, Sims says that a "basic statutory power to use derivatives could be established as far as 1997".

Echoing TPR's reasoning, Sims highlights the 2005 investment regulations, that were brought in under the Pensions Act 2004 to ensure that the UK complied with the IORP I Directive, arguing that these gave "clear authority by which pension funds may use derivatives".

"LDI as an investment strategy was built on these statutory rocks of risk reduction and efficient portfolio management", he continues, explaining: "Initially there was no linkage to borrowing in such arrangements but leveraged LDI funds became popular when LDI managers and investment consultants created pooled fund structures to capture enhanced returns from return-seeking asset classes in other structures. That made sense, especially in the low interest rate environment that followed the GFC, but in the wake of the September mini-Budget that created the liquidity crisis, it begs the question again about whether any borrowing was indeed temporary and for liquidity only.

"At one level, such an analysis will always be fact specific. But it is important to ask who was actually doing the borrowing too. Where a pension scheme uses an LDI pooled fund solution, the counterparty to any derivative transaction that has been entered into will be that fund, not the scheme. That principle applies to all financial instruments."

"We are confident of our interpretation of regulation 5 of the 2008 investment regulations, informed by the analysis of our experienced in-house legal team"

Danger ahead?

However, broader concerns have also been raised around the UK's transposition of this IORP I Directive.

In a recent Work and Pensions Committee (WPC) hearing, Brighton Rock Group head of research, Con Keating, argued that the "use of derivatives to hedge liabilities is also almost certainly illegal", stating: "The European directive limits the use of derivatives for investment purposes, for investment risk management. The UK transposition omitted the word 'investment' and added a second line, which appears to permit this.

"No English court, to our reckoning, would support that transposition. We believe that a court would just put a line through the added sentences and reinsert the word 'investment'. The use of derivatives to hedge liabilities is also almost certainly illegal."

Keating also expanded upon this issue in written evidence, making the point that, given the purpose of the directive is to protect against excessive risk taking by pension schemes, it would "seem strange that its restriction on borrowing could be easily circumvented by economic borrowing using repos".

Inquiries around the issue are still ongoing with Bowles also reaching out to WPC on the issue, while WPC chair, Stephen Timms, reached out to Pensions Minister, Laura Trott, to request further information as to whether the government took external legal advice and its reasoning for the amendments.

In her response, Trott confirmed that the transposition made reference to risks in general, rather than a specific reference to investment risk, explaining that this change was made in response to feedback on the consultation held at the time, in which the DWP explicitly set out that it wanted to allow derivatives and repos.

This is an extremely complex area, and one in which trustee knowledge concerns have already been raised, and with inquiries still ongoing, many in the industry seem to be waiting for the dust to settle, with experts even reluctant to comment on the issue to industry press.

But should schemes conducting reviews of their LDI programmes worry about having run the risk of acting illegally in entering into derivative transactions under an LDI mandate?

"In our opinion, that seems both an extremely remote risk but also one where, classically, trustees should be careful what they wish for," Sims says.

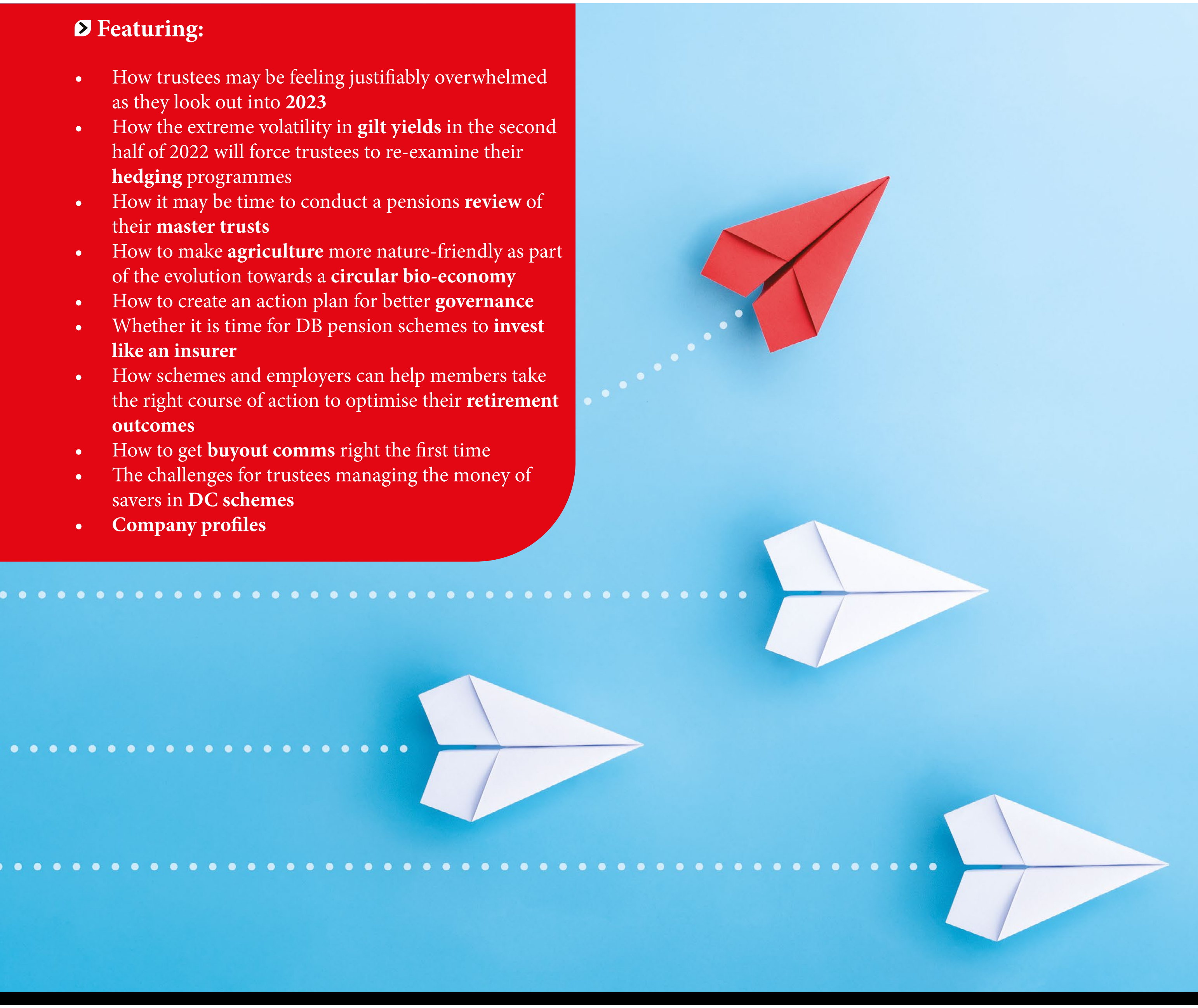
Instead, Sims suggests that it may be better for scheme trustees to spend their energy, and legal costs, on the operational issues that the LDI liquidity crisis exposed.

In particular, he encourages trustees to consider whether they understand what they are investing in, whether communications between managers, trustees and their advisers were clear, and whether improvements can be made to execution of instructions, e.g. by use of powers of attorney.

Written by Sophie Smith

Trustee Guide 2023:

New opportunities



Featuring:

- How trustees may be feeling justifiably overwhelmed as they look out into **2023**
- How the extreme volatility in **gilt yields** in the second half of 2022 will force trustees to re-examine their **hedging** programmes
- How it may be time to conduct a pensions **review** of their **master trusts**
- How to make **agriculture** more nature-friendly as part of the evolution towards a **circular bio-economy**
- How to create an action plan for better **governance**
- Whether it is time for DB pension schemes to **invest like an insurer**
- How schemes and employers can help members take the right course of action to optimise their **retirement outcomes**
- How to get **buyout comms** right the first time
- The challenges for trustees managing the money of savers in **DC schemes**
- **Company profiles**

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Trusteeship in 2023: A rocky road

With the ever-constant regulatory change and uncertain economic landscape, trustees may be feeling justifiably overwhelmed as they look out into 2023. Francesca Fabrizi explores

Summary
- 2023 looks set to be busier than ever for pension trustees working in both the DB and DC arenas.
- The constant stream of new regulation is hindering innovation and the value-add that trustees can bring.
- Trustees feeling overwhelmed are not alone and should tap into the resources that are widely available.

For many trustees, 2023 may conjure up a sense of doom. The role of the trustee seems to be ever-more challenging, with an economic landscape that remains unpredictable and regulatory change coming in thick and fast, so this year is unlikely to be any less demanding in terms of workload.

"It's hard to believe we can be busier than we were in 2022, but this year we have a huge amount to work on," says Ross Trustees trustee director, Grant Suckling. "From investment strategies and funding codes, to governance practices and environmental, social and governance (ESG) considerations, there are several key themes that are going to dominate trustee in-trays."

The buy-in and buyout markets will also remain a major factor, Suckling adds, along with continued consideration for GMP.

DB highs and lows

Specifically on the defined benefit (DB) side, trustees are still dealing with the fallout from the liability-driven investment (LDI) crisis, says Zedra Governance managing director, Kim Nash, so a lot of trustee boards will be thinking about where they are today, where they want to get to and what steps they need to take to get there. "Some will be revising their strategy, looking at how they're using their LDI funds, for example, what growth assets they need to have in place and how to structure that."

On a positive note, she says, many schemes are seeing their funding levels improve quicker than expected, so may be closer to buyout. "Some might have been working on a three to four year plan that's now looking more like two years. So there's going to be a huge volume of work with schemes trying to get themselves transaction-ready. That involves data and legal work; and talking to the sponsors about where they want to get to and how to get there."

BESTrustees president, Alan Pickering, agrees that, in DB land, journey planning will be top of the agenda; but, while some schemes will be closer to risk transfer than they were before the liquidity crisis, some will have inevitably slipped backwards. "We will need to take stock in both sets of circumstances. In each scheme, it would be useful to get a disinterested party to provide the employer and trustee with a snapshot of the different risk transfer options that exist. We can then concentrate our fire power where it is most appropriate and, in so doing, avoid wasting the time of potential counterparties," says Pickering.

DC priorities

From a defined contribution (DC) perspective, a specific focus for trustees in 2023, argues Nash, will need to be helping members with the cost-of-living crisis – communicating and trying to support members to make the right decisions. "As a trustee, you don't have oversight of a member's individual financial circumstances, so you don't know whether opting out of a pension is a good thing for them to be doing or not. So it's about what information we can provide to help members make decisions for their specific circumstances."

Trustee focus should also be on building confidence among DC members, which today is more of a challenge than ever, given recent history. "People are generally distrustful of pensions," observes Nash. "They've also seen the negative press around DB pensions, and your typical member is not going to understand the differences between DB and DC and what was happening in the markets. So there's work to be done to build understanding, and build confidence in those people that can continue to keep saving."

Retirement support

Alongside all of this, Pickering argues that a focus for trustees in 2023 should be on member outcomes and providing a joined-up journey between accumulation, consolidation and pay out.

Nash concurs that the pensions industry needs to get much better in terms of that glide into retirement for people and support them around what steps they need to make the right decisions.

"Part of that is communication and part is product development – how can you package up investments in a way that makes it easy for DC members to make a choice? That's going to take some innovation as well," she states.

Compliance versus value-add

But while innovation in pensions is arguably needed more than ever, the constant stream of new regulation is acting as a hindrance to the development of new ideas, warns Nash. "If we look back over the past 12 to 18 months, providers were having to make changes to their processes to meet regulations, so resource was being used there rather than on the developmental side, so innovation has been slower than it could have been."

The extra regulation around pensions is also adversely affecting the value-add that trustees can bring: "This year is nothing new in principle, in terms of regulation," argues Pickering, "but it is excessive in terms of quantity. Each intervention is well intentioned but often fails to take account of the implementation challenge. Because we are suffering from overload, compliance rather than added value may be the new order of the day. This would be very sad."

Indeed, one of the biggest challenges as a trustee, agrees Nash, is striking that balance between compliance and strategic thinking.

20-20 Trustees trustee director, Jim Robson, agrees that while legislation is designed to improve governance and outcomes for members, in most cases it makes sense, but in other areas less so. "If we look at the market turmoil at the end of September/during October last year, was this down to a lack of legislation? Or possibly a lack of understanding. I expect that there will be some fall out from what happened and the Work and Pensions Committee is gathering thoughts and evidence as we speak."

What Robson hopes does not happen, however, is that the mis-communication around LDI and its purpose leads to legislation that makes it harder for trustees to get on and manage schemes in the best interests of members. "Overall, we have a reasonable balance, and it's all about how trustees allocate their time and risk budget to ensure compliance, but that legislation doesn't stop them from focussing on the big ticket items and driving schemes towards their longer term objectives."

Trustees' wishlist

Looking ahead into 2023, while many trustees might therefore be hoping for less red tape, Suckling in general welcomes the extra regulation. "For a long time, the pensions trustee industry operated with limited regulation which meant, for many schemes, good governance often fell towards the bottom of the agenda.

"Our philosophy has always been that running pension schemes in the most professional way possible is beneficial to everyone involved, and as long as extra regulation is helping bring up standards across the industry, then this can only be a positive."

Instead, at the top of his wishlist for the new year is an increase in the number of experts in the industry.

"As many schemes are now fully funded, we should also be looking to find alternatives to buyout, should one day we find ourselves with capacity constraints in the insurance market," Suckling adds.

Robson echoes this argument, wishing that 2023 would not only bring with it more time but also more resource.

"There is a full agenda for 2023, and a lot of issues to address. We are seeing a lack of resource in all areas – administration, investment consulting and the insurance market to name but three."

Schemes also need to think about how they can do things differently, he says.

"We need to reflect that schemes mostly operate on a cycle of four meetings a year. That makes decision making and implementation too slow in my book. Schemes should really look at their governance model and perhaps consider moving to more frequent, shorter and more focused meetings. This really helps order the agenda, and what areas can be delegated to allow the trustees to focus on strategic matters," Robson adds.

There is no question, concludes Nash, that the demands on the pension trustee have been increasing year-on-year and that, compared to 10 years ago when she entered trusteeship, the role today feels "fundamentally different in terms of what the requirements are and what you're expected to do".

But for the trustee who might be feeling overwhelmed looking into the year ahead, the message she would offer is that they are not alone: "You are working as team, as a trustee group. You have your adviser there, whose job is to support you and help you to understand. If you do not understand something or you feel it's too complicated, that's a failing on your adviser's part.

"So link in to the resources you've got around you. Ask questions and take the support that's on offer to you. You are not alone."

Written by Francesca Fabrizi

Learning lessons from the 2022 liquidity crisis

The extreme volatility in gilt yields in the second half of 2022 will force trustees to re-examine their hedging programmes. CDI has been found wanting

From September to October 2022, inflation-linked gilt yields rose nearly 2 per cent, twice, each in the space of a week. This volatility was the result of an unprecedented sell-off by pension schemes who lacked liquidity to support their liability hedges after inflation sparked a wave of panic.

Markets have recovered, but the volatility has caused lasting impact to many schemes and forced trustees to re-evaluate their liability hedging programmes.

What went wrong?

Schemes that struggled in September and October generally combined too much leverage with too little liquidity in their matching portfolios. Many of these schemes moved a material proportion of their interest rate hedges out of gilts and into higher yielding, less liquid credit and infrastructure securities using an increasingly popular hedge framework known as cashflow-driven investing (CDI).

There is nothing inherently wrong with CDI: A fully-funded scheme with a hedgeable liability can take a literal approach to CDI and simply match bonds with future cashflows. Because everything is aligned, trustees can take comfort that interest rate risk is fully hedged and that assets are designed to become liquid at exactly the right time.

However, UK funding is more complicated:

- In general, UK pensions are well funded on a 'technical provisions' basis. To maintain this, scheme assets need to earn excess returns to keep pace with liabilities.
- UK liabilities are complex, most cannot be hedged with a static portfolio of bonds.

The dual objectives of full hedging and excess return generation have forced Trustees away from pure CDI into something much riskier. Moving out of gilts degrades the quality of the hedge and reduces liquidity, while adding leverage to create a full hedge ratio increases the need for liquidity – creating conflict.

Leverage, investment risk, and illiquidity have historically been a dangerous combination and schemes paid the price.

2022 crisis!

Interest rates had risen steadily throughout 2022 and the surge accelerated in late September. As yields rose, schemes began to accumulate losses on their matching portfolios. As losses mounted, schemes received cash demands on short notice, they were not prepared. Many schemes were forced out of their hedges to avoid insolvency.

Schemes with high hedge ratios and limited liquidity fared worst. CDI is not the only culprit in the crisis, but the tendency towards illiquidity in CDI portfolios caused significant problems.

What can we learn?

