Sackers

DC briefing

October 2014

Highlighting the latest developments in DC for trustees and employers

Welcome

Welcome to our first edition of DC briefing, which highlights topical news on DC pensions from a legal viewpoint.

We are living in times when DC pensions are regularly hitting the headlines and generating political debate. All eyes are on April 2015 when a host of changes will go live and the doors will open to either a world of flexibility or Pandora's box (depending on your opinion). Either way, "retirement savings" will never be quite the same again.

Speaking to both trustees and employers, it seems there is so much going on that it can be difficult to work out what to do for the best. Clearly, there is a difference between what must be done and what could be done. You do not need to do everything by next April – many schemes have limited resources and there is only so much you can do in the time available.

Schemes can get through the next few months by prioritising and not trying to do too much too quickly. It is an important time in the industry for us all to ask each other questions – no question is ever too small or silly. We have picked on some of the common questions of the moment in this first issue of our new briefing. We hope you enjoy it, and would welcome your feedback.

Four key DC issues

Charge cap – don't get caught out

We are still expecting the charge cap of 0.75% on default investment funds to apply from April next year. Now is the time to check whether your default complies because, if it does not, you will need to act quickly to make changes. We do not believe transaction charges will be covered in the 0.75% initially, essentially because there is not enough clarity on what they are in different funds or how to quantify them at the moment.

In a trust based scheme, investment powers will usually be wide enough to change the composition of funds without members' consent to bring charges down. While this might not be attractive, the existing fund design is likely to be the fruits of many months' consideration, at least it should be achievable, even if you are just starting to engage with your investment consultants now.

However, if you are using a contract based scheme with an insurance provider there is unlikely to be so much flexibility, and it may come down to a straightforward negotiation with the provider on fees. They should not be surprised you are asking given how high profile this issue is and the pressure on firms to reduce their charges.

Technically, the cap applies just to default funds in schemes used for automatic enrolment (AE), but since most people who are currently in a workplace pension scheme will either have been auto-enrolled into it, or be in a scheme that qualifies for AE purposes so they do not need to be enrolled in another scheme, in practice it is an issue for most schemes.

Four key DC issues cont.

Drawbacks with lifestyle funds

Lifestyle funds, which gradually move members out of higher risk assets into more stable funds as they near their target retirement date, have been designed with the expectation that at retirement members will take some cash and buy an annuity with the rest.

They may therefore need to be redesigned in response to members' ability to use their funds for cash and drawdown (as well as an annuity) from April 2015.

Initially, it is worth spending some time thinking about what information members need about the impact on their investment choices, rather than rushing to design new fund options. Does your scheme offer individual funds as an alternative to lifestyle that members could use if they want to diversify out of money markets and bonds if they want to use drawdown?

Also, are the money market and bond funds members are in close to retirement suitable if they want to take cash? A fall in bond values may not matter if someone is about to buy an annuity, and annuity prices have gone the same way, but could make a big dent in the cash fund the member was expecting to take.

Given the percentages of people who default into lifestyle funds, many schemes are going to need to redesign them. But it is worth analysing how quickly current investment strategies are going to become an issue for the current membership, and educating members about their options, before jumping in at the deep end.

Guidance guarantee – don't panic

We are still waiting to see what the legal requirements for this are going to look like. But the FCA's proposed structure in its consultation document looks sensible. Yes, it is going to be tough to deliver (by TPAS and MAS and other "delivery partners"), and yes it is generally going to be too late if people do not actually start to think about what they want their retirement savings to deliver until four months before they retire, but it is a start.

Schemes will need to familiarise themselves with the way the guidance guarantee will be delivered so they are ready to provide members with the information they will need about their pension in order to get the most out of their guidance session. In a nutshell, think about what you would expect an impartial financial adviser to need to see in order to have a meaningful discussion with you about your pension, and that is the information people will need.

Schemes will also need to signpost the guidance guarantee.

It looks like this will mean:

- setting out clearly the fact that the guidance is available, and that it is free and impartial
- showing clearly how the service can be accessed
- providing the information the member will need to make an informed decision about their pension savings (whether or not they use the guidance).

Signposting of itself should not be onerous for schemes, but follow-up questions from guidance may impact on scheme resources. As the guidance guarantee develops, it will make sense for schemes to think about how they might evolve their communications and broaden out their current annuity broking arrangements to help educate members before they even use the guidance service.

