Sackers

Corporate briefing

July 2022

Highlighting the latest developments in pensions for employers and corporate investors

Welcome

2022 has been an eventful year to date. The war in Ukraine, combined with rocketing inflation and general economic uncertainty, has impacted schemes and employers in different ways.

Despite the uncertainties, some employers are finding that the current economic environment has improved the funding position in their DB schemes. This will come as a relief to some finance directors, whilst the current circumstances might prompt others to reconsider pension arrangements more generally, both DB and DC. On pages 1 and 2, we take a look at the types of things that might be on the back burner, but where there could be opportunities to find solutions sooner than you think.

The Pensions Regulator ("TPR") published its annual funding statement for DB schemes in spring this year and we also take a look at what this means for DB sponsors on page 3 of this briefing.

2022 is also an important year of reflection for other reasons, as it has been 10 years since automatic enrolment was rolled out, resulting in a large increase in both the number of UK pension savers, as well as pension pots. On pages 4 and 5, we consider the key changes over the last decade, as well as looking at some of the issues that we have helped our employer clients resolve over that time.

Finally, we are delighted to let you know we recently won Best Pensions Law Firm at the Corporate Adviser 2022 Awards, a testament to the dedication to pensions of both clients and colleagues alike.

Rise to the pensions challenge!

Perhaps there is nothing on the pensions agenda screaming for your attention for the moment. So is it time to kick back and relax? It might actually be the ideal moment to think about those pensions conundrums that have slid down the to-do list: is there anything you can do now that can save you time and resources in the longer term?

1

Risk transfer and journey plan

Your DB scheme's funding level may be healthy but what is the plan from here? Employers are increasingly taking a more active role in discussions with their trustees on risk transfer (eg buy-in / buy-out) and other end game solutions. Maybe it is time to get on the front foot in these discussions and we can support you with an appropriate strategy in this area.

Rise to the pensions challenge! cont.

2

Clear out that closet

Have you got any legacy pension arrangements that could use some TLC?

Our employer clients, particularly those that have a history of mergers and acquisitions, will often have legacy pension arrangements on their books, sometimes with only a handful of members that have not worked for the employer group for many years.

If you think you might have some of these, you could ask your administrator or HR team to check their records. These smaller, unloved arrangements can be some of the fiddliest to deal with but a few simple steps might go a long way. So it pays to find out what you have now and put a plan in place.

3

Shine a light on your DC benefits

Have you got a small DC scheme, or a DC section of a much larger scheme? With the new "value for members" requirements for schemes with under £100m in assets, you will need to give this scheme some more attention. Are you confident that it is achieving value for members and is well governed? We have helped several of our employer clients work through these questions with their trustees, with some concluding that transferring benefits to a DC master trust is the solution.

4

Are your pensions in the right place?

After business reorganisations, some employers are finding that pension schemes in the group haven't kept pace with people moves, with the result that one part of the business may be looking after pension liabilities for employees that are no longer connected to it. Other employers may have acquired several different schemes over the years.

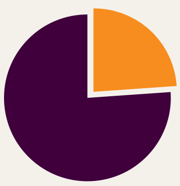
Again, it pays to explore whether reorganising (eg merging / splitting) the pension schemes themselves might better align the benefits with the business. A little time invested upfront agreeing objectives and issue-spotting typically means these sorts of projects run more smoothly to completion.

5

Governance, governance, governance!

Governance requirements on schemes have increased massively over the past few years. This is only set to continue with TPR's new "single code of practice" due later this year, requiring schemes to have an effective system of governance in place, as well as carrying out an "own risk assessment" annually. Do your trustees have the resources to keep up with these requirements? We are always happy to work through any concerns you have in this area and share experience of how sponsors and schemes can be supported in the ever-changing regulatory landscape.

Some highlights from our risk transfer work up to 2021



We advised on 24% of the bulk annuity market over the last three years

Advised on over 55 bulk annuity transactions

totalling over £29bn+

in the last 5yrs

Significant economic uncertainty – TPR's view

TPR published its latest annual funding statement back in April. It focuses on the current period of "significant economic uncertainty" and how this may impact schemes. The statement echoes themes from previous years: an integrated approach to risk management, an emphasis on long-term planning and the importance of an open dialogue between employers and trustees.