The recent crisis highlights weaknesses in typical matching portfolios:

- Cashflow matching ties up capital and leaves little room for growth assets or liquidity reserves
- Illiquid LDI can be prohibitively expensive to sell on short notice
- Leverage increases the potential need for additional liquidity
- Rebalancing cashflow-driven strategies can be a burden

Trustees will use the lessons from 2022 to review and strengthen hedging programmes. Schemes should take a hard look at their return-focused CDI programmes and consider expanding to a broader definition of liability hedging, which is commonly called liability-driven investing (or LDI). We highlight the key differences below:

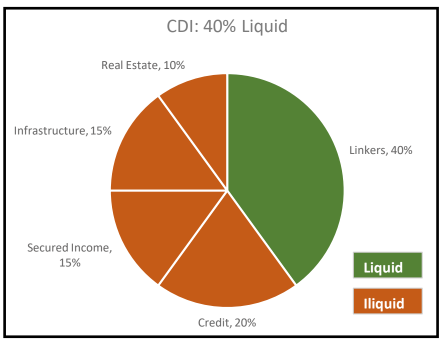
CDI	LDI
Seeks to meticulously buy a bond to match every cashflow	Aligns to the sensitivities of the liability as rates and inflation changes
Seeks to minimise the need for cashflow management	Willing to reinvest income or sell liquid assets if it makes economic sense to do so
Prioritises investments that provide both hedging and return generation	Separate growth assets from matching assets to improve the outcomes for both
Seeks returns from more risky and less liquid hedges	Hedge with liquid capital efficient gilts/ linkers and earn returns from a separate growth portfolio

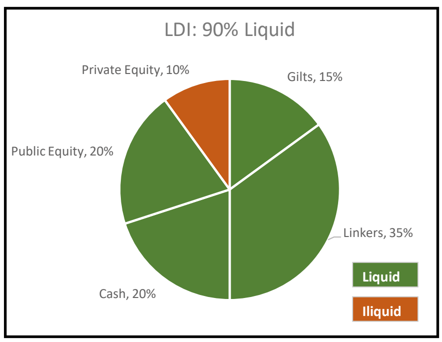
During the crisis, the most successful schemes had large pools of cash and significant additional liquidity buffers.

Strengths of full LDI

Fully utilising LDI requires more work and often works best with a fiduciary manager who has the tools to advise, oversee, and manage cashflows and hedge overlays. LDI captures most if not all of concepts behind and benefits of CDI while avoiding the blunt singular matching framework of just cashflow.

While the concepts are the same, LDI generally leads to significant differences in the asset allocation. Below is a comparison of typical portfolios in each framework:





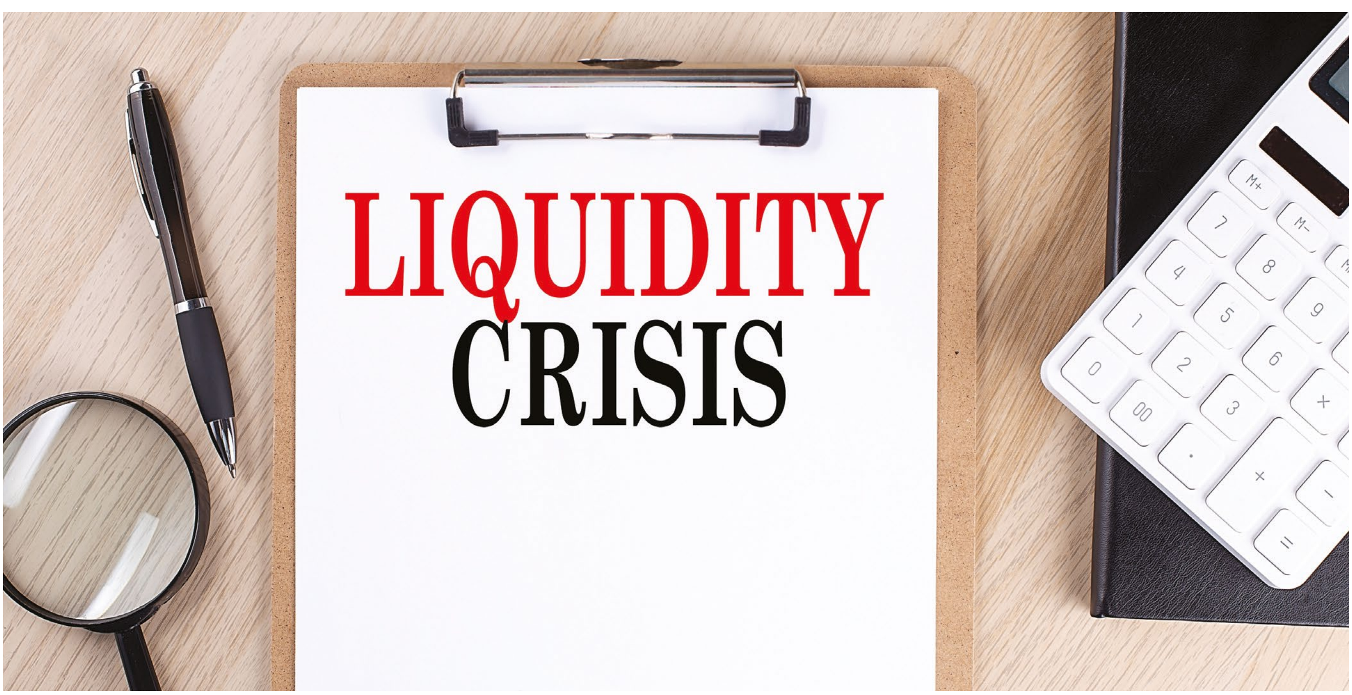
In conclusion, comparing the two portfolios:

Link to liability: Both portfolios match the liability with bond-like investments linked to the maturity and indexation liabilities.	Tie
Precision: Inflation-linked gilts are more closely linked to indexed cashflows than infrastructure debt and a liquid bond portfolio can be rebalanced between gilts and linkers as inflation changes.	Winner: LDI
Return potential: Is higher for the LDI portfolio as excess returns can be sourced from anywhere and are not required to come from matching assets.	Winner: LDI
Liquidity: The LDI portfolio has more liquidity as all hedges are liquid, public market growth assets are more liquid than typical CDI return generators. This efficiency leaves room to dedicate an allocation to high confidence illiquid alternative investments like private equity.	Winner: LDI

Ironically, although CDI is often chosen for its direct focus on matching, liquidity, and excess performance, moving away from direct cashflow matching to a broader LDI framework can lead to significant improvement on all fronts.

Written by SECOR partner, head of strategy and risk, Scott Freemon

In association with SECOR ASSET MANAGEMENT



Stick or twist?

Many UK companies opted for a master trust for the first time in 2012 to meet their auto-enrolment duties. A decade on, Standard Life head of master trust, Donna Walsh, says it may be time to conduct a pensions review

Driven by technical innovation, since the start of great auto-enrolment reforms, the world has seen huge changes such as the first Apple watch, Uber in the UK, the rise in social media and development of the Cloud.

Not surprisingly, both individual companies and pension providers have also raised their game with vastly improved pension schemes for their staff and clients. In such changing times, it can make sense to test the market frequently on value, quality and innovation and even on 'evergreen basics', such as caring for colleagues. These could have such a profound impact on employer and member experiences. We know just how crucial it is to look after our people so they in turn can look after clients and members.

From master trust to master trust

A master trust is a multi-employer occupational scheme with every employer having its own section within the trust. Coming in all shapes and sizes, the 36 authorised master trusts are offered by financial services firms such as Standard Life, a brand with a 200-year-old history; consultants and independent providers and the government-backed provider Nest. Master trusts are governed in a similar way to traditional trust-based schemes, with rules on value for members' assessment, chair's statement, and statement of investment principles, for example.

Reviewing and selecting a master trust is a complicated task as there are many factors to consider, including trustee and governance set-up, investments, administration and service levels, member communications and the commitment of the pension provider. Advisers will scrutinise across each of these areas to support employers with their review.

Even after a review, some employers, (and their advisers) may come to the conclusion that their own in-house offering or existing master trust is the most suitable for them and their staff. Others can be apprehensive about change given system, data and member communication considerations, but with specialist implementation and member engagement teams coupled with good relationship management, these obstacles are often not insurmountable. Whatever the outcome, such an exercise can be enlightening, even if you decide simply to 'stick'.

This check list is a quick way to see whether your existing master trust is still right for you or whether it might be time to 'twist'.

Review your master trust: 20-point check list

1. Pensions are long term – how long has your master trust provider been in business? Is your provider continuing to adapt and evolve in line with changing needs?
2. How financially sound is your master trust provider?
3. How does your master trust compare against your companies' values? For example, are your sustainability objectives aligned with your staff pension provision?
4. How are your members treated when facing uncertain times?
5. What is the quality of governance like?
6. How quickly can the independent trustees act in times of crisis?
7. How easy is it to administer your scheme?
8. Have there been any admin hiccups recently?
9. What service levels are your members experiencing? For example, do members have to wait longer than a minute for calls to be answered?
10. How satisfied are your members with digital and telephone interactions?
11. How many fund options does your master trust offer, including ESG, that suit your own employees' profile?
12. How easy is it to switch funds at a click of a button?
13. How good are the member communications?
14. How personalised are member experiences?
15. How easy is it for members to take the next step after nudging?
16. How flexible are the retirement options?
17. Does your master trust offer all retirement options to members?
18. Does your master trust support investment pathways into retirement?
19. How transparent and inclusive are charges? Are there any hidden extras?
20. Lastly but not least: can you show any proven member outcomes? How are they benchmarked?

At Standard Life, we don't just tick the boxes we always aim to deliver the best experience for employers and their members. If your master trust doesn't get full marks perhaps it may be time to 'twist'. If you are tempted to move, make sure advisers have a central role in your choice; they know the market and can select the most appropriate master trust for you and your employees

In my view, the most important thing for employers is to consider carefully what they want to achieve and what outcomes and service they want from the master trust. For one of our new clients their objective was clear. They said: "The financial wellbeing of our people is of paramount importance to us, so choosing the right master trust was a critical decision and one which we didn't take lightly. Following an extensive tender process, we eventually selected Standard Life as our partner as they were able to deliver a truly member-centric proposition, backed by impressive administration. One year on and we have not been disappointed."

What is most important to you and your employees? Finding the right master trust may not mean staying with the master trust you know best.

If you have not reviewed your master trust provider for a while, now may be the time to do so. Your existing master trust provider may no longer be the best performing or most innovative. It may even fall short on areas that may be important to you such as financial wellness support or caring for members when they need it most.

We really care. We always listen to employers, their advisers and members. We continually adapt our offerings as regulation, technology and members' needs change. So, why not visit the Standard Life website, where you can read more about key considerations should you decide to 'twist'. You can also learn more about the truly trailblazing research and solutions from Standard Life here:

SCAN ME

Written by Standard Life head of master trust, Donna Walsh

In association with Standard Life
Part of Phoenix Group

How can we make agriculture more nature-friendly?

It's time to rethink our current wasteful and unsustainable farming practices. As part of the evolution towards a circular bio-economy, we need to replace toxic and inefficient methods that deplete nature in favour of regenerative agriculture, precision farming and nature-positive techniques, finds LOIM's Alina Donets and Pascal Menges

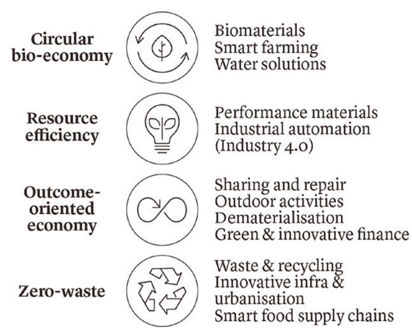
Sustainable food systems and the circular bio-economy

Humans have overconsumed the earth's resources for generations in a way that threatens to cause irreversible damage to vital land, water and biological resources. However, technology and innovation are enabling an evolution to a new, circular bio-economy – where resources are renewable, sustainably managed, recovered and reused as much as possible.

At LOIM, we recognise that nature is one of the most vital and productive assets in our economy. Our Natural Capital strategy invests in companies that leverage nature's regenerative power in order to benefit from strong secular drivers that translate into resilient financial performance.

Addressing food waste, promoting sustainable food systems, and paving the way for environmentally friendly farming techniques are all ways to protect and harness nature's own capabilities while improving resource efficiency and fostering a leaner form of industry. Commercial solutions are available to improve the efficiency and productivity of agricultural practices, and Natural Capital aims to play an important role in this transition.

Sustainable food systems are aligned with the circular bio-economy, one of four investment sub-themes and growth opportunities in our Natural Capital strategy.



Source: LOIM. For illustrative purposes only.

Inefficient and toxic agricultural production

Agriculture alone drives 80 per cent of global land-use change[1] and 70 per cent of global freshwater use[2], and it is a threat to 86 per cent of species at risk of extinction[3]. In addition, agriculture remains associated with unsustainable practices such as monocropping and heavy tilling, or working the soil when it is too wet and not ready for turning. This can disrupt soil structure and quality, accelerating surface run-off and erosion, while reducing the variety of landscapes and habitats.

Current food production depends heavily on the use of fertilisers, pesticides and water. It harms wildlife through water extraction and reduces water quality because of soil and chemical run-off. Downstream pollution, especially from fertilisers, further damages marine systems.

Excessive fertiliser use and disruption of nitrogen and phosphorus nutrient cycles have already led to the degradation of one-third of soils, with 90 per cent potentially at risk by 2050[4]. It is also one of the planetary boundaries that have been already transgressed.

Insufficient regulation

While environmental damage in the agricultural sector is widely recognised, regulatory action has been insufficient. Regulators are looking to rectify this through programs such as the European Commission's Farm-to-Fork initiative. Launched in May 2020, this 10-year strategy aims to address the challenge of producing and consuming food within the capacities of the planet.

In China, more inroads are being made towards sustainable farming practices. In 2021, the government issued its 14th Five-Year National Agriculture Green Development Plan. Resource protection, pollution control, restoration of agricultural ecology, and the development of low-carbon agricultural industrial chains were all identified as key goals to be achieved from 2021 to 2025.

Agricultural technology solutions

The future of food does not have to feature scarcity, pollution, and the degradation of soil and water ecosystems. Commercial solutions to these problems exist. Our Natural Capital strategy seeks to find companies that are making positive strides toward addressing the sustainability challenges in agriculture.

A number of technologies have already been introduced such as:

• smart and precise irrigation that helps save water and reduces crop strains

• precision application of fertilisers and pesticides that reduces the amount of chemicals sprayed while achieving the same yield enhancement potential

• no-tilling practices that preserve the nutrients within the soil

With greater technological advances, innovation is continuously pushing forward – creating superior precision and significantly greater integration of vast amounts of data, including geological and weather conditions – all to benefit the soil and ecosystem growth while persistently optimising yields.

Furthermore, innovations in the bio-economy include safe and environmentally sound breakthroughs in seed development, green chemistry for crop protection and yield enhancements. Consumer preferences are also incentivising a larger proportion of farmers to shift toward sustainably-aligned, organic or biodynamic means of operating their fields and farms.

Given the vulnerability of global supply chains – where disruption can significantly alter agricultural commodity flows as well as the availability of core chemicals widely used to ensure productivity – even greater investments are pouring into this space.

Due to constrained land availability and looming climate change, agricultural systems are set to become more self-sufficient and trade-independent. This further shifts the sector mindset toward innovation, exercising greater care over natural resources, and, eventually, a willingness to allocate capital to enhance and upgrade the system.

Reimagining farming

We need to farm in a more nature-friendly way, replacing wasteful practices. This can be achieved through combining technological innovation with time-tested practices of regenerative agriculture to improve yields and minimise harm to natural resources.

Precision agriculture leverages a range of technologies aimed at achieving efficiency according to the '4 Rs' principle: the right source, in the right rate, in the right place, at the right time[5]. By 2030, precision agriculture could provide up to 200 million more tonnes of crops[6].

Software systems connected to machinery can help farmers work more efficiently with high-degree sensors and application sprayers, while optimising the amount of inputs needed.

Precision irrigation, for instance, can help dramatically reduce water usage by targeting the roots of plants and monitoring soil conditions. Variable rate irrigation was found to potentially imply water savings of up to 25 per cent[7]. Smart farming equipment must be complemented by digital technologies. These can help ensure that farmers do not irrigate before rain, for instance.

Precision farming also helps reduce soil compaction, run-off and erosion[8]. Several studies show that herbicide use, for instance, could be reduced between 11 per cent and 90 per cent by precision application in different types arable crops[9]. Digital tools also enable more regenerative farming techniques.

Increasing the autonomy of machinery through better connectivity could create as much as $60 billion of additional value by 2030. By establishing better connections between soils, farm equipment and farm managers, as much as $175 billion in value could be unlocked[10].

Natural fertilisers and pesticides

Using more bio-fertilisers and bio-pesticides that enrich soil health and increase resilience to drought and flooding could help offset the negative impact of synthetic fertilisers and pesticides. If 10 per cent of chemical pesticides were replaced with biologicals, 250 million tons of chemicals could be kept away from our ecosystems[11].

Regenerative agriculture focuses on strengthening soil health, increasing land productivity, promoting biodiversity, and controlling foreign species through practices like crop rotation, intercropping and reduced tilling. Other benefits include close to a 40 per cent reduction in nitrogen run-off.

Finding solutions

The future of food will depend on nature-friendly commercial solutions, improved efficiency and innovation. These include precision equipment that reduces nutrient and pesticide run-off and soil erosion, smart-farming systems and the use of bio-based fertilisers and pesticides.

Our Natural Capital strategy seeks out companies that are aligned with the circular bio-economy, including those developing or providing agricultural solutions that address efficiency, productivity and sustainability challenges with technological and digital innovation, seed science, biological and green chemicals, and an overall integrated, sustainable approach to farming.

Written by Lombard Odier Investment Managers portfolio manager, Alina Donets, and head of research and investment process, Pascal Menges

[1] Chatham House (2021)
[2] World Bank (2017)
[3] UN Environment Program (2021)
[4] UN Food and Agriculture Organization (2015)
[5] Chatham House (2021)
[6] "Innovation with a Purpose: The role of technology innovation in accelerating food systems transformation," World Economic Forum (January 2018).
[7] (Sadler et al. 2005, Evans et al. 2013)
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Maintaining good governance

Sue Austen explains how to create an action plan for better governance

All pension schemes need exemplary standards of governance. From trustee recruitment and engaging with savers, to delivering large-scale one-off projects such as GMP equalisation, there are many different aspects to effective, efficient scheme management. Maintaining good governance ensures that members' pension savings work hard, are kept safe and provide them with the outcomes needed at retirement.