New legal requirements for DC

We are expecting requirements for DC as part of the Government's drive to create a more level playing field between trust and contract based schemes. Looking at what appears in current codes and consultations, but does not currently appear in legislation, it looks like we could see a considerable addition to DC specific legislation in the shape of requirements for trustees to:

- assess value for money (ie weighing the quality of the scheme against its cost to members)
- comply with a charge cap on default funds
- produce an annual governance statement
- assess whether default investment strategies are designed in members' interests, with a clear statement of aims, objectives and structure appropriate for scheme members
- review regularly the characteristics and net performance of all investment strategies to ensure they align with members' interests, and make any necessary changes
- ensure that core scheme financial transactions are processed promptly and accurately.

And this will probably be complemented by a new power for TPR to intervene "in situations where members' savings may be at risk because of a lack of oversight".

Spotlight: communication

If we think of pension savings in car terms, a DC member sits in the driving seat. Contrast this to a DB member, who is really more of a passenger. To make sure the car goes in the right direction, the driver needs a clear road map and sound directions. The same goes for a DC member.

Trustees and employers are, in effect, a form of "sat-nav". They have the knowledge and experience to help explain which general direction members should be going in. But they cannot be too specific and give financial advice. That is not easy at the best of times and, with all the changes going on at the moment, there is a lot of scope for confusion.

The buzzword of the moment is "communication"

It is all over trustee meeting agendas and looks set to become one of the biggest risk areas in the next few months as schemes introduce new flexibility over their retirement options and review their default investment strategies. The possibility of slipping up is huge, with a real chance of members making the wrong choice and so ending up at the wrong retirement destination.

So what should trustees be doing right now?

1 Agree key messages

It is a good idea for the trustees and employer to agree on the key messages they want to get across to members. That way, the trustees can align their strategy with that of the employer. After all, if different messages are coming through, that is only going to add to any confusion.

2 Use help points

There are places to go to for help. There is plenty of commentary in the DC Code of Practice and related guidance issued by TPR.

3 Keep it simple

The more complicated you make it, the more chance there is that the message will be misunderstood. Outside of the usual statutory disclosure requirements, what is the "right" information will differ from one scheme to the next. While there is a current trend to think about "segmenting" memberships, for example, by age and pot size (which brings its own risks), general information which contains clear signposting can be equally effective.

4 Seek feedback

Trustees can analyse member behaviour and seek member feedback. This can be a good way of finding out if your message has got through and achieved what you were hoping for.

5 Get it right

Last but not least, make sure any facts provided are accurate.

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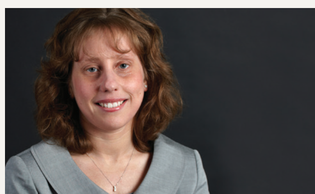
Contact

Sackers is the leading law firm for pension scheme trustees and employers. Over fifty lawyers focus on pensions and its related areas, including our DC experts who provide practical and specialist help on all aspects of DC schemes. For more information on any of the articles in this briefing, please get in touch with Helen Ball, Faith Dickson or your usual Sackers contact.



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Upcoming seminars & events

We offer an extensive programme of workshops, seminars and trustee training specifically on DC issues and developments. If you would like to attend any of our events, please contact our marketing team at marketing@sackers.com or visit www.sackers.com.

Event	Date	Details
DC: What is your plan?	06/11/2014	Morning seminar (9.00am-10.30am) Aimed at trustees and employers of schemes with DC benefits, this seminar will explain which decisions must be made in the next few months and which can be left until later. We will also offer practical tips to help you deal with common concerns, and identify the major pitfalls to be avoided.
NAPF Hot Topic Seminar: Good Pension Scheme Governance	18/11/2014	With new codes of practice from TPR on DB and DC, trustees are under ever more pressure to demonstrate good governance. Sponsored by Sackers, this all day seminar at NAPF's London office is aimed at everyone involved in the governance of both DC and DB pension schemes. It will help attendees learn about the latest governance issues and best practice, with practical case studies and briefings on the latest regulatory changes.
DC trustee training	05/02/2015	Afternoon workshop (1.00pm-4.30pm) Aimed at new trustees or those wanting an introduction to DC benefits, this seminar will look at key legal issues for trustees. The session will provide an overview of trustee powers and duties, legal requirements including minimum standards, investment, TPR's approach to DC regulation, retirement options (including the 2014 Budget changes), communications, and disputes.

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