The statement is particularly relevant to employers whose DB scheme has a valuation date between 22 September 2021 and 21 September 2022, as well as those whose schemes are "undergoing significant changes that required a review of their funding and risk strategies".

What does the statement mean for employers?

Impact on covenant

Companies can expect increased focus on covenant strength, given high inflation, increasing energy prices, the conflict in Ukraine and the aftermath of the pandemic.

Recovery plan and affordability

How hard will trustees push in light of the statement?

- Where market conditions have had limited impact on the employer's business, TPR advocates a "business as usual" approach to setting deficit repair contributions.
- Where employers are experiencing short-term affordability constraints, it is clear trustees should consider requests to accept a temporary reduction in contributions. But these are expected to be short-term, with higher contributions in subsequent years rather than longer recovery plans.

Shareholder distributions and other covenant leakage

TPR has continuing concerns about employers returning cash to shareholders through recommencing dividends, paying "special" dividends and share buybacks. Companies can therefore expect heightened scrutiny from trustees assessing whether the scheme is being treated fairly when compared with other stakeholders.

Trustees are also expected to be on the lookout for other types of covenant leakage, such as cash pooling arrangements, group trading arrangements and management fees.

Long-term funding target

By way of reminder, the Pension Schemes Act 2021 ("PSA21") provides a framework for introducing a new requirement for trustees of DB schemes to determine (with the agreement of the employer) a strategy for ensuring that scheme benefits can be provided over the long term. The DWP's consultation on draft regulations to introduce this was expected before the summer. However, the new regime is not expected to come into force until late 2023.

As with last year's annual funding statement, TPR notes that the PSA21 will require trustees to have a specific strategy in place to deliver an agreed long-term objective. Whilst these aspects of the PSA21 are not yet in force, companies should expect trustees to start pushing now to agree a long-term funding target with their employer.

Employers with DB schemes should:

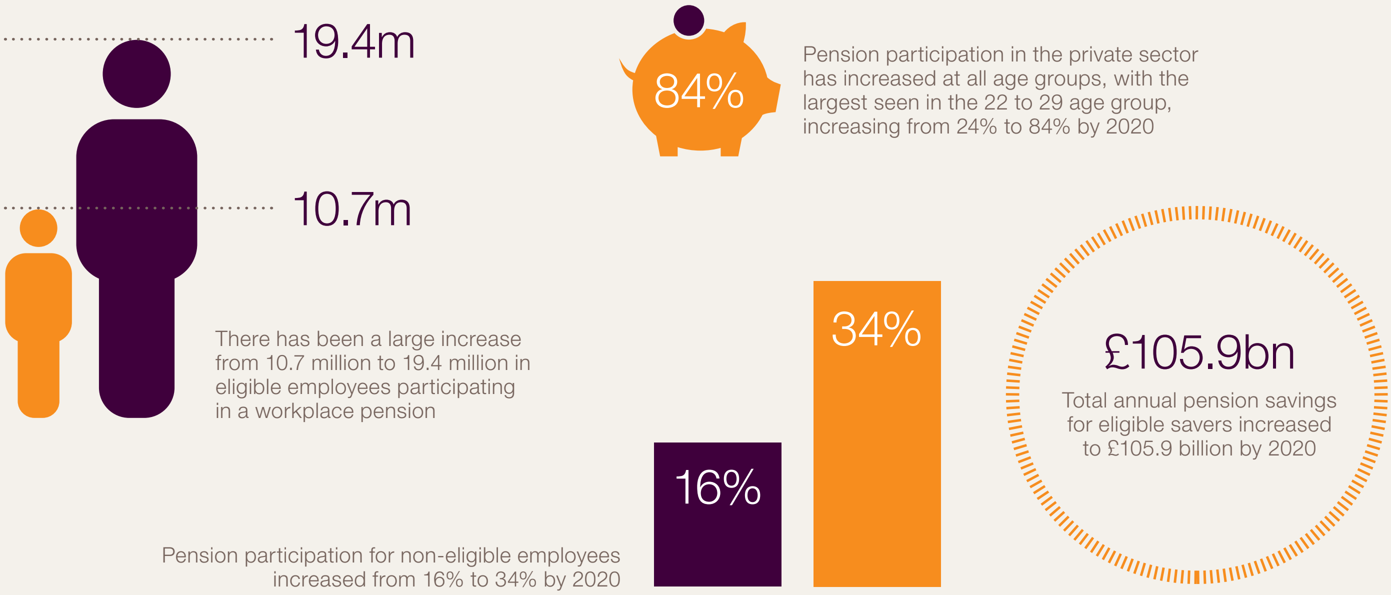
- be prepared for trustees seeking to engage on how the current economic environment has affected your covenant
- consider how the trustees may react to any potential covenant leakage, such as dividend payments
- keep the trustees informed of any corporate activity that could impact covenant and consider mitigation if this could have a detrimental impact on the scheme
- keep an open and ongoing dialogue with the trustees, sharing relevant information.