Governance is the backbone of every scheme – whether it is defined benefit (DB) or defined contribution (DC) trust-based, master trust or group personal pension (GPP); managed by a third-party or an in-house executive team. The structure may differ, but the actions that schemes' governing bodies need to take in fulfilling their day-to-day activities and achieving long-term goals remain the same.

Here are nine steps that should be in every governing body's action plan. They will help to ensure the correct resources, skills, dynamics and operational efficiencies are in place to manage savers' pensions on their behalf.

Map out short-term projects and longer-term goals
Creating a roadmap for the future strategy will help governing bodies to identify their priorities and the risks and opportunities that are likely to have greatest impact – positive or negative – on their goals. This will help in building appropriate risk management, training plans and budgets. This roadmap can also help to identify the pace at which projects can be tackled, or what resources are required and where specialist skills from advisers or others might be needed for a short-term project, or at a particular point in a longer-term exercise.

Match structure, operations and skills to the programme of work
Now that the activities have been mapped out, think about the skills and expertise that the governing board needs both day-to-day and to complete its long-term programme of work, and how best to align the sub-committee or working party structure to these activities. Also, agree how the day-to-day operations will work and who will oversee actions. Here a strong board secretary can be invaluable in driving actions forward and ensuring information is provided to the board at the right time to facilitate good decision-making. Governing bodies should identify which required skills are already available, and where there are gaps.

Launch recruitment exercises to fill gaps in board expertise and for succession planning
Once governing body members understand the skills and characteristics that the governing body will require for the future, they can use this as the basis to recruit people with the required traits and talents when they are needed. Succession planning should also form a part of this process. Governing bodies need to keep track of when tenures will finish, what this will mean in terms of future skills gaps and how they will nurture existing or new governing body members to replace the knowledge and experience of departing ones.

Rethink recruitment methods for member-nominated trustees (MNTs)
With a trustee board structure, driving better diversity of thought can mean breaking the mould of how trusteeship is perceived and how trustees are recruited. Encouraging scheme members to put themselves forward as member-nominated trustees may mean rethinking recruitment processes and the language used to describe the role. Potential candidates may be deterred by advertisements that suggest they need to be an investment expert, or know everything there is to know about actuarial valuations. Trustees are not expected to know everything – but, crucially, they need to be confident in asking questions, be comfortable in a board role and happy to ask challenging questions that will hold the experts who support the scheme to account.

Recruitment advertisements can instead emphasise aspects of the role such as working in a team, or that they will be helping their colleagues gain better financial security in retirement. It is important to move away from tick-box evaluation of particular experiences, and make the role of trustees seem a more inspiring and a personal story. Rather than a text-based advertisement, it could also be helpful to record videos or create other materials that give potential candidates a more dynamic insight into the role of the trustee.

Create an inclusive board
Effective decision-making is crucial to good governance, and that means ensuring the board includes people with a variety of different views, experiences, cultures and thought processes. However, simply appointing individuals from a variety of backgrounds does not guarantee diversity of thought. It is also essential to ensure that everyone feels comfortable and confident in asking questions, putting across their views and contributing to discussions to make good quality decisions. Bringing different ways of thinking and valuing every individual for the contribution they can make is vital, and that means recognising the strengths that difference brings.

For example, one individual might feel at home with discussing high-level strategic overviews, whereas another may want to focus on intricate detail. Both of these approaches are fundamental to the success of projects but could be a cause of friction in a meeting. As part of good governance each board member must be able to recognise and respect the value of others' points of view – and this can also require additional training.

The same approach can be used equally successfully for governance committees.

Encourage sponsors to promote the benefits of pension board membership

Sponsors can also help encourage employees to apply for roles – whether as MNTs or employer-nominated representatives. Messaging from the scheme sponsor might focus on supporting employees who are ambitious and aiming to pursue a board-level career. Trusteeship is an excellent stepping-stone to understanding how a corporate board functions and how successful decisions are made. It is a great way of supporting people who want to advance their career within a company, to have a better understanding of financial information and to connect with other senior individuals who are already on the pension board. This also helps to introduce people onto the board who are at different stages in their career and should support greater diversity of thought.

Look to the long term

Recruiting trustees does not just have to be about filling current vacancies – it can also be about nurturing individuals for the future. For example, promising candidates who are not successful in a MNT election could be excellent future prospects for board positions. This will enable the scheme to build a talent pool to support future appointments and other projects.

Think about other key people

Succession planning and maintaining the right balance of skills does not just apply to governing bodies. In-house pension schemes are also exposed to the risk of losing key people, such as managers, experienced administrators or investment specialists. Many DB schemes have become legacy arrangements with teams that are shrinking in size – but are still managing the pensions of thousands of people, as well as billions of pounds of assets under management. With shrinking teams, it becomes increasingly difficult to maintain the breadth of resources and skills that they might have done in the past and to have the flexibility to deal with additional projects alongside everyday business. Identifying which employees are a key person risk, and deciding when it is appropriate to bring in additional expertise to handle ad hoc projects is also important.

Include advisers and other experts in plans

While governing body knowledge and experience are crucial to ongoing governance, there may also be occasions when the board needs to rely on external experts to support ad hoc projects. Boards can identify these pressure points in their roadmaps and use this as a basis for discussing needs with their current advisers and others in the market. That should include understanding costs, lead times and the scope of future work.

Analysing and documenting future scheme needs, identifying the skills and resources needed, encouraging diversity and inclusion within the governing body to help better decision-making and nurturing talent for the long term are all vital elements of governance for schemes of all types. By working closely with advisers, the sponsor and members, boards can be confident of maintaining robust management processes that will deliver good member outcomes over the long term.

Written by Aon associate partner, Sue Austen

In association with

AON

Time for change?

Jon Exley, head of solution innovation at Schroders Solutions, considers whether it is time for defined benefit (DB) pension schemes to invest like an insurer

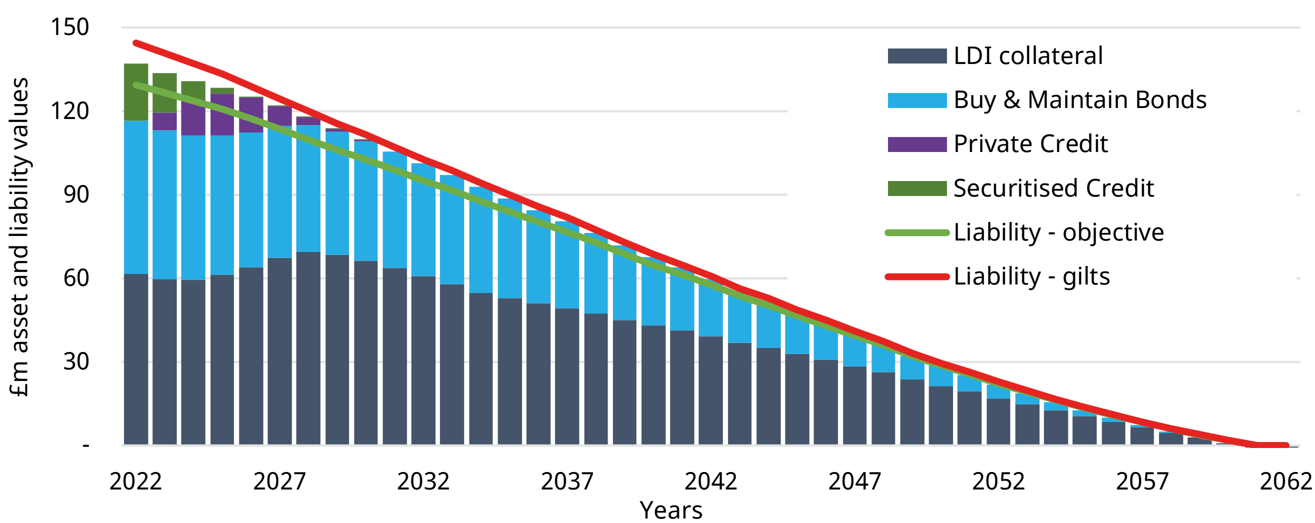
Most DB pension schemes benefitted materially in funding terms over the last year. Sharp increases in gilt yields have meant that many schemes are now close to fully funded on a more prudent 'low dependency' funding basis. A low dependency basis is consistent with investing in low-risk assets, reducing reliance on the covenant, and increasing security for members.

What does this mean for trustees setting future investment strategy?
It is a shift in mindset for trustees. The emphasis moves away from 'well-risk managed growth' portfolios to the mindset of our insurer clients where their core aim is to achieve 'stability and certainty of return'.

How do insurers invest their assets?
Solvency II regulation and sound risk management principles encourage insurers to invest conservatively to ensure they can meet their obligations, even in very stressed market scenarios. This means a strategy with less reliance on equity markets or manager skill. Instead, they invest in more secure and contractual assets, such as high-quality corporate bonds and infrastructure debt, intending to hold those assets to maturity. The contractual nature of these assets means 'locking in' yield at the outset (assuming they set aside adequate reserves for any potential impairment or default), giving more certainty on meeting those obligations in the future. Through derivatives and other means, an insurer will also remove unwanted risks, such as interest rate and inflation risk, with low leverage. This is the same philosophy of cashflow-driven investment (CDI) strategies used by, and becoming popular with, pension schemes.

The below chart illustrates a CDI strategy. It shows the forecasted values of a CDI portfolio against a DB pension scheme's projected liability values. We can invest a CDI portfolio across the risk and illiquidity spectrum, considering scheme circumstances. For example, this illustrative solution includes the building up and running down of a private credit portfolio in the early years.

Illustrative CDI portfolio relative to scheme liabilities



Source: Schroders Solutions, for illustrative purposes only

By investing like an insurer, a scheme can achieve several things:

- Improve the certainty of outcome by reducing the reliance on market returns (beta) or the need for manager skill (alpha)
- Increase the certainty in delivering member benefits
- Invest in line with end-game objectives

Consistent with endgame objectives

For schemes targeting buyout, investing in similar assets to an insurer's investment portfolio can provide a match for annuity pricing when the time comes. For trustees looking to run their schemes on in a low dependency manner, a CDI strategy is also attractive. CDI portfolios of schemes targeting low dependency may differ from that of a client targeting buyout. For example, these portfolios may hold a wider range of private credit and infrastructure equity, and longer-dated assets. This can be attractive assets for clients with a longer time horizon and offer attractive risk-adjusted returns at present.

Have a 'Plan B'

As a final thought, the recent rise in gilt yields has meant that there has been a surge in demand in the bulk annuity market. This has risen to a point where it is not clear how many schemes the market can absorb, and whether some schemes cannot transact for a period of time. For schemes targeting buyout in the short to medium term, having a 'Plan B' is going to be important. Instead, seeking to invest like an insurer may be the best way to ensure certainty of the outcome, and ultimately greater security for members.


Written by Schroders Solutions head of solution innovation, Jon Exley

In association with
Schroders solutions

Navigating the challenges ahead

Jonathan Watts-Lay looks at the challenges members may face in the year ahead, including the increasing pressure from risings costs and how this may impact pension savings, as well as the key considerations for members approaching retirement. With this in mind, he also outlines how schemes and employers can help members take the right course of action to optimise their retirement outcomes

Since the pandemic, people have been faced with a multitude of challenges impacting their finances and none more so than the cost-of-living crisis. It is therefore more important now than ever that members are engaged with their pensions.

Protecting pensions

Recently, the pressures on household income has raised concerns that members will look at their pension contributions as a way of cutting back on their monthly costs. But is this what is happening in reality?

According to PLSA's survey the first signs of the cost-of-living crisis in pensions are beginning to emerge. It found that one in five (19 per cent) pension schemes have seen members asking about reducing or stopping their pension contributions and 17 per cent wanting early access to their pension after age 55.

However, the Department for Work and Pensions latest figures show that there has been no indication that pension savers are actually taking action, as there has been no significant rise in people who are currently saving into workplace pension schemes choosing to stop contributions. But there does appear to be an upward trend for those newly enrolled choosing to opt out. The PLSA survey also noted that only around one in 10 (12 per cent) schemes surveyed said that they have seen members wanting to opt out, which is only slightly above the long-term trend of 9 per cent.

However, as the cost-of-living crisis continues, employers should closely monitor pension opt-out requests and do all they can to ensure pension scheme members recognise that it really should be a last resort.

It's important for members to understand that opting out of their pension can have a huge impact in the long term and could be damaging to their standard of living during retirement. Whilst reducing contributions now would make relatively small savings each month, the impact on a member's retirement savings in later life can be dramatic, due to lost employer contributions and tax relief.

Making the smallest reductions in contributions possible, and avoiding opting out altogether, will limit the reduction to future retirement savings. However, saving money is a habit, and once it has stopped, it can be very difficult to start up again.

There are some practical steps that members can take to save money that they may not yet have considered. Whilst some of them seem small, they all add up. This includes checking all outgoings to find other ways to save money such as cancelling any unused subscriptions or memberships, shopping around for better deals on insurances at renewal such as car and household insurance, as well as broadband and mobile suppliers, and switching brands on their regular shop. Rising energy costs are a big concern so things like avoiding tumble dryers, utilising smart heating, using more efficient light bulbs, and finding cheaper ways of cooking such as using a slow cooker or microwave can all help. It's always a good idea to look out for online discount vouchers for any purchases, and it's also an ideal time to remind members of cost savings available through the workplace as part of their benefits package e.g. discount on parking, shopping, car leasing, medical care and insurance. Financial education and guidance delivered in the workplace can really help members understand these issues and help them to protect their future retirement savings from unnecessary damage.

What about those considering retirement?

While the cost-of-living increases means that it is a difficult time for many, it is particularly challenging for those planning to retire, especially when faced with a fall in the value of their pension due to market volatility. In this climate, it's particularly important that members are informed and understand the key issues to be considered if they are to optimise their retirement outcomes.

Many will be questioning if they can afford to retire right now. In fact, research by an insurance provider found that a third (33 per cent) of those planning to retire in the next five years are changing their retirement plans due to the current cost-of-living crisis. Financial education can help members to work out a financial plan for retirement and understand what costs they need to think about in retirement, the impact of inflation and if they can afford to retire. Some may even realise that as they are likely to be paying less income tax, no National Insurance, mortgages and loans may be paid off, and that they will have no more pension contributions – retirement may actually be more affordable than they thought. Or, if these savings are still not going to be enough, it may help them to consider if they should delay retirement or if working part-time could be the solution.

As well as this, members should be aware of the common pension pitfalls that people fall into when accessing their pensions so that retirement income is optimised. This includes paying unnecessary tax, not shopping around for the most suitable retirement income option, or even falling for a scam which unfortunately members who may be struggling with their finances could be particularly vulnerable to.

What should be done?

As part of an overall wellbeing objective, many employers now offer their workforce support to help them understand the value of their pensions and workplace savings, as well as how to best manage their money in times of crisis.

Supporting members with their day-to-day needs, especially in the current cost-of-living crisis, should be a key area of focus, alongside support around longer-term needs such as pensions and retirement savings. This means offering financial education programmes that help with a full range of money matters throughout their career, from debt and money management to preparing for retirement. This includes providing financial education workshops, one-to-one guidance or coaching and digital tools and helplines.

When looking at how to provide this support for employees and members, it can be daunting knowing where to start. However, there are specialist providers available who can help with all of this.

But before going ahead with a provider, carrying out due diligence on them first is crucial. This should include checking that any financial education and guidance providers are workplace specialists with experience in providing support to members. Due diligence on regulated advice firms should cover areas such as; qualifications of advisers, the regulatory record of the firm, compliance process e.g. compliance checks of 100 per cent of cases, pricing structure, and experience of working with employers and trustees.

Ultimately, empowering members by providing them with access to appropriate support at the right time can improve financial capability and resilience, and help them to navigate any challenges that may lay ahead, which should result in better retirement outcomes for all.

Written by WEALTH at work director, Jonathan Watts-Lay

In association with WEALTH at work KNOWLEDGE | EXPERIENCE | OPPORTUNITY

Buyout comms - avoid the headaches!

Julia Fox explains how to get buyout comms right the first time

DB schemes are winding up left and right. At this point, the Quietroom team has worked on more of the accompanying communications than we care to count.

We've been asked to step in when buyout announcements go down badly. We've been called up to navigate the regulatory red tape of surpluses, AVCs and transfers. And (when we're lucky) we've been there from day one to help members understand and make the whole process easier on everyone.

It's gotten to the point where some of us could communicate buyout in our sleep. (At least one of us literally has.) So instead of reinventing this process, we decided to perfect it – into one suite of excellent member communications that any scheme can use.

We could avert disaster, but who was recording 'good feeling'?

When we set out to create a set of model buyout comms, we were aware which messages were likely to do well. We knew how to frame the buyout positively, when to reassure members, and where all the requisite legal messages slotted in.

What we didn't know was how members received them. There were no complaints, few calls, and even a couple of reports of happy members giving good feedback. But no data.

How well were people really understanding the journey to buyout and the reason for it? Who recognised that their scheme was closing? Was there anyone who just didn't understand a surplus well enough to get in touch?

It was time for proven member outcomes

Instead of relying on positive feedback, we took our buyout comms straight to members. We got their first impressions and asked what they would do with the information. We asked if they understood it all, and then we quizzed them. If anything didn't hit the spot, we rewrote it until it did. And for all our experience, we learned a lot. Including:

1. Members want all the information, or almost none of it

Do you want to explain journey planning, covenants, and insurer ratings? Or just tell members their pension will continue to be paid for the rest of their lives? Because the hybrid approach doesn't work.

When we alluded to the wider context, members had questions. And when they have questions, they pick up the phone. So give them detail, or stick to the headlines.

2. Burying surplus options will get you into trouble

We've already seen what happens when members feel they don't have all the information they're owed about a surplus. (Spoiler, it involves a select committee and intervention from the regulator.) So we wanted to test which level of information members understood best and responded to positively. The winner? Total transparency.

Don't hide information for fear of your members' reaction. It's not just a bad idea, it tends to bring about the very thing you're trying to avoid.

3. You can't claim comprehension until you've tested it

In some of our earlier drafts, members reported that they fully understood the message. But when we tested them, some

couldn't recall important details and a few actually got it all wrong. Of course we want members to feel confident that they've understood something – but more than that, we need to make sure they really have.

Unfortunately, no one is a better communicator than a scammer. If you leave room for questions, you risk your members getting 'answers' in the wrong places.

What we don't know CAN hurt us

Even with the best intentions, you can't control how your message lands. Just because it's factual, doesn't mean it makes people feel the way you want them to. And when bad feelings have the power to upend your endgame, you can't really afford to rely on assumptions.

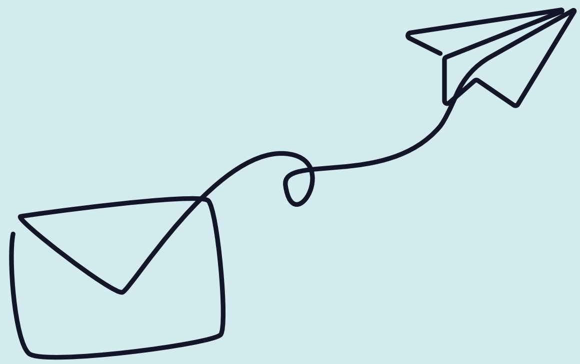
It took a couple of reworks to get 100 per cent positive results to our buyout comms, as well as the desired member outcomes to each individual letter. They were then checked by our legal partner, so we could be sure they meet schemes' disclosure requirements too.

The result? A buyout announcement that can't be misinterpreted. Surplus, AVC and transfer messages that tick every regulatory box. And a suite of comms designed to make your buyout a breeze.

Written by Quietroom lead consultant, Julia Fox

In association with QUIETROOM

All the buyout comms you need, ready to go



Thinking about buyout? We've used our expertise in the field to create pre-written communications that will take your members on the journey with you – from the first announcement through to wind-up.

Focus your time, effort and budget elsewhere – our suite of model buyout communications has been:

- Written by our expert team
- Tested with real members
- Reviewed by our legal partner

Communications with proven outcomes, that meet your regulatory requirements – for a fixed and affordable fee.

These letters come as pre-written Word documents, so all you need to do is enter your scheme details, get sign-off internally, and send them out to members.

We're here for anything else you might need along the way – from consultancy time with a Quietroom expert, to bespoke edits for your scheme, or just a final review before you send.

Are smaller DC pensions facing a cost of governance crisis?

Dale Critchley explores the challenges for trustees managing the money of savers in DC schemes

The financial futures of over 23 million private sector workers rely on the trustees of defined contribution (DC) pension schemes according to figures from The Pension Regulator[1]. They look after over £113.5 billion set aside for later life and invest the contributions of over 10.6 million people each month.

While most members are looked after by the trustee boards of larger schemes there are over 27,700 DC pension schemes according to The Pension Regulator data. Only 1,370 boards of trustees look after more than 12 members, and the boards of 36 schemes (master trusts) look after £78.8 billion of savings for over 20.6 million members.

There's a huge responsibility on trustees, not just within the boards of large master trusts, but within all occupational pension schemes, to manage their scheme in a way which gives their members the best chance of achieving their goals.

The biggest cost within large pension schemes is administration, but in smaller schemes the cost of good governance can easily outstrip that, and the cost of governance can only be expected to rise. Current levels of inflation are likely to be reflected in the cost of professional services, and in the cost of trustee time next year. Alongside this, the scope of the work that needs to be done by trustees continues to increase, as the expectations of government and members grow.

Expectations of government

The increased regulatory workload of trustees is reflected in the growth in the size of the Chair's Statement. What began life as window into the workings of the trustee board has become an increasingly difficult read.

Disclosure of costs and charges has been followed by disclosure of net fund performance. Policies and progress in managing environmental, social and governance risks are supplemented by a separate report aligned to the tax force for climate related change disclosures (for large scheme's currently, but all schemes are included on Treasury's roadmap).

Soon we will see additional disclosure of the asset mix within default arrangements, with a requirement to explain the trustees' rationale in the statement of investment principles. The aim is to nudge trustees to consider wider asset classes including infrastructure, private equity and private debt, a potential win/win of higher returns for members and more investment in UK economic growth.

Within the next two years we expect to see further change impacting on governance costs. A review of the Chair's Statement itself, to perhaps carve out compliance related reporting. The results of the discussion paper on helping members make decumulation decisions may result in a need to offer more structured support on investments and member communications. We will

see the final version of The Pension Regulator's Code of Practice, which may well require more documentation of governance processes and audits of effectiveness. Finally, we will see the requirements for a revised value for members assessment.

All of these will need to be funded. There will be one off and ongoing legal costs to ensure compliance, as well as professional advice to potentially build revised investment solutions and ensure the trustees are delivering effective communications, as well as operating an effective system of governance.

Expectations of members

There was a time when members simply expected their DC pension to deliver a pot of money when they stopped work, which they could convert into an income outside of the scheme, but expectations are changing, and the current cost-of-living challenges, alongside pension freedoms has perhaps accelerated the change.

Pension savings represent the largest component of wealth for a large proportion of the UK population[2]. As expenditure takes up a greater proportion of net income each month the UK savings index is expected to fall to zero next year[3] and some pension scheme members will be looking to rely on savings or debt to make ends meet. For a proportion of those over 55, their pension fund represents a savings buffer they might need to rely on before they retire.

HMRC statistics[4] show a 23 per cent increase in the number of taxable withdrawals in the second quarter of 2022 compared to the same period in 2021. The number of individuals making withdrawals increased by nearly 100,000 to 508,000. What this doesn't show is the number of members accessing tax free cash only, a number which is likely to rise as cost-of-living headwinds strengthen.

Many occupational pension schemes are ill equipped to meet member expectations around retirement flexibility. Clunky paper-based administration, and rules that don't allow non statutory payments or transfers are more suited to cliff edge retirement than the phased approach to retirement favoured by many. Schemes can be modernised, but this will come at additional cost.

Most single employer trust-based schemes don't allow members to designate to drawdown within the scheme. This can result in a need to transfer to access tax free cash or provide an unintended nudge to cash in the whole pot, potentially reducing a member's annual allowance and their ability to rebuild their savings. Those who are still saving in the scheme might be forced to carry out a convoluted in-out hokey cokey to arrange a transfer while maintaining their contributions, in schemes with rules designed to stop them doing just that.

Trustees should also recognise that they may well have financially vulnerable members, looking to make decisions that they didn't plan for. The need for advice has never been greater.

Changing the scheme rules, administration, and governance to allow drawdown would be a huge step forward for members, enabling them to benefit from the economy and oversight of their workplace scheme, but it's beyond the means of many trustee boards. Due diligence on a trusted adviser or partner drawdown provider should be a more achievable aim, however.

How can trustees avoid a cost of governance crisis?

When we're looking at spiralling household budgets our first inclination is to cut back, to do less, to save money, but that shouldn't be an option for trustees. If, as individuals, we choose to cut back on our heating it's we who feel the chill. If trustees choose to cut back on their governance, and on keeping their scheme up to date, it's their members who are left out in the cold.

The DWP made it clear that schemes that don't offer good value compared to alternatives should wind up and seek a transfer to a scheme that offers better value. Members shouldn't suffer poorer outcomes due to a lack of funding for the scheme's upkeep.

The value for members assessment was meant to address the issue of small schemes who lack the financial backing to deliver good outcomes but there's little evidence that small schemes have taken decisive action, and there may be larger schemes that are equally unable to cope with upcoming cost of governance challenges.

Automatic enrolment has amplified the role that DC trustee boards play in delivering the later-life income of UK workers and they need to be supported to deliver the very best outcomes. It's the trustees who carry much of the liability for poor outcomes, and who deserve to be supported. If that's not happening, they should think about their own position, as well as that of their members, and look at the options to consolidate into schemes that have the resources deliver the modern DC pensions that people need.

Written by Aviva policy manager for workplace benefits, Dale Critchley

[1] https://www.thepensionsregulator.gov.uk/en/document-library/research-and-analysis/dc-trust-scheme-return-data-2021-2022

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Company Profiles

SECOR Asset Management

SECOR is a boutique global investment advisory firm with offices in London and New York. Our clients include pension funds, insurance companies, endowments, and family offices from across the globe. Our team has decades of experience as asset owners and portfolio managers excelling at helping clients manage portfolio allocation and risk through the implementation of bespoke and sophisticated investment solutions.

Led by individuals with decades of 'hands on' experience at one of the largest and most sophisticated long-term investors in the world with portfolio managers from some of the most prominent investment firms, we are able to offer clients access to sophisticated investment strategies and cutting-edge capabilities – all in one nimble, client-centric boutique.

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Standard Life

Standard Life is a brand that has been trusted to look after people's life savings and retirement needs for nearly 200 years.

Today, we serve millions of customers, who come to us directly, through advisers and through their employer pension scheme, and we're proud of the consistent high-level of customer service we provide.

Overall, people are living longer and we can support them at every step in their financial future - whether they're looking to maximise their long-term savings, explore options to have an income in retirement, or better understand financial wellness, we're here to help.

We know we can't achieve this without doing our part to build a strong and sustainable future. It's why we are integrating sustainability into everything we do; from incorporating responsible investing into our solutions, to fostering an inclusive savings culture and improving financial wellbeing for all.

We're part of Phoenix Group, the UK's largest long-term savings and retirement business. We both share an aligned ambition to help every customer enjoy a life full of possibilities.

Standard Life
Part of Phoenix Group

Company Profiles

Lombard Odier Investment Managers

At Lombard Odier Investment Managers, we are rethinkers with one goal in mind. To provide our clients with outstanding investment solutions that meet their needs for the long term and evolve to thrive in the challenging world in which we all live.

A major sustainability transition is currently underway: it will radically alter the global economy, how companies do business and how individuals consume. It is fuelled by unstoppable forces including government policy, technological innovation, consumer behaviour and market influences. We see it accelerating to deliver change on the scale of the industrial revolution at the speed of the digital revolution.

Sustainability is today one of the most important drivers of risk and return. This core investment conviction at Lombard Odier Investment Managers fundamentally shapes our ethos, our investment approach and our solutions. Our team of sustainability experts combine sophisticated data sources, academic rigour and technical innovation to create leading-edge, science-based and forward-looking tools to adapt portfolios to this new economic landscape and to create novel strategies centred on nature-positive and climate-aligned goals.

These dedicated sustainable investment strategies are aligned to our core belief – that to respect and preserve the planet's resources and ecosystems, we must move the economy away from a 'take-make-waste model' that takes more than is sustainable, makes more than we need, and wastes most of what we produce. We must transition instead towards a regenerative, circular bioeconomy that combines nature-centric value creation as well as better economics. This new model preserves nature through resource efficiency and outcome-oriented business models, while closing the loop towards zero-waste. We call it the CLIC® economy because it is circular, lean, inclusive and clean.

With more than 180 investment professionals, we are a global business with a network of 14 offices across Europe, Asia and North America and have assets under management of 67 billion CHF (as at 31 March 2022).

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INVESTMENT MANAGERS

Aon

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.

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AON

Company Profiles

Schroders Solutions

Schroders Solutions is a £200 billion global capability with employees in the UK, US, Singapore, and Germany. Our dedicated solutions experts provide investment and advisory services to public and corporate pension schemes, official institutions, insurance companies, individual investors, intermediaries and wealth providers worldwide.

Solving investment problems is integral to what we do. We draw on our knowledge and experience as a global provider to build bespoke investment solutions and strategies. We partner with our clients to understand their investment challenges and construct investment portfolios that deliver their desired financial outcomes. Our consultative approach draws on both Schroders' investment skills and those of the wider investment industry.

Schroders Solutions offers fiduciary management, outsourced CIO, liability, duration and cashflow-driven investing, as well as derivatives-based growth strategies. Our solutions are accessible to clients of all sizes through a flexible approach to implementation, sensitive to their needs and objectives.

Source: Schroders as of 30 September 2022.

Schroders

WEALTH at work

WEALTH at work is a leading financial wellbeing and retirement specialist – helping those in the workplace to improve their financial future.

Established in 2005, we work with hundreds of organisations across both the private and public sector by offering financial education, guidance and regulated financial advice.

Our financial education and guidance services are delivered on a bespoke basis and can be specifically designed to help the entire workforce make informed decisions about their finances.

For example; financial education services cover everything from debt and money management through to optimising employer sponsored benefits and retirement. This can be delivered face-to-face or online and utilises digital nudge technology to encourage employee engagement and participation. A telephone helpline is also provided following this.

Support is also provided through the creation of digital content such as webcasts, animations and interactive tools including the Financial Healthcheck.

All our interactions are measured and can be benchmarked against the industry standard to fully understand the impact. This is of particular importance when meeting financial wellbeing objectives.

Financial guidance services provide one-to-one support on a range of financial subjects which can be accessed face-to-face, via telephone or a virtual call.

As well as this, we provide regulated financial advice supporting those who need specific recommendations regarding their savings and investments, including those who need to make important decisions about their retirement income options. This service also supports those in retirement who may need to adapt their retirement planning in line with their changing needs.

In addition, we also have broad experience in a number of specific projects where we support employees in financial decision making, including; defined benefit pension closures; the introduction of pension changes such as the implementation of a new scheme, share scheme programmes and offering financial helplines to EAP providers. Our services also cover specialist topics including; lifetime allowance, annual allowance and help with redundancy plans.

WEALTH at work
KNOWLEDGE | EXPERIENCE | OPPORTUNITY

Company Profiles

Quietroom

Quietroom is an insight-led communications consultancy that exists to make pensions, investment and insurance more accessible to the people that need them.

There are over 30 million workers in the UK and over 12 million pensioners. Some are confident and capable when it comes to managing money. Most aren't. They don't think of themselves as investors. They don't see themselves as having assets or wealth. They don't feel they have any influence in the boardroom or in the stock market. They just want to live decent lives - and they're looking to us for help.

We work with their employers, their pension schemes and their financial providers, along with every part of the ecosystem that supports them. We help those organisations listen to their audiences and consider their needs, motivations and priorities when they're designing services for them.

We help them create content, journeys and experiences that are:

- human-centred and user-driven
- founded on evidence and smart thinking
- easier to understand, engage with and act on
- brought to life in the channels their audiences use.

By doing that, we play our part in making the whole financial system work better for the people it was set up to serve.

QUIETROOM

Aviva

Aviva Master Trust has been chosen to provide pension saving for over 430,000 employees, working in over 400 companies across the UK. The scheme holds over £7.2 billion of pension saving trusted to it by scheme members.

Aviva Master Trust brings together the skills, knowledge and expertise of the trustee board with Aviva's industry-leading product design, digital technology, and investment capability. These combine with the aim of delivering the best possible retirement outcomes for members.

Key areas of focus are:

Sustainable investment returns – a key focus of the trustee investment committee, to ensure effective management of investment risks, including ESG risks, to deliver sustained investment performance.

Member engagement – the trustees take advantage of Aviva's compelling digital proposition to promote member engagement. Supported by online access and dedicated apps, members can log in via thumb print or facial recognition, making it incredibly easy to view, model and manage their pension.

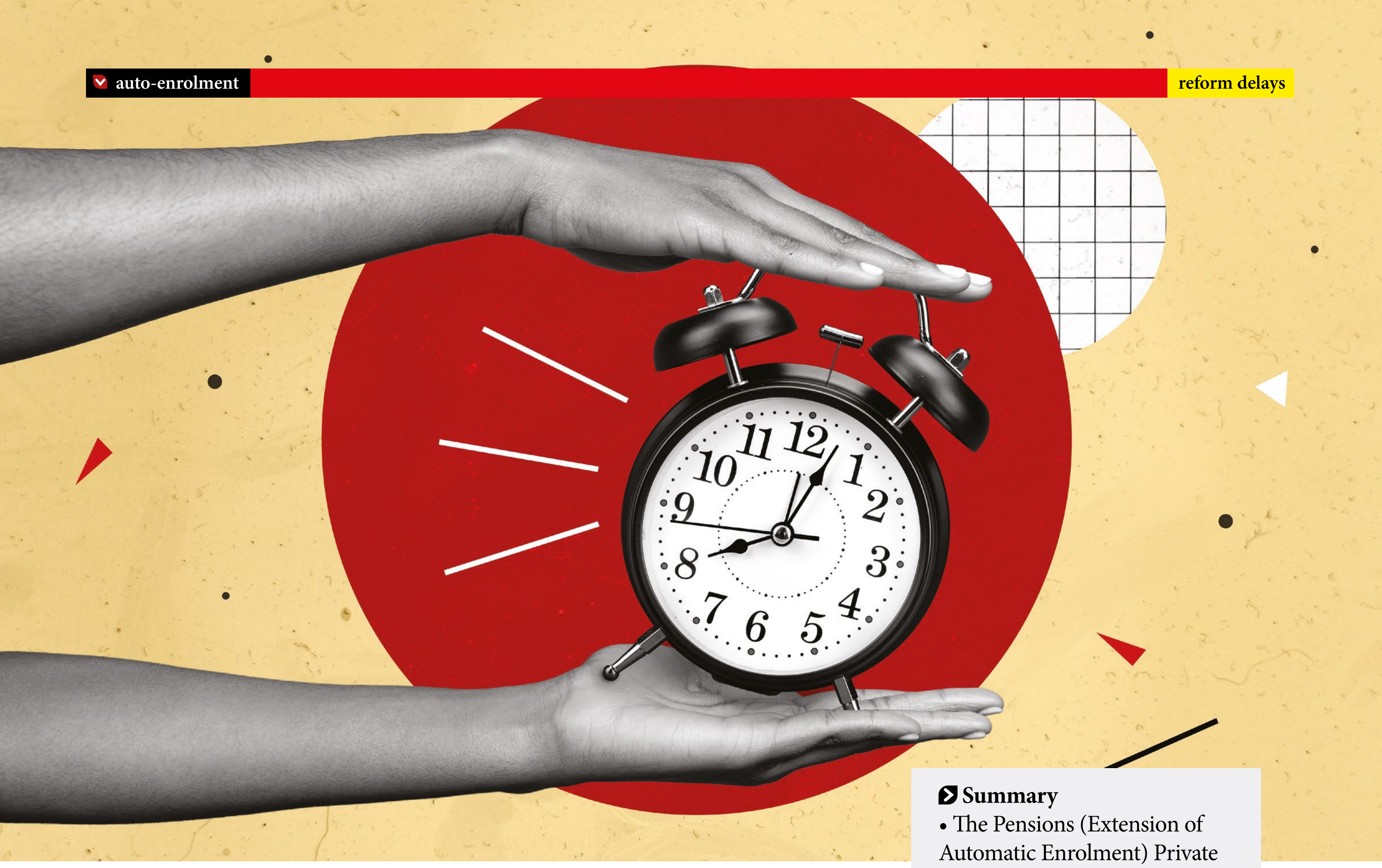
This is supplemented by regular proactive communication delivered at key decision points, and financial education within the workplace, delivered digitally as well as face to face.