Automatic enrolment – 10 years on

Automatic enrolment was introduced in 2012 to help address the decline in individuals saving for their retirement and to make long-term pensions saving the "norm".

With automatic enrolment phased in, both in terms of when the requirements first applied based on an employer's size and the percentage of contributions payable to DC arrangements, the roll-out of automatic enrolment was only finally completed in April 2019.

Some key government statistics since 2012



Source: Workplace pension participation and savings trends of eligible employees: 2009 to 2020

Our work with employers on automatic enrolment has evolved significantly over the last decade. From initial compliance issues ranging from technical queries on exactly when employers needed to comply, to working out whether their scheme was a qualifying scheme, we moved on to more "business as usual" issues. These include:

- challenges around identifying eligible employees
- the implications of changing payroll providers
- group re-organisations where employing entities or payroll are changed
- missing workforce sections coming to light
- keeping track of opters out and opters in
- taking care on structuring benefit packages to ensure there is no inducement to opt out
- individuals changing status, eg turning age 22 or earnings suddenly exceeding the qualifying threshold
- ongoing compliance, eg re-enrolment and record keeping.

We have found that by getting the basics right, employers can avoid the cost and time of correcting historic mistakes.

Automatic enrolment – 10 years on cont.

What's still to come?

Since automatic enrolment arrived on the scene, there have been questions as to whether the regime should be expanded. The Automatic Enrolment Review 2017 recommended:

- reducing the lower eligibility age limit from 22 to 18
- removing the lower qualifying earnings threshold (currently £6,240 for 2022/23)

A private member's bill, which would have brought these recommendations into law, failed to make it through Parliament earlier this year. However, Guy Opperman, Pensions Minister, has said that the Government will "in the fullness of time, bring forward or support legislation to take the matter forward", and the Work and Pensions Committee has recently issued a call for evidence asking employers and trade unions when and how the Government should implement the above recommendations.

How we can help

Automatic enrolment requirements are complicated, with many traps for the unwary. Whether you are approaching your re-enrolment date, facing a reorganisation which could impact pension savings, or managing a mobile workforce, Sackers can help ensure your automatic enrolment legal obligations continue to be met.

New notifiable events regime – timings delayed

As discussed in our last briefing, the industry had been expecting a significant shift in companies' duties to disclose information to TPR and trustees to come into force in early April. However, nothing materialised from the DWP and no revised timeline for publication has been given yet.

By way of recap, the notifiable events regime requires trustees and employers to notify TPR when certain events occur in relation to a DB scheme. A DWP consultation last autumn included draft regulations setting out two new notifiable events for employers to report to TPR, relating to material sales and granting or extending certain security. Under the proposed changes, in some cases, employers would need to inform the trustees as well as TPR.

Key takeaway

- When the new regime comes into force, certain corporate plans will need to be divulged at a much earlier stage, and potentially numerous times. This will lead to additional complexity, and is likely to have both timing and confidentiality implications. Compliance with the new requirements should therefore be added to the very beginning of any transaction plan and reviewed regularly. See our Hot Topic for more information.
- As they may come into force at short notice, DB employers should be ready to act swiftly when the final regulations are published.

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Contact

Sackers is the leading law firm for pension scheme employers, trustees and providers. Over 60 lawyers advise employers on all aspects of their pension arrangements. This includes getting automatic enrolment right, advising on corporate pensions strategy, managing DB risk and funding solutions, advice relating to DC schemes including transfers to DC master trusts, and advising on the pensions aspects of M&A activity and corporate group restructuring. For more information or to arrange training, please get in touch with David Saunders, Philippa Connaughton, Faith Dickson, Fuat Sami, Tom Jackman, Ferdy Lovett or Vicky Carr, or your usual Sackers contact.

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