Retirement solutions – the scheme offers a full range of pension freedoms, with communications designed to promote good decision making and preserve the value of members' savings. The trustees are currently engaged with Aviva in their development of an innovative Guided Retirement solution.

Ease of transition – Aviva and the trustees recognise that transferring a pension scheme can seem daunting, but dedicated implementation managers, relationship managers, legal and transition management experts help things run smoothly and keep costs down.

Value for members – the above, along with a focus on charges and service levels, combine to deliver value for members, and the ultimate focus for both the trustees and Aviva, which is the very best retirement outcomes.

AVIVA



Time's up

With work on auto-enrolment (AE) reforms again delayed, Sophie Smith considers whether AE reforms could be on the horizon for the year ahead, or whether this could be another failed New Year's resolution

Summary
• The Pensions (Extension of Automatic Enrolment) Private Members Bill was recently delayed until March 2023, and further delays seem likely given the current economic and political environment.
• Although the cost-of-living crisis has exacerbated the need for reform, it has also made the potntial impact of such reforms on members harder to justify.
• AE reforms are not enough in isolation and more holistic changes will likely be needed, particularly for under-pensioned savers.

With the start of a new year, the events of the 2010s are becoming increasingly distant. It's been six years since Donald Trump's inauguration, six years since Prince Harry proposed to his girlfriend Meghan Markle, and six years since the 2017 auto-enrolment (AE) reforms were published.

But while Trump has been replaced with President Joe Biden, and the Sussex's have wed, had two children and even launched a hit Netflix documentary, the AE reforms have seen much less progress.

As Cushon director of policy and research, Steve Watson, points out, whilst AE is widely praised as a resounding success, there is appetite for additional reform across the savings landscape.

Indeed, industry experts have increasingly called for the government to introduce the 2017 AE review recommendations, with the Work and Pensions Committee also urging the government to introduce legislation for the reforms "no later than the beginning of the next session of parliament".

High hopes

Although many had placed hopes on the Pensions (Extension of AE) Private Members Bill, the government recently confirmed that the second reading has been delayed until 17 March 2023.

Pensions and Lifetime Savings Association (PLSA) head of DC, master trusts and lifetime savings, Alyshia Harrington-Clark, highlights this delay as a disappointment, stressing that "we're not going to get the reform we need as quickly as needed, even where there's broad consensus on what is needed".

Barnett Waddingham partner, Martin Willis, also warns that this delay is likely to negatively impact those who need support in retirement the most – those on lower salaries, who start work earlier in life and those who work across multiple simultaneous employments.

"It is also likely that the delay will serve to preserve the gender pensions gap," he adds, warning that "these changes are long overdue".

Adding to this, Pensions Administration Standards Association (Pasa) director, Paul Sturgess, says that although the delays are understandable at a practical level, they do not drive comfort, especially when there has been so much change in the government.

There is still some optimism, however, as Watson says that, while frustrating, the delay is likely to be more to do with the economic climate rather than a change of heart in government, pointing out that the bill was also part of the last Conservative manifesto.

However, Harrington-Clark notes that despite a supportive DWP, parliamentary time remains key constraint, and one that lies out of the control of the pensions industry.

"It is always just about space and time," she stresses, warning that "the longer you leave it, the worse it gets", with the repeated delays becoming "very, very difficult to justify".

A rocky landscape

And further delays seem likely, as Pensions Management Institute director of policy and external affairs, Tim Middleton, points out: "Since summer 2022, we have seen Guy Opperman's resignation, Opperman's reappointment, the brief era of Alex Burghart and the advent of Laura Trott. Although it appears that Trott is enthusiastic about AE reforms, it is inevitable that a period of disruption and instability will result in delays to the implementation of policy."

Echoing this, Sturgess says that, given all the macro uncertainties and government changes, while it is still technically possible for the bill to be laid before the end of parliament, it is perhaps not likely, warning that a general election could at the very least slow it down.

Pensions Policy Institute (PPI) senior policy researcher, Lauren Wilkinson, also suggests that it delays are possible if other areas take priority or if there is governmental changes.

This seems increasingly likely, as Middleton warns that the current cost-of-living crisis, the war in Ukraine and the political turmoil that has followed since the resignation of Boris Johnson have completely refocused the government's priorities over the remainder of this parliamentary term.

"Over the short term, the public is more likely to appreciate support with personal debt and the cost of domestic fuel. Realistically, reforms to AE are unlikely to be made before the next general election," he states.

A missed opportunity?

And the government may have already missed its chance, as People's Partnership, provider of The People's Pension, director of policy, Phil Brown, argues that the bigger issue is the cost-of-living crisis, hard on the heels of Covid, stating: "It's sensible to make plans for the future of AE right now but no one can argue for immediate increases in pension saving during the current cost of living crisis."

Willis agrees, acknowledging that the cost-of-living crisis makes increasing contributions to pensions challenging, both for employees and employers.

"However," he clarifies, "this doesn't mean that an element of the system, that disadvantages those who need support, shouldn't be addressed. Consideration should be given to a short-term relaxation on the need for employee contributions to be paid in order to receive minimum employer contributions."

Wilkinson also says that, for low earners in under-pensioned groups, in particular, it should be recognised that it may not currently be appropriate to default them into saving and divert income away from current needs.

"Although it also needs to be recognised that inequalities experienced by low earners in under-pensioned groups are likely to be exacerbated by the current economic situation so the gap could increase further," she clarifies.

Echoing this, Now Pensions head of PR and campaigns, Samantha Gould, warns that while the current economic circumstances mean it is challenging for the government to implement potential remedies, doing nothing is not an option.

"Action is needed now to reduce the pensions gap and allow everyone to enjoy the comfortable retirement they deserve," Gould says, suggesting that the removal of the £10,000 earnings threshold would have the biggest and most immediate impact to bring more people into workplace pension saving.

Adding to this, Harrington-Clark says that while there are some arguments to suggest that the delay to AE reform could have had a protective effect on incomes, it is unlikely to outweigh the potential loss in living standard at retirement.

Instead of delaying change altogether, Sturgess suggests that "perhaps the key

is not to deprioritise the discussion but to give extended advance notification of changes so people can prepare, lest we forget that people who enter retirement with inadequate pensions are the very same people that a cost-of-living crisis will punish most."

Adding to the list

And broader changes could still be needed, as Middleton points out that there are also ongoing concerns around the "clear gender imbalance", the rise of the gig economy and issues around self-employed saving, as well as considerations around the dashboards.

Sturgess agrees that although AE reform is a good start, broader change is probably needed, noting that the risk transfer to members that has occurred over the past 25 years has been unchecked and the options available to members give them more opportunities, but also greater risk.

Particular concerns have been raised around supporting under-pensioned groups. Wilkinson explains that these savers are likely to need be supported to achieve adequate retirement outcomes, after recent modelling suggested that for those on median earnings, contribution rates may need to be around 20 per cent in order to reach target replacement rates, or more depending on working patterns.

"Encouraging savers to increase their contribution rates, either through communications or more direct action, such as introducing opt-up or opt-down mechanisms, could improve outcomes for those who are able to contribute more," Wilkinson continues.

"However, for people in under-pensioned groups who are more likely to be unemployed or on low earnings, greater support may be needed in terms of means-tested benefits to ensure adequate retirement outcomes."

The industry may also need to look further than pensions, as Brown suggests that "there is no pure pension solution for Generation X", explaining that while the reform of AE would likely have a positive impact for workers under 40, it would have less of an impact for older workers.

Harrington-Clark echoes this, suggesting that the 2017 reforms should form part of a wider suite of components.

"The ideal circumstance would need to be a full review, including the 2017 AE reform, but that's the minimum," she says, warning that a limb-by-limb approach could result in unintended consequences.

"Over the short term, the public is more likely to appreciate support with personal debt and the cost of domestic fuel. Realistically, reforms to AE are unlikely to be made before the next general election"

She explains that looking at the earnings trigger in isolation, for instance, could provide evidence that is both too high and too low, warning that a suboptimal choice could be made if not considered holistically.

"I don't think it's implausible to do it that way and it may be pragmatic," Harrington-Clark acknowledged, emphasising however that "there are some mechanisms here that are pretty complex and have very, very mixed evidence associated with them, so the government would need to be careful about doing it in that way".

In particular, Harrington-Clark draws attention to the PLSA's *Five Steps to Better Pensions* report, which recommended reforming the state pension to ensure everyone achieves the minimum retirement living standard, alongside broader changes to AE reform, and additional policy interventions for under-pensioned groups, including women, gig economy workers, self-employed people.

Watson agrees, stressing that there is a growing understanding that reform can't be just about pensions, stating: "Pensions by themselves do not meet the savings needs of many people – we need a new approach to workplace savings more generally. We need to take a longer-term view when it comes to financial resilience, not just focusing on it in retirement but using workplace savings products to build a financial buffer throughout our working lives."

There are also steps that the industry can take to support members in the meantime, Willis warns that "without support around the complex choices our pensions legislation presents to people, even large pots may fail to meet member needs because of poor decision making".

This is echoed by Harrington-Clark, who emphasises the importance of engagement campaigns, such as the recent Pension Attention campaign.

However, she clarifies that these efforts "do not replace strategic policy reform", emphasising the need for the industry to prepare arguments for greater change, and reach a consensus.

"The key thing that we can do as an industry is rally around those things that we all already support, and also have detailed, hearts-on-the-table type conversations about what things we do and don't agree on, or that we just don't have the evidence for yet and gather it so," she stresses.

Adding to this, Gould highlights the slow progress over the past decade as demonstration of the importance of making plans today to improve inequalities over the long-term, even if policy changes cannot be implemented until the economy has stabilised.

"It takes a long time for structural changes to the pensions framework to affect the ability of people to build their pensions pot," she says. "Yet it is vital that thought is given to potential policy solutions, even in these challenging times."

Written by Sophie Smith

2023 for the APPT

As the new year starts, Tom Dunstan speaks to Association of Professional Pension Trustees (APPT) chair, Harus Rai, about the association's goals for 2023, the challenges they envision facing, the reforms they would like to see occur, and more

What are your goals for the next year?
The association has a number of external and internal goals for the year ahead. On the external side, the priority of our members is to ensure scheme members' benefits are secure and that they are paid as they fall due.

In public policy terms as an association that means making representations to the Department for Work and Pensions (DWP), The Pensions Regulator (TPR) and other relevant bodies of the need to carry trustees with them in pursuing further reforms aimed at better securing and encouraging pension saving. The outcome of the new Defined Benefit (DB) Funding Code is one area where it is important reforms continue to allow scheme specific funding and investment to thrive in a flexible environment. Another key area is the outcome of the Single Code and the gradual implementation of pension dashboards.

What reforms would you like to see in 2023?
The association is leading a study alongside the DWP, TPR, the Pensions Management Institute (PMI) and the Association of Member Nominated Trustees (AMNT) of how the accreditation of professional trustees, which began in 2020, has provided benefits to sponsors, members, advisers and our sector. We hope the outcome of that study will give further impetus to changes whereby more schemes appoint accredited professional trustees to support their governance arrangements.

Are there any challenges that you foresee in the future?
A major challenge in an era where both government and regulators are pushing ahead with reforms is the danger that schemes' governance and administration within available resources is compromised by an overload of new and changed requirements. We foresee that the expectations falling particularly on volunteer, lay trustees may place even further difficulties on retaining and recruiting members to this important role. We must also be concerned that the DWP and TPR will feel further regulatory requirements are placed upon all trustees to address perceived governance problems brought on by the liability-driven investment (LDI) crisis.

Are there any issues from 2022 that you believe will need to be addressed in 2023?
Those legislative and regulatory reforms unfinished in 2022 are the most obvious ones to be addressed in 2023. The emerging signs of more members leaving pension arrangements because of the cost-of-living crisis might also prompt the need for the DWP to relax auto-enrolment (AE) rules to allow members greater flexibility to reduce their contributions in difficult times. We also feel that the DWP will need to map out its next steps in AE and collective defined contribution (CDC) reforms so the impetus to widen pension coverage is kept going for the longer term.

Is there anything in particular that you wish to achieve in the next year?
The successful adoption, through the leading role played by our members, of reforms arising from the Single Code, DB Funding Code and pensions dashboards initiative, whilst also making incremental improvements in schemes' environmental, social, and governance (ESG) and diversity priorities.

Is there anything else you would like to mention about your plans for the coming year?
Internally we will be looking to represent an increasing number of accredited professional trustees, building on our 370 members, with us investing greater resource in furthering members' professional development across all areas of legislative and regulatory change, including more training guidelines.

We will also be developing the role of our Small Firms Forum that already helps over 50 small firms and sole practitioners to meet the challenges encountered by our sector and their clients.

Written by Tom Dunstan

Summary

- The government released its consultation response on Solvency II reform in November 2022.
- Insurers will be able to invest in a wider range of assets to support UK growth.
- Impact on buy-in and buyout preparation is likely to be minimal.

Good for pensions, good for Britain?

Will new Solvency II proposals help insurers cope with the buyout big-bang of the next few years and invest in UK growth? Maggie Williams explores

HM Treasury's 17 November 2022 consultation response on UK-specific reforms to Solvency II was positive news for insurers and pension schemes, even if it didn't pack the same media punch as other aspects of the Autumn Statement, delivered the same day.

Since its launch in April 2022 by then-Chancellor Rishi Sunak, the review of Solvency II has been the poster child for post-Brexit UK-specific rule-making. The government says that it aims to create a "vibrant, innovative and internationally competitive" insurance sector, enabling insurers to access a wider range of assets and to help ignite then-Prime Minister Boris Johnson's promised 'investment big-bang'.

Since then, debate on rule changes has been the subject of frustration from Johnson, caution from the Prudential Regulation Authority (PRA), nervousness from insurers – and confusion for pension schemes waiting to see how the regulations might affect future buy-in and buyout transactions.

The November consultation response will have provided more certainty for insurers and trustees alike, although it could still be some time before the new regulations come into force. The government hasn't yet set out a timetable for implementation, and the proposed regime changes will require primary regulation. All in all, it could be 2024 before the new rules are in place.

Perhaps the good news is that, despite the disagreements and frustrations while the regulations have taken shape, the impact on buy-in and buyout is likely to be minimal *[see our boxout for more detail on two key aspects of the proposals and how they will affect pension schemes]*.

"Trustees will no doubt have been keeping a close eye on developments, but we do not expect the proposed reforms to impact the plans for schemes preparing for buyout," says Standard Life senior business development manager, Kieran Mistry.

Hymans Robertson partner and risk transfer specialist, Michael Abramson, is also upbeat about the new proposals: "These changes will help buyout insurers to invest more broadly and with less frictional cost. They will cut some of the existing Solvency II red tape, and reduce some of the capital requirements – in particular for longevity risk."

The details of the government's consultation response will also help to provide more certainty about deal pricing and allay fears that the reforms would undermine security for policyholders. On the first of these, Abramson says there could even be a little good news: "We expect the reforms to bring a marginal improvement to pricing in some cases, though this is likely to be lost in the noise of market movements."

Security for policyholders will be monitored through extra powers given to the PRA, which regulates the insurance sector, including additional stress tests.

LCP partner, Charlie Finch concludes: "There are some aspects of the proposals that are materially helpful, both around how deals are structured and also greater flexibility. This will help insurers to cope with the significant rise in volumes of buyout deals that we expect to see over the next two to three years."

Being able to support higher volumes of deals will be particularly important over the next five to 10 years. Barnett Waddingham's End Gauge index for November showed that the average time for a FTSE 350 scheme to reach its buyout funding level is now just six years. The gilt yield volatility that we saw in the second half of 2022 may also have prompted even more schemes to see buyout as a viable destination.

How will the new rules affect buyout insurers?

Given the long road ahead until the reforms are finalised and become law, schemes that are planning to transact a buyout in the short or medium term will see little or no impact on their plans.

For those that are at an earlier stage in the de-risking process, Mistry expects the flexibility in asset allocation proposed by the new rules *[see boxout]* to help insurers cope with intense periods of activity in the future. "Enabling insurers to source from a wider pool of assets should provide some additional comfort in the market's ability to service the expected rise in demand," he says.

That additional flexibility may also mean that, in the future, schemes could transfer illiquid assets that qualify for matching adjustment to insurers as part of a premium payment. This would reduce one of the more complex and time-consuming steps in de-risking preparation.

The new response also includes a more nuanced approach to reserving rules related to the risk profile of an asset. "Insurer reserving requirements will change more smoothly between assets of different credit ratings, which will add greater precision to the current rules," explains Finch.

But will more flexible asset allocation options drive the hoped-for 'investment big-bang'? Royal London director of policy and external affairs, Jamie Jenkins, believes so. He says the proposed rules will "allow the industry's capital to be used more effectively", helping insurers to "invest in the infrastructure the UK needs to drive future growth and deliver on the country's net-zero ambitions". Mistry says new approaches could include support for "house building, green energy and local communities across the country".

Mistry adds that this could help trustees align their scheme's ESG principles with buyout goals. "Schemes can continue to have confidence that insurers will invest for the good of wider society," he adds.

What do the reforms mean for buy-in and buyout?

There are two key areas where the proposed Solvency II reforms will affect pensions buy-ins and buyouts.

1. Asset flexibility

What's the change? The new rules would broaden the range of assets that insurers can hold within matching adjustment portfolios. Matching adjustment enables insurers to recognise a part of the excess returns from eligible assets above the risk-free benchmark in their reserving calculations. This is a significant benefit for them – in 2020, insurers' balance sheets were boosted by £81 billion through matching adjustments.

To qualify for matching adjustment under the proposed new regulations, assets will need to provide 'highly predictable' cashflows. This is an important change of wording from the 'fixed' cashflows required by the current Solvency II legislation (which effectively restricts matching adjustments to bond-like assets), and opens up a wider potential range of investments.

What does it mean for buy-in and buyout? "This change should widen the asset pool available to insurers and help them to price competitively for a larger number of schemes," says LCP partner, Charlie Finch. Matching adjustments enable insurers to price annuities competitively, offering a benefit to pension schemes as well as the insurers.

2. Risk margin reduction

What's the change? The risk margin for long-term life insurance business will be reduced by 65 per cent.

What does it mean for buy-in and buyout? The risk margin reflects the cost of transferring liabilities that the insurer cannot hedge, to a third party. For buyouts, this mostly applies to longevity risk. Insurers add the risk margin to their best estimate of the liabilities.

The new proposed approach would reduce the capital required to cover the risk margin by 65 per cent. While that sounds like a significant drop, in practice, "it will result in a relatively limited reduction in capital requirements for buy-ins and buyouts for most insurers, depending on their approach to managing and reinsuring longevity risk. We still expect this to be an important part of insurers' risk management", says Finch.

> **"Schemes should not put their de-risking plans on hold as a result of these reforms"**

What impact will it have on schemes?

"Schemes should not put their de-risking plans on hold as a result of these reforms," says Abramson. "We do not expect the changes to fundamentally shift pricing or the security of the insurance regime."

Mistry says: "Speaking to consultancies and trustees, it appears there's no slowdown in sight, with many more schemes preparing in earnest to approach the market early in 2023." Abramson adds that the same principles of good buyout planning – such as data cleansing and preparing benefits specification – will remain as important as ever. "Now more than ever, there is a need to be well prepared before approaching insurers to maximise market engagement," he says.

While the government works out the finer details and passes the legislation needed to bring Solvency II reforms into force, for schemes aiming to complete buy-ins and buyouts now or in the future, it remains business as usual.

Written by Maggie Williams, a freelance journalist

Cleaning greenwash out of pensions

With an increased focus on ESG in both pensions investment strategies and the activities of underlying businesses in which funds are invested, greenwashing is not just an irritant but a real danger to schemes, members and trustees. David Adams reports on attempts to tackle the problem

Greenwashing is a dirty business. It could undermine efforts to combat climate change while also threatening the financial futures of pension schemes, members and savers. With more pressure from members, savers and regulators for pension pots to be invested in ways that help drive positive outcomes around environmental, social and governance (ESG) factors, these considerations are being integrated into pension scheme investment strategies. But if those strategies turn out to be based in part on exaggerated or false claims about investment funds or underlying assets, that creates financial, reputational, regulatory and possibly legal risks for schemes and trustees.

"Trustees for the most part have defined ESG factors as material and they're looking to manage them through investments," says PwC manager for the ESG pensions advisory team, Alexandra Westley. "If trustees fall victim to greenwashing it can mean risks are not managed as well as they should be."

"It damages trust; and our industry is built around trust," says WTW senior director and head of sustainability solutions, Monique Mathys-Graaff. "The more that *[schemes, funds or businesses]* set targets like net zero but don't deliver, the more we lose that trust."

Policymakers, regulators, businesses and the pensions and investment industries have all responded to the rise of greenwashing in different ways. Those responses are beginning to cohere, but only very slowly.

An evolving space

One problem is that there is some disagreement as to exactly what constitutes greenwashing. It certainly includes deliberate fraud, as when Global Forestry International marketed a fake green pension scheme invested in a Brazilian teak forestry fund. But it might also include cases where a lack of transparency has led to misunderstanding or miscommunication about the underlying assets in which funds are invested.

"It's very difficult to quantify the scale *[of greenwashing in the UK pensions landscape]*, because there hasn't been a common way of measuring the impact and reporting of green issues to a straightforward compliance regime and taxonomy," says Pensions and Lifetime Savings Association (PLSA) deputy director, Joe Dabrowski. "Different companies might assess how green a product is, or how green a company is, using different lenses. *[The underlying companies are not]* subject to consistent regulatory or reporting requirements.

"So if you're investing in multiple portfolios, invested in multiple underlying companies, dragging this information into view is really difficult. You're having to live with uncertainty as to whether a fund or an underlying company is matching up to their stated aims. But it's an evolving space – everybody's trying to improve things."

That includes The Pensions Regulator (TPR), which introduced updated guidance for trustees on managing and reporting on climate-related risks and

Summary

- Greenwashing has the potential to create financial, reputational, regulatory and legal risks for pension savers, schemes and trustees.
- It is difficult to quantify the extent to which greenwash is prevalent in the pensions system because of a lack of consistent, international, interoperable measures for carbon emissions and other environmental impacts. Such a system is developing, but only slowly.
- A focus on stewardship will also help to identify and mitigate greenwash risks.
- At present, trustees would be best-advised to continue to monitor strategies and work with advisers and service providers to identify and manage ESG and greenwash-related risks. Improving member communications will also help.

opportunities in October 2022. Trustees must calculate and report these risks using a portfolio alignment metric linked to the Paris Agreement goals for restricting global warming to no more than 1.5 degrees centigrade above pre-industrial levels. These rules were rolled out in 2021 for authorised master trusts and schemes with net relevant assets of £5 billion or more; since October 2022 they have applied to those with assets of more than £1 billion.

Those regulations are guided by the recommendations of the Taskforce on Climate-related Financial Disclosure (TCFD). But pension schemes and investment managers may also be signatories to, or be working with, the Principles for Responsible Investment (PRI), an independent, international organisation which works to help create and support sustainable markets and businesses; and has coordinated development of actions for integrating ESG issues into investment practice.

Schemes and their service providers may also be signatories of the Financial Reporting Council (FRC) UK Stewardship Code, which sets standards for investors on behalf of UK savers and pensioners to allocate, manage and oversee assets that will create long-term value and "sustainable benefits for the economy, the environment and society".

All these initiatives and tools may help to reduce the extent to which schemes and savers are exposed to greenwash-related risks. But Westley says this plethora of ways in which scheme trustees can seek to combat greenwashing can actually be split into two areas: Strategy and stewardship.

She points out that some trustees are wary of using investment strategies based in large part on exclusions, because of a perceived or real clash with their fiduciary duties. Instead, "a lot of trustees are deciding to focus on engagement".

One way to do this is to use tools such as those developed by fintech Tumelo, which helps scheme members engage with the businesses in which their money is invested. Tumelo CEO, Georgia Stewart, argues that this sort of engagement, aiming to drive change from within a business, can have hugely positive impacts, including a reduction in greenwashing. "I think the modern perception of ESG is more than just what you do or don't invest in," she says.

"If trustees fall victim to greenwashing it can mean risks are not managed as well as they should be"

Regulatory scrutiny

Meanwhile, we are also likely to see more regulatory efforts to reduce greenwashing. In October 2022 the Financial Conduct Authority (FCA) proposed anti-greenwash measures based around how terms such as ESG, green or sustainable can be used to label investment products. It suggests using three categories for labelling, including one for products that should become more sustainable over time. The proposals do not currently cover pension products, but the FCA says it is "considering how we might bring these products into scope".

However ,the current proposals, due to be finalised during 2023, may be helpful to the pensions industry anyway. "I think the FCA proposals … could be quite a leap forward for everyone using these products," says Westley.

"It is exciting to see regulators stepping into this space," says Mathys-Graaff. "It is a positive development that will prevent greenwashing, but it is also an exciting opportunity to ensure that consumers make better informed decisions about how their money is invested."

But she also highlights the need for a more integrated international approach to help reduce the potential risks of greenwashing. "It's a systemic challenge, so interoperability is key," she says. "You can only measure performance if you can trust the interoperability of the data."

Maintaining momentum

While we wait for truly interoperable standards for risk identification and climate disclosures, the best thing trustees can do, Westley suggests, is review the extent to which ESG considerations and metrics are built into their strategies. "Trustees can look at their whole strategy, at funding, at the sponsor and investment, to ask: 'How do we think ESG impacts this and what choices to we want to make?'" she says.

She also thinks communication with scheme members around ESG – and by extension, greenwashing – needs to improve. "We need to make *[reporting]* more understandable for members," she says. "We need to make sure that claims around how trustees are managing ESG risks and opportunities can be demonstrated, to ensure members can also be part of the accountability process."

The optimistic view of where all of this activity will lead is that a proactive approach, among schemes, their advisers, the investment industry and businesses in general will accelerate meaningful progress: reducing the risk of and the risks related to greenwashing, while using pension savings to help reduce carbon emissions and pollution. The alternative scenario, where businesses and consumers become more cynical about ESG credentials, isn't pleasant, at a time where we need to take every step we can to mitigate the effects of climate change.

"The direction of travel is really positive," says Dabrowski. "But it's important that we keep up that momentum."

Written by by Dave Adams, a freelance journalist

Summary

- Fixed income – which includes bonds, gilts and other forms of debt – has long played an important role in pensions investing.
- It's likely that pension funds will be more drawn to investment-grade bonds rather than their high-yield equivalent, as they look for stability from the fixed-income elements of their portfolios.
- Historically, fixed income has provided stability when compared with equities. Recent economic conditions have made this less true – but some argue that the stabilising role will return in a higher-interest rate environment.
- Some argue that this area has not been as attractive as it is now, compared to equities, since the global financial crisis.

Asset class round up: Fixed income

In the first of a regular series providing asset classes overviews, Sandra Haurant explores the latest developments within fixed income

The basics

Fixed income is a broad term that covers investments that pay a fixed amount of income through, for example, dividends or interest payments. Capital invested is locked away for a set amount of time, and an income is paid until maturity, after which the capital is returned. Corporate bonds, government bonds or gilts are among the most common types, and the asset classes can be accessed directly or through fixed income exchange-traded funds (ETFs).

According to Aon partner and co-head of global fixed income manager, research, Paul Whelan: "Fixed income continues to be an ever-evolving, vast universe, which contains many heterogenous sub-asset classes. These sub asset classes range from highly liquid investments to illiquid investments, but serve to fulfil one or more of the following roles in investors allocations; liquidity, diversification, liability hedging, return seeking and capital preservation."

What's in it for pension funds?

Individual pension funds, says Whelan, have seen allocations to or from different areas of fixed income change and develop as their requirements evolve. "Particularly as funding levels have improved, we have seen clients increase their allocation to high quality, liquid credit instruments in both corporate bond and asset-backed securities, seeking modest excess returns whilst maintaining liquidity."

As for those looking for growth, he says: "We have seen pension funds diversify from public equity and diversified growth fund (DGF) allocations in particular, to multi-sector credit and less liquid fixed income strategies, including bank capital relief and direct lending strategies."

Traditionally, fixed income assets were considered to have a stabilising effect on a portfolio – but in recent years this has not always been the case. As DWS head of rates, fixed income EMEA, Oliver Eichmann, says: "When coupons or income are low, bonds are not able to provide stability in an environment of volatile rates and spreads."

However, this is now changing. "As coupons or yield levels have risen by two percentage points in many geographic areas," says Eichmann, "there is finally income in fixed-income portfolios to mitigate market risks or volatility especially from rates and spreads." As a result, he says: "Fixed-income portfolios should, after many years of low income, be in a position again to provide stability in investor portfolios going forward."

What are the challenges?

With such a broad spectrum of assets in the fixed income world, it's clear that specific areas will be facing different challenges. According to Eichmann, some of the biggest include "refinancing existing debt, or meeting funding needs in an environment of substantially higher rates; as well as economic slowdown and high commodity or input prices".

Some segments are more vulnerable than others, he adds, singling out high net debt leverage (with low credit rating and especially high yield), emerging market sovereigns with high commodity exposure, debt issuers with large maturities in 2023, debt issuers from cyclical areas and debt issuers with high energy consumption as those who will be particularly at risk from the current difficult economic environment.

Pensions, then, are likely to lean towards the more stable sectors, says GIB Asset Management head of fixed income, Samantha Lamb: "If the current environment is to continue into 2023, then investors can expect investment grade credit to be favoured over high yield credit." She adds: "Given the high level of economic uncertainty and the higher rate environment resulting from inflationary pressures, we expect high-yield companies to be more exposed to refinancing risks and a weaker economy."

Arguably, few assets have escaped the turmoil of the markets over the past few years. And fixed income has been no exception. "A key characteristic of 2022 was the indiscriminate nature of the sell-off in credit markets," says Ninety One portfolio manager, Darpan Harar.

"Most credit asset classes have cheapened significantly, with spreads well above their 10-year averages. As a general theme, this has been most pronounced in the higher quality sectors of the market, such as investment grade and high-quality structured credit.

"It is very rare that we see corporate bond yields exceeding earnings yields that are available in equity markets, but that is currently the case in some key markets like the US. From a variety of angles, valuations are historically very compelling," Harar adds.

Indeed, the key question, Eichmann suggests, is not so much whether to re-enter or rebuild fixed income allocations, but when and how, with what are now decade-high yield levels across market segments. After all, the ground is still shifting underfoot, making it difficult to navigate reentry. "Central banks are not yet done with the monetary tightening, economies continue to slow and may enter recessionary territory in Q1 2023; while inflation also remains very high and is only expected to slow down to a still relatively high level in many monetary areas," Eichmann says. "Trustees and clients are interested in engaging with us to assess relative attractiveness of fixed income segments, ongoing risk factors and our return outlook for various markets."

What's next for fixed income?

Fixed income assets have long formed a major part of pension portfolios, and this is unlikely to change. But just now, there are some areas that are significantly more inviting than others, says Harar. Firstly, he suggests, like Lamb, that investment grade debt is a compelling segment of the market. Secondly, he says: "We like high-quality structured credit, which has underperformed this year and offers a significant cushion in the event of further credit stresses." What's more, he says, the fact that coupons in this sphere have floating rates means that this area is a lot more attractive – in an environment of high interest rate volatility, it makes sense to attempt to benefit from increases in rates.

"Finally, we like high-carry opportunities," Harar adds. "We believe that these will be the engine for credit returns, as they provide investors with a high and stable income source. That said, we believe it is important to remain dynamic in order to take advantage of current mispricing opportunities and to navigate the increasing dispersion we expect to see across the asset class as the cycle evolves."

Fixed income is also set to become a key part in environmental, social and governance (ESG) strategies, explains Whelan. "As allocations to fixed income have, typically, increased, we've also seen the asset class play a greater role in aligning to and helping achieve pension funds responsible investment and ESG objectives," he says. "We have observed a marked improvement in ESG integration and awareness across fixed income products, as well as a growth in products and solutions seeking to achieve an impact objective without impairing the risk-return characteristics of such strategies."

The focus on these solutions has been varied, but Whelan cites assisting the climate transition required – for example net-zero and Paris-aligned strategies, as well as positive alignment to the UN Sustainable Development Goals, as key areas.

After a tricky time, Harar suggests that a selective approach will allow investors to benefit from a more positive run in this area. "We can expect a much more diverse picture in 2023," he says, "as investors start to discriminate between the winners and losers in a challenging economic climate."

And while the mantra may not quite be 'the only way is up' for fixed income as a whole. there is certainly room for optimism in the right areas, says Lamb: "Despite volatility, in our opinion, credit has not been this attractive compared to equities since the global financial crisis."

"The challenge this year has been that inflation variability has been the issue, leading to interest rate increases, weaker government bonds, and (via consequent expectations for weaker growth) falls in equity prices and higher risk components of global bond markets," says Payden & Rygel's managing director (London), Nigel Jenkins. "Whilst inflation volatility may be a bigger issue on average over the next 10 years than it has been over the past 20, for the most part we think it will once again be economic growth expectations that will be the dominant factor. And in that environment, fixed income assets should again provide stability in a balanced portfolio allocation."

Written by Sandra Haurant, a freelance journalist

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CHAIR

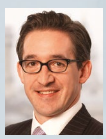
Andy Cheseldine, Client Director, Capital Cranfield
Andy joined Capital Cranfield in 2017. Before joining the firm, Andy acted as an adviser to trustees and employers at Watson Wyatt, Hewitt Bacon & Woodrow and as a partner at LCP. Using his experience of over 30 years in consulting on both DC and DB arrangements and liaising with regulators throughout the pension and financial services industry, he is able to use his wide knowledge and understanding for the practical benefit of trustee boards. He has served on the PLSA DC Council since 2013. Andy is also chair of the Small Pots Co-ordination Group.

PANEL

Sam Burden, Client Director, ZEDRA
Sam is client director at ZEDRA Governance. He has more than 24 years' experience in the pensions industry and has worked with a wide range of DB and DC schemes. Sam has specialised in DC arrangements and has advised companies and trustees on all aspects of DC provision. His clients have included companies in the FTSE 100, multi-nationals, and the not-for-profit sector, with DC pension assets up to £1 billion and with over 50,000 employees. Sam is a former Birmingham City Councillor, a current charity trustee, and even stood for parliament in 2010.

Dominic Byrne, Head of DC Strategy for EMEA, BlackRock
Dominic is head of DC strategy for EMEA. This includes pooled and custom portfolios that span target risk, diversified growth, factors, multi-alternatives, and lifecycle investment processes. Dominic is responsible for business development, investment strategy and product and solution evolution across the region. He serves as the lead client-facing resource for EMEA distribution teams and engages with external stakeholders who drive DC decision making. Dominic has spent over 15 years of his career in product and investment strategy roles.

Sophie Moore, Associate Partner, Aon
Sophie is an associate parter at Aon. She advises DC pension schemes (ranging from £20 million to £2 billion plus) on all aspects of strategy and governance. She enjoys taking a collaborative approach to working with her clients, and brings a wealth of experience in delivering practical solutions, having joined Aon in 2005 and worked in both actuarial and DB investment roles prior to her current DC focus. She is part of Aon's DC Investment Committee, which meets regularly to consider DC issues and agree guidance for the wider business. She also leads Aon's DC relationships with professional trustee firms.



Matthew Swynnerton, Partner, DLA Piper
Matthew is a partner at global law firm DLA Piper and heads the London pensions team. He advises on all aspects of pensions law, including corporate and bulk annuity transactions, reorganisations, benefit redesign and liability management projects, reviewing and updating scheme documentation and advising trustees and employers on their legislative and trust law duties. Matthew drafted key legal sections of the Combatting Pension Scams Code of Practice, which received widespread praise from The Pensions Regulator, The Pensions Ombudsman and the Pensions Minister.

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New considerations

The impact of the recent market volatility, inflation, and cost-of-living challenges, along with the need for innovation, not least with investment strategies and at the retirement stage, are all discussed at our latest DC roundtable

Chair: Let's look at market sentiment and the impact of recent market volatility. What is our feeling on how that has panned out and what problems it has caused people close to retirement? What do you think might happen in the future, both in the stock market and in the pension market?

Burden: I was in a trustee meeting recently and saw the returns for individuals coming up to retirement. Some members close to retiring, within that 10-year de-risking period, who were supposed to be in a low-risk environment, were seeing a 10 per cent fall in their DC account in some instances.

This is obviously a period when risk should be reducing and for most of these individuals that would have been a real shock. The overall de-risking strategy was drawdown-focused, so less of an issue for those remaining invested, but would have a real impact on those taking cash. I've got real reservations around the huge focus we have on drawdown in retirement and this crisis should prompt us to reassess the role of annuities.

Moore: What we've seen from client schemes is members experiencing a drop in fund value, more pronounced for those closer to retirement who typically hold more fixed income or those invested wholly or partly in long-duration bonds in annuity strategies. But then on the flip side the cost of providing benefits has come down. Annuities are now cheaper. And even where members' drawdown pots may have fallen, the *[bond]* yield on their savings should have gone up.

Most schemes have had a handful

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of queries through from members, mainly around the fall in pre-retirement funds. But other than that, we haven't seen a great deal of opt-outs or declines in contributions. So, I think there is an element of inertia working quite well there and maybe that's something we need to celebrate.

It's been the same in our delegated solutions, very little noise from members or opt outs. Anecdotally, there were a few members cutting contributions driven by the cost-of-living crisis. But it was interesting that it wasn't necessarily from the industries you might expect. One client in a really well-paid profession had a member asking to cut contributions, so perhaps driven more by mortgage rates than other factors.

Byrne: From an investment perspective, I think we're being reminded that these flexible drawdown strategies do have a level of volatility and we need to highlight to members what the objectives of these strategies are. I was also thinking about how to compare DC defaults in this environment. We have to compare defaults with similar objectives; it's not fair to compare a pre-retirement experience with a cash default experience, they're designed to do completely different things.

One is designed to cash out, the other one is to provide a link into some sort of annuity income, so it wouldn't be fair to compare a flexible drawdown strategy that's designed to provide income through retirement, with a strategy that's designed to provide cash.

The big impact of the recent market volatility will be on the future. Defaults going forward will have to navigate greater levels of GDP volatility, and they're also going to have to manage things like the transition to a low-carbon economy.

Swynnerton: We've tended to see much more generic information and health warnings: Pointing members in the right direction of where they can get appropriate guidance, emphasising the importance of taking, and explaining where members can get, regulated financial advice, sending them to MoneyHelper before making decisions about pensions savings, for example. I think trustees and employers have got comfortable with knowing where the balance lies in terms of not straying too far into financial advice territory but being proactive enough to ensure members aren't disadvantaged and can get the advice they need.

Burden: In the old days of savers buying an annuity, you wouldn't have been so fussed about the recent market volatility, because your account value goes down but that's okay because annuity rates have improved, which offsets it. But in our new drawdown world, where most people are going to be managing their money in those first few years of retirement, people don't understand the risks that they're exposed to.

If you look at some of the reports that have come out over the past few years, there's evidence that individuals don't know what is a safe amount to be taking out of their drawdown accounts. So, you've got this compounding impact of drawing down too much income coupled with the recent falls in markets. That's a real worry, which we haven't seen borne out yet because drawdown, as the majority at-retirement choice, hasn't been going long enough. But when we get to the point where lots of individuals are running out of money, it will be too late to fix the problem.

Byrne: I totally agree on that point. This is actually a spending issue as much as anything else. Individuals need more information around what the impact of their spending plans is. That requires some kind of estimation around the forward-looking objective of your pot if you continue to spend as such. Obviously, we find ourselves in a really difficult environment where people need to spend more to maintain a basket of goods and their pot size may have gone down. But without the information around what the

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potential impact on the future looks like, it becomes an incredibly difficult issue.

Burden: We should be thinking again about the case for annuities, because annuity rates have massively improved over the past couple of years and became really competitive for a very short period in particular. Members want a secure, steady income over a long period of time and that's what annuities provide. Drawdown has been perceived as an answer because members can take more cash than they should but it is not a like for like comparison if members are drawing down more than is affordable.

Investment trends

Chair: We've had a 10-year-plus bull market. I think the industry may have forgotten that markets can go down as well as up and there's no one right answer, it depends so much on your particular scheme. What do we think the prospects are for interest rates particularly, ignoring overall equity returns, in the next two to three years? Do we think that interest rates have stabilised where they are?

Byrne: There's a danger of people repositioning portfolios to solve what has just happened in the past 12 months, and then maintain that exposure. We must think about, well what role do bonds play? How am I getting access to those bonds? If I buy a blunt index instrument, what is the interest rate sensitivity? Where am I positioned? Fortunately, the investment toolkit has expanded, so there could be more precision around how we get access to fixed income or parts of the fixed income market. I think there's a bit of a rethinking to say, well, there's the volatility associated with interest rates, and there is possibly an increase in the risks of policy error – meaning bonds could be impacted by these risk factors. So, how we access fixed income might be revisited, but I don't think we can turn our back on fixed income as an asset class within pensions portfolios.

Innovation

Chair: What innovation are we going to see and how effective will it be?

Burden: Collective DC (CDC) in the retirement space is another alternative to annuity purchase. I think that's a really interesting idea. It's about essentially improving the income that individuals could get through that period, whilst managing risk in a more proportionate manner. For the industry as a whole it's the part of journey that isn't working well and where we need new options that provide better value to members.

Swynnerton: It seems like there does seem to be some coalescing of views around what people need in retirement, which is probably more flexibility and ability to manage longevity risk. Possibly we'll see more products that are designed to help with that. But also, particularly for non-advised individuals, there could be existing products that could be better used within post-retirement structures to provide the flexibility of drawdown, with the security an annuity provides.

Moore: Objectives vary so differently for individuals in retirement. You could have someone who is single, low life expectancy and no plans to leave an inheritance, and then someone married, supporting their kids, with loads of DB savings. It's just so broad.

Another tricky issue is that you don't really get linear spending patterns in retirement. There's a lot of evidence around people wanting to spend early in retirement when they may be a bit fitter, more active, or wanting to clear debts. Then you get a dip down in spending. Followed by a surge in costs later, perhaps when health isn't so good.

So, to Matthew *[Swynnerton]*'s point, we probably do need a mix of income, security and growth, and to be able to cover unexpected short-term liquidity needs. Personally, I can see a role for annuities in there. Cognitive decline gets worse around age 80 and people are more vulnerable, so actually there is a need for something more protective in later life, like bringing in annuities.

One of the barriers around using deferred annuities has been pricing, so it might be interesting to see if and

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how that's going to change, given the shifts we've seen recently. There have been some products, particularly in the US, which tried to blend drawdown and annuities, although bulk-buying annuities on behalf of members can throw up all sorts of issues for product design.

Byrne: What we see in markets like the US is the incorporation of more DB-like features into DC defaults – and I emphasise the default there. I agree with the statement that what people want is a paycheck in retirement; they want income security; they want to reduce the variability of that income; and they want to manage longevity risk. This is not easy.

Within some of the strategies we look at, what we've seen is thinking around lifetime income as an asset class. Essentially what it means is putting something aside within the default, as you get closer to retirement, which will eventually convert into an income stream in retirement. That has a lot of DB-like features, in the sense that you have a defined income stream; you have the option to purchase that income stream; and, there's increased certainty. The more that we can do within DC defaults to incorporate the potential to have lifetime income, the better.

Chair: Sam *[Burden]*, what do you think from the trustee perspective? What would be the restrictions you see on guidance to members?

Burden: The biggest restriction is that there's always a cost. Ideally there will be a budget to be able to pay for every member to have advice, but often you're very restricted around what's available. Some of the providers now have developed guidance that's available, but in many instances it's still quite limited. From a trustee perspective you want to give individuals as much guidance and support as you can, but cost is the biggest restriction and you are dependent on having a sponsor that's willing to help meet the cost, otherwise you're very much dependent on what the provider is doing.

Chair: CDC might not need advice as they are not getting a choice of product at the at-retirement stage.

Moore: The innovation opportunities are there with CDC; the pension for life, while sorting out the longevity risk, and investment pooling which can target better returns.

Chair: So, CDC, is that not just a form of with-profit annuity which no actuaries will say yes to?

Burden: We need to see the final CDC design because there's a lot of debate and conjecture as to whether it is genuinely viable. The basis of CDC is actually being able to invest in higher growth assets but with some smoothing so in that respect it is akin to with-profit products.

Chair: Both products are heavily reliant on an actuary, someone making a decision about how much income for members is sustainable. The big question is, how much information do you give people about products like this to keep them informed, but not to confuse?

Moore: Helping members take sensible decisions at retirement is still a massive gap which needs fixing. One of the big trends coming from the market issues this year, has been the increase in schemes putting in place preferred IFA support to secure financial advice discounts for members, and running financial wellbeing seminars and initiatives. Although that kind of support package is something which many schemes have been thinking about for a while, recent events have really brought things into focus and made schemes reflect on the positive difference it can make, and they are proactively choosing to do something about it and take action.

Chair: We've mentioned briefly – but not gone into depth on – longevity. We've seen with Covid-19, the development of mRNA vaccines in very short periods of time and they're moving on rapidly with what else can we use mRNA for. Plus gene therapy for cancer, they reckon that could double the life expectancy of people with cancer. Now okay, it might be from two or three years, to six years, but that's still fairly significant. Women tend to retire at 60 and in turn live longer. White-collar workers tend to retire at 60 and live longer. There's a lot of discussion about what life expectancy could be in the future, but we just need to understand what it is today. Because most people vastly underestimate how long they're going to live.

Moore: On innovation, we've talked about decumulation but there's still lots happening in the pre-retirement phase as well, particularly around multi-factor solutions, diversifying the sources of return and bringing in less-liquid exposures.

Within The Aon MasterTrust the team have put in place a target-driven investment approach. It's based on looking ahead to the projected retirement outcome for members, then working backwards to construct an investment strategy to meet that end goal; so, it brings those helpful DB strategy concepts into DC.

If members do experience positive market returns and move significantly ahead of target, we can de-risk a bit. I think that's proved quite helpful recently. Obviously, there's lots of challenges and it's never going to be perfect, but it's also thinking about the fact that traditional lifestyling in DC is not perfect either; switching assets just based on a pre-agreed strategy without any cognisance of market conditions, or where members are trying to get to, is fraught with even more challenges.

Retirement expectations

Chair: That brings us nicely onto the next question, which is around retirement expectations, as discussed in Phoenix Insights' recent *Great Expectations: Are people's retirement income expectations adequate and achievable* report.

The PLSA Retirement Living Standards are partly an extension of some work done a decade or so ago by Winterthur/Axa. At the top level would be someone in retirement on a yacht in the Caribbean having a holiday. The middle one was someone in their local restaurant, a McDonalds, having a burger. The bottom one was someone living under an arch at Charing Cross. We perhaps need that kind of vivid communication for members, whether it's pictorial or in words. Those were some of the things I picked up from the report. What else did people find from the report?

Byrne: Just broadly, there's a lack of confidence – or clarity - around what a retirement outlook looks like. Providing supportive services to members, like regular financial health MOTs or checks on their pension, is what's required early on. Additionally, from a default design perspective, the other thing we have to consider is real world insights and how we construct defaults. Not necessarily solving things like people not being confident in their investments, but rather understanding that savers have lots of volatility within their own lives.

So, they may have variability of income; be in and out of work; and see wages go up and then peter off. So, for me, this highlights the importance of these real-world inputs into default design.

Also, if you just tell people to save more it's quite a blunt and difficult message. What we can focus on is people's financial wellbeing, and associate their pension savings or emergency savings with a broader attitude to financial wellbeing.

Burden: The PLSA have done a great job on the Retirement Living Standards. One of the pieces it misses however is when you do not own your own home because renting hugely increases your living costs in retirement.

The assumption has always been that people own their own home at retirement, but there's a growing proportion of pensioners who are now renting in retirement and that means they're having to carry on working to fund that. There comes a point where you can't do that any longer. It was a really helpful report and it showed the lack of awareness and the challenge around retirement expectations, particularly in the current economic environment.

Moore: Contributions are such a big factor. Although the industry needs to be a little more thoughtful around communication during of the cost-of-living crisis, as clearly a 'pay more' campaign isn't necessarily going to be as effective.

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Many schemes that I've worked with have been more cautious around encouraging contribution increases and shifted the focus to financial wellbeing. Some schemes have offered employees the option to pause contributions but structured it so the employer still pays theirs, just for the time being. But fundamentally you want to get contributions up because current levels are not going to be enough *[to provide an adequate retirement income]*, it's just that timing is tricky for some people.

Burden: It's very difficult to ask people to increase their pension contributions when their energy costs have stepped up and their mortgage is going to increase next year.

Swynnerton: It seems like a very challenging time to be delivering those kinds of messages generally. But I think the report does support a lot of what we've been discussing, particularly around longevity, and the mismatch between people's retirement expectations and the likely reality. I think it's very helpful that these themes are drawn out.

Illiquid assets

Chair: Moving on then to illiquid assets, there is clearly some pressure from the government on the industry to introduce illiquids, with the Department for Work and Pensions' (DWP) recent consultation on 'Broadening the investment opportunities of defined contribution pension schemes'. Is it a good thing to have illiquids in DC portfolios?

Byrne: We are supportive of the proposed amendment. We think schemes documenting their allocation policy to illiquids is a good thing. We like the fact that it covers a broad range of illiquid asset classes too. We think DC schemes should explore these investment opportunities offered by private markets. But also think it's important to note that a good default doesn't necessarily mean one that owns private markets, and a bad default is one that doesn't. How they access, and how they grow the allocation is key.

I think it's helpful to understand different schemes attitudes and their objectives. I think there's a lot to consider when you're allocating to private assets, it's not as simple as buying a multi-factor fund or flipping your home country bias in your equity exposure.

Moore: The investment rationale feels sounds. When we take a step back to basics with DC, we're talking about members with typically a very long-time horizon and low liquidity needs. So, it makes sense to try and take advantage of the illiquidity premium and the opportunity to diversify those sources of return. When we've been working with managers and giving feedback on launching LTAFs *[which meet the Long Term Asset Fund regime]* the main challenges are around platform constraints, which we know is always a challenge in DC investing, and managing costs.

As these less liquid assets are more expensive, and we are in a charge cap world; naturally we are constrained. Most illiquid products, to be DC-friendly and for this work, need to blend in some liquid exposure. So actually, how much true exposure to illiquid assets are you really getting, and how can we find the right balance? Also, another issue is trustee perception of lower liquidity, and gating risk. I think potentially this is going to be an important issue, not just managing the risks themselves but also trustee nervousness because of past experiences.

The new regulations require disclosing the asset allocation for illiquids, which makes sense; it's a suitably straightforward measure but helps with trustees having to properly engage and explain their policies. My reservations are around the fact that in most cases schemes will just be showing the end result. In practice there's a lot of thinking, and modelling and analysis, and discussion, and reasoning around objectives, which goes into forming a strategy. Yet when you just see it laid bare in terms of the asset allocation alone, there's so much more underlying that which just won't come across.

Swynnerton: It seems like the government has listened to some of the concerns that have been raised over the proposed requirements, particularly the disclosure requirements, and a slimmed down version will hopefully be less prescriptive and burdensome, so that is I think positive. As we've seen the shift

DC roundtable

in the pensions landscape from DB to DC over the past 20 years, it seems right that there should be the ability for DC members to invest in the same kind of assets that have been available to DB schemes for a long time.

There's also the increasing focus on ESG, sustainable investments like social housing and wind farms are things, where illiquidity is an integral factor, that we'll increasingly see investment in. But there's a lot of development that still needs to happen because to date there hasn't been the demand. Therefore, there is not the pressure on providers to make these kind of products available and in a sophisticated way. As a result, there's probably still a lot more that needs to be done from policymakers and regulators in terms of driving that change.

Burden: If you look at the Australian superannuation schemes, they've got a greater portion of their assets in illiquids than we have. The UK government see this as a great opportunity to release investment and capital. But it's all about scale, you need big funds to be able to do this and UK funds are still much smaller than their Australian counterparts.

With my trustee hat on I would be really cautious about illiquids in DC. I'm working on a couple of buy-ins for DB schemes at the moment and one of the real challenges is where you've got illiquid assets. We're probably going to be in recession for a period of time and trying to sell illiquid assets in a depressed market is not easy. Investment in illiquids needs real care and you need that scale so that you're not going to be a forced seller at the wrong time.

Chair: I agree with you entirely on that. Master trusts can afford to do so. If you're a standalone DC scheme, what are the odds that you're going to get moved to a master trust and therefore, if you've invested in illiquids, when does that get

taken into consideration? I think it would be healthy to have a statement from the current Minister of Pensions on what her policy is for consolidation in the markets, because *[former Pensions Minister]* Guy Opperman was very keen on consolidation and wanting all the small DC schemes to disappear fairly quickly. Which is actually completely counter to being able to invest in infrastructure – you can't do both because of the transition difficulties.

Byrne: One thing that has been really encouraging over the past couple of years is the significant change from discussing how do we do this, rather than why do we do it. Despite consolidation, I believe a number of schemes will see the benefits of owning private assets, and be able to access the asset class going forward as they strive for more sophistication.

The other thing that I see is really encouraging, is there is a joint desire to get this done, not just from asset managers, as you'd expect, but also platforms and advisers. That level of consistency hasn't been there before.

Sharia law

Chair: Moving to Sharia law. How well is your scheme working with Sharia investment? Are we seeing much take up, given about 6 per cent of the population in theory, is Muslim?

Burden: The starting point is the same as for any other member. Most members aren't engaged as to where they are invested, and your typical Muslim member is probably no different. We haven't seen huge take up on any of the schemes that I've had any contact with, it's been by exception really and that reflects low levels of overall member engagement.

One of the problems is that all we do is offer a fund and that's not good enough. I've not seen a Sharia de-risking strategy in place. There are limitations around where you're allowed to invest, but surely the industry can come up with a de-risking strategy that we all acknowledge is essential for members approaching retirement.

Moore: There is a small but growing market in sukuk bonds, the equivalent of traditional bonds with a payment stream, but investable under Sharia law. There aren't yet funds for DC, but it feels like the next development.

For schemes offering Sharia equity,

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DC roundtable

it's tricky, because from an investment perspective it will seem relatively expensive for a passive equity fund. But that's partly driven by the dividend cleansing process and having an independent Sharia board. The fund itself is very concentrated which increases risk, but as we all know there is a lack of competition and only really currently one platform-friendly fund option, so schemes are limited in what they can do. Our team has been looking at both the equity and bond options and the level of demand, to see if we can potentially work with a manager and launch an option to improve competition. The main issue is lack of scale, given the difficulty in getting traction on self-select options, and the knock-on impact for costs.

Swynnerton: Some unions have helped workers bring complaints brought against employers who have failed to offer Sharia funds in the DC space. The requirement to provide Sharia law compliant funds is more problematic in the DB space, because for DB schemes it's really impossible to comply with Sharia rules relating to investment and insurance given scheme funding requirements necessitate interest bearing assets to back liabilities and the provision of a Sharia law compliant DC vehicle as an alternative for their DB members is unlikely to be able to provide the same level of benefits that they can through DB.

In the DC world, even where a Sharia-law-compliant option is available, quite often it will be just a single Sharia-compliant fund that is made available. That raises questions as to whether that in itself is discriminatory because it doesn't provide sufficient diversification of investment choice, compared to what's available to non-Muslim members. As a result, the Muslim members are being disadvantaged and have a potential discrimination claim.

Even within Sharia-compliant funds there are differences of opinion between Islamic scholars as to what constitutes Sharia compliance and also amongst Muslim members about what constitutes Sharia compliance. So just because you offer a Sharia-compliant fund doesn't necessarily mean that any particular Muslim member may regard it as Sharia compliant.

Also many Muslim members may participate in non-Sharia compliant funds. They also potentially have a claim that they've been discriminated against because they've been forced to compromise their religious beliefs by participating in a non-Sharia compliant fund in order to benefit from the financial benefits of the scheme.

Certainly some of my clients have been on the receiving end of complaints, but at the moment, there has been no reported case of a successful claim in the tribunals, courts or the Pensions Ombudsman in this area. However, if a discrimination claim one were to be brought where a Sharia-compliant fund wasn't provided, it is certainly possible that it could succeed.

Given that this is an untested area, there could be possible defences for employers and trustees. For example, until Muslim workers come forward, it's impossible to know whether they need to provide a Sharia law compliant scheme given that religious belief is a protected characteristic that they can't easily ask about or keep records on.

Auto-enrolment

Chair: Auto-enrolment 10 years on, has it been a success? Should the regulator be more proactive in enforcement and what are the difficulties faced by the regulators in doing this? Has it been successful?

Moore: I feel like it's been undeniably successful in getting more people saving towards retirement, just looking back to where we were, it's a huge improvement. What's interesting for me is then the next issue, because as an industry we know that many people are just not saving anywhere near enough. So, a fantastic success, but clearly more to do to address the underlying adequacy risks, and making sure we communicate effectively with members so they know how they can make sure they're on track for the quality of retirement they want and

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expect.

Burden: It's been a huge success but the question now is what's next and there's three obvious steps to my mind. The self-employed are a big a group who aren't saving sufficiently for retirement. Part-time workers need legislative change so that every pound of pay is pensioned. Thirdly we need to increase the minimum level of contributions for everyone.

Swynnerton: I think the obvious way to get more people automatically enrolled and contributing more will be to reduce the minimum age threshold and reduce the lower earnings threshold, or remove it completely, which hopefully will happen. Then it's broadening auto-enrolment out to the gig economy, that's obviously a focus for the regulator at the moment. That's an area where there seems to be quite a lot of challenges, because the auto-enrolment regime was designed when the gig economy was really in its infancy, so it's very much based around traditional employment relationships, as opposed to more flexible arrangements, where workers may multi-app for a number of different businesses. There needs some regulatory change I think to make the regime sit more happily with those new kind of business models.

Moore: We need to capitalise on auto-escalation, to make sure that we get to a level of saving that's high enough. A minimum of 12 per cent in the next year, it feels like we need to try and get there.

Byrne: On the gig economy, I think we are seeing interest in different ways for people to save for their pensions. I think options to doing it are really important, such as saving through a SIPP, and if that SIPP can be accessed through an app, and it's as simple as increasing savings every month, then that is a fantastic thing! I think it aligns with the changing nature of how people work, and how they engage with their financial services. They still want an asset manager or a provider to do it for them and so supporting products that can deal with that advancement are very helpful.

Dashboards

Chair: Onto dashboards, how prepared are we in the industry?

Byrne: I think it's understanding the implications for different parts of the pension industry, and I don't think that's well understood yet. It feels to me that we know we've still quite a lot to do in terms of filtering that through to different stakeholders.

Moore: DC data tends to be digitised and more recent than DB data, so there are fewer historical issues *[for connecting to dashboards]*. DC projections are more of an issue, given the recent changes to TM1, but schemes have time to get that in place, so no particular concerns there. DB in contrast has a lot of issues, both with historic data and the complexity of the calculations.

One issue is how does your engagement strategy change when you move from a world without dashboards to a world with dashboards? I was chatting to one of our dashboard specialists the other day and really liked his analogy, comparing it to being like a car insurer going from a world where price comparison sites didn't exist, to one where they do; the underlying product is the same but the way in which people engage changes so dramatically.

Swynnerton: In terms of whether we're ready, there's going to be a lot that needs to happen in a relatively short period of time. The idea is that the final regulations are published as soon as possible so people have a longer time to get their heads around them. So that's positive and will help people to get ready. How easy it will be, however, I think still probably remains to be seen.

It certainly feels as though dashboards are something that schemes have been putting off because to date they haven't really needed to engage with it and they've got so much else on their plate. It just feels like it's been something that hasn't had enough focus but I think people are going to have to act very quickly.

A change of plan

As recent research has found that almost half of global asset owners were not happy with their investment performance in 2022, *Pensions Age* asks: How may pensions schemes' investment strategies change in 2023 compared to 2022?

Rising (and more volatile) inflation expectations and higher interest rates, alongside the prospect of recessions, will be key global themes driving investment strategies for 2023. A special case applies in the UK, where the ramifications from the recent volatility in government bonds will be playing out, likely resulting in reduced use of leverage, more care around illiquid assets, and possibly lower return targets. More widely, geopolitical tensions may lead some schemes to rethink their allocations to certain regions. Following the succession of 'extreme' events (Covid, war, inflation etc), some investors may be looking to add explicit protection strategies to improve portfolio robustness under downside events. Finally, sustainable investment practices will continue to become more prevalent, with many larger schemes setting out explicit net-zero targets – this will mean specifically investing more in positive-impact opportunities, and less in companies that could be adversely affected by the transition to a greener economy and using investment vehicles that facilitate this.

WTW DB solutions specialist, Lok Ma

The events witnessed in 2022 – from war in Ukraine to the LDI crisis – have been seismic reminders of just how volatile markets can be, and that 'once in a lifetime' events may be more common than we think. Moreover, they have put a firm marker in the ground for the end of the low-interest, low-inflation, steady-growth environment we have all become so accustomed to.

This tectonic shift in the macro ecosystem, coupled with the huge moves in both fixed income and equity, has resulted in the beginning of a completely new economic era that will undoubtedly cause a number of investors to change their strategies – even though many have been reasonably happy with how they have performed over the past year.

For DB schemes, many have been fortunate to see their liabilities shift such that they are now closer to buyout, leading to an inevitable de-risking of portfolios. For others, the drop in fixed income and equities will need them to hold off allocations into illiquids thanks to the 'denominator effect'. On the flip side, the complete breakdown of the traditional fixed income and equity inverse relationship now means illiquids may well form a bigger part of some DB scheme's allocations – the days where you could rely on fixed income and listed equity to act as your diversifier are long gone.

Ironically, whilst DB schemes came out bruised but alive from the LDI issues, many DC schemes saw member's portfolios drop substantially – the lack of investment into illiquids meaning they were unable to diversify away a portion of this year's systemic risks. As such, there are now a number of larger DC schemes beginning to look more closely at allocating into this asset class.

Broader themes encompassing all investors are the increased focus not just on ESG (which is becoming a pre-requisite) but impact strategies, as well as a renewed interest in active management, given the changing landscape. The former is of particular interest for LGPS, whom are seeing increasing messaging from government about the importance of local place-based impact investing.

Octopus Investments director of institutional business, Jason Bermont-Penn

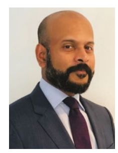
The gilt market volatility and its impact on the LDI market will be the key driver of pension scheme investment strategies in 2023. Reduced leverage will force the biggest change to portfolio design in a decade. The world of low-risk growth, hedged liability risk and low funding volatility is not possible. Tough choices need to be made between liquidity risk, hedging levels and returns. This may well have to be done in a recessionary environment where company covenants are probably weaker. The ultimate destination of pension schemes will drive asset allocation – those focused on buyout are likely look to lock down risks and align portfolios with the insurance market. Those with a longer-time frame will be in a strong position to capitalise on less-liquid assets being sold at attractive prices. 2022 was testing for many pension schemes. 2023 will be the year of big investment change.

Aon partner, Calum Mackenzie

Perhaps the most long-term concern to trustees will be restructuring portfolios to address the problems posed by inflation. For defined benefit (DB) schemes, there is likely to be a greater emphasis on hedging strategies with index-linked gilts playing a more prominent role. Trustees of defined contribution (DC) schemes are likely to review derisking strategies to ensure that lifestyling switches in particular do not have a detrimental impact on the real value of members' funds.

Trustees will have learned much from the economic traumas of 2022. It is to be hoped that they will now be better prepared for the challenges of the new year.

PMI director of policy and external affairs, Tim Middleton



Within DC pensions, the competitive environment with regards to fees has made allocating to private and illiquid markets challenging. This will however be a key area of focus for pension schemes going into 2023, to allow members to access the illiquidity premium to try and help them achieve better outcomes. ESG integration will also continue to be important as schemes look for ESG integration across all asset classes, covering the entire member journey.

Aviva head of investment strategy and proposition, Maiyuresh Rajah

Many schemes' funding levels improved markedly in 2022, and if their hedges remained in place through the 'mini-budget' induced yield spikes, they are very likely to be ahead of plan. Their required investment returns will be lower going forwards and many schemes may now be much nearer their long-term objective.

Schemes are likely to be overweight in their illiquid assets, such as private equity. As they are nearer their end game, that's not a position they would wish to maintain. Market innovation will be required to address this issue and unwind illiquid positions in preparation for buyout. Some potential solutions are beginning to emerge, including specialist funds to buy these assets without an excessive discount in value but more creativity is needed here, with sponsors and trustees working together to unlock the ability for well-funded schemes to settle their liabilities with an insurer.

Isio partner, Ed Wilson

The re-emergence of inflation and the attendant higher interest rates fundamentally change the nature of equity investing.

First, bonds will be much less attractive in this environment and investors will increasingly seek out investments that can help protect them against inflation. This is likely to mean a renewed focus on equities. Secondly, given the relatively high valuation level (still) of many stock markets relative to their history it is likely that, as in the 1970s, dividends will in future form a much larger proportion of total equity returns than has been the case in recent decades. For example, in the 1970s dividends represented over 75 per cent of total shareholder returns versus barely 25 per cent in the 2010s. Thirdly, with the higher costs of debt, investors will be less forgiving of corporate leverage and of lower-quality corporate earnings. They are therefore likely to adapt their strategies to concentrate more on equities with better-quality earnings and balance sheets and with a greater focus on growing dividends as a key driver of total investment returns.

Guinness Global Investors head of institutional, Charlie Crole

Pensions history

Recollections may differ......

Depictions of Janus, the Roman god of beginnings, endings, and transitions that we remember in January, shows him looking backwards to the year just gone and forward to the year ahead. Modern newspapers do the same with their 'reviews of the year' and New Year predictions.

In this column, I remind readers of past events that shaped our pensions system and try to relate contemporary materials from the Pensions Archive Trust (PAT)'s to provide context to the change. Hindsight is not the best way to help us understand why decisions were made, practices adopted or policies chosen. Not only may recollections differ, but misunderstandings can arise if we do not appreciate the social, commercial and political background against which these decisions were made. Those who cannot learn from history are doomed to repeat it.

PAT's archives record corporate responsibility in action, years before it became fashionable. They record the events which thrust change onto employers and schemes and track the effect of policy responses. Our records are essential reading for anyone interested in past pensions policy or its future development.

Our New Year's resolution? To increase the number and scope of our collections and digitise more to better share this little known, if somewhat battered, British success story. Contact us to find out more.

www: pensionsarchive.org.uk

The Pensions Archive Trust director, Jane Marshall

Fun and games

Wordsearch

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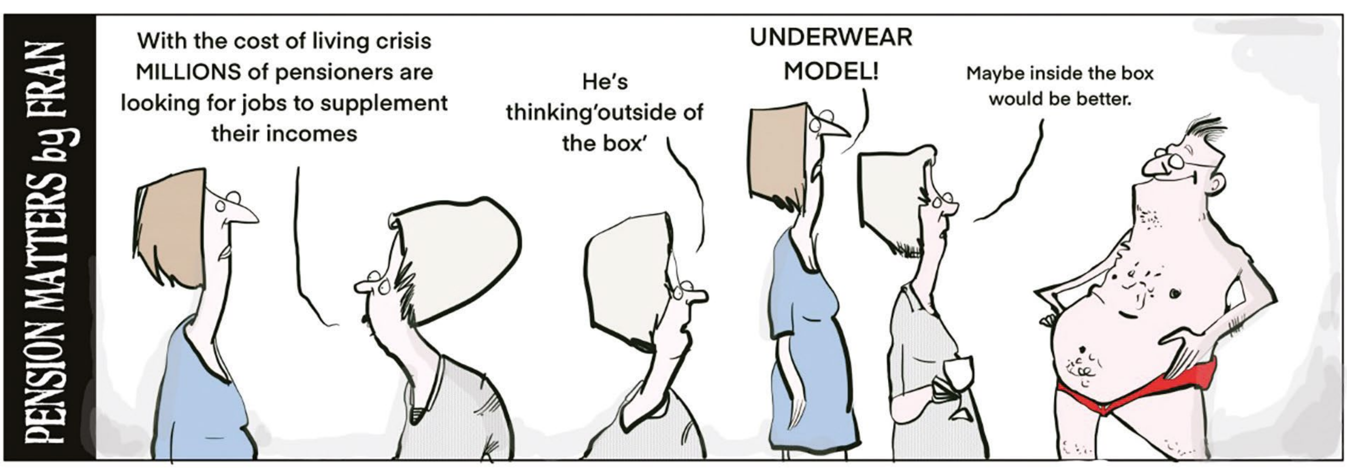
AUTO ENROLMENT
DASHBOARDS
GREENWASHING
LABOUR
LDI
REFORMS
SCAMS
SOLVENCY II
TRUSTEES
YEAR AHEAD

I know that face...

Answer at bottom of page



I know that face... Answer: Legal & General investment committee chair and trustee, Tegs Harding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