Title: The Occupational Pension Schemes (Scheme Administration) Regulations 1996	Post Implementation Review
PIR No: DWP 001_2021	**Date:** 6 April 2021
Original IA/RPC No: DWP 0045	**Type of regulation:** **Domestic**
Lead department or agency: DWP	**Type of review:** Statutory
Other departments or agencies: The Pensions Regulator	**Date measure came into force:** 06/04/1997
	Recommendation Keep
Contact for enquiries: Mike Moore mike.moore@dwp.gov.uk	**RPC Opinion : N/A**

1. What were the policy objectives of the measure?

Background

In 2013 the Office of Fair Trading (OFT) carried out a study of Defined Contribution (DC) pensions and concluded that there were significant weaknesses that prevented competition working in the interests of consumers. Following publication of the OFT interim findings, the Government issued a call for evidence on the issue of scheme quality in summer 2013. This was followed in October 2013, by a public consultation, “Better workplace pensions: a consultation on charging”. This brought forward proposals to address the OFT’s concerns that competition alone could not be relied upon to ensure value for money for all savers through a range of charge controls, including a charge cap, and disclosure requirements.

The governance, charges and transparency were brought together in March 2014, in “Better Workplace Pensions: Further measures for savers”. In this publication the Government set out a range of measures to help ensure schemes are governed in members’ interests. This paper also consulted on proposals to introduce minimum governance standards across workplace pension schemes and announced the Government’s intention to bring forward a range of measures to improve transparency of all costs and charges in workplace schemes.

In October 2014 in “Better Workplace Pensions: Putting savers’ interests first” the Government confirmed its plans to introduce these new measures on governance and charges and consulted on draft regulations by which these measures would be implemented. The policy objective was to ensure that all individuals saving into DC workplace pensions get value for money.

The Explanatory Memorandum and Impact Assessment which accompanied the Regulations requiring this review (SI 2016 No.427) set out in detail the policy objectives which included the introduction of minimum governance standards to address buyer-side weakness in the market, to help to maintain trust in automatic enrolment and private pension savings and improve retirement outcomes for scheme members.

Legislation

Part V (governance of relevant schemes) of the Occupational Pension Schemes (Scheme Administration) Regulations 1996 was inserted into the 1996 Regulations by the Occupational Pension Schemes (Charges and Governance) Regulations 2015. The intention of the Regulations was to control the level and range of charges in pension schemes which are used by employers to meet their automatic enrolment measures and also to apply new governance measures across broadly all occupational pension schemes which offer money purchase benefits.

The regulations placed a duty on the scheme provider to appoint a chair of the trustees or, where the relevant scheme is not a trust scheme, a chair of the managers. Also, additional requirements to strengthen the independent oversight of schemes used by multiple employers (Master Trusts). These included Master Trusts being required to have a minimum of three trustees, of which two – including the chair of trustees – were independent of the scheme's providers. This addressed the OFT's concerns that some of these arrangements may have similar potential for conflicts of interest as contract-based schemes.

The subsequent introduction of The Occupational Pension Schemes (Master Trusts) Regulations 2018 means all Master Trusts have to be authorised and there is a requirement for them to provide evidence that they continue to meet the five authorisation criteria under a supervisory regime administered by the Pensions Regulator (TPR).

Part V makes it a requirement that, as part of their duties, the trustees or managers must prepare a statement – the Chair's statement, include it in the scheme's annual report and accounts within seven months of its the end of each scheme year and notify TPR of its completion.

Part V also set out what should be contained in the statement. This included information about: the scheme's default investment strategy and its governance; the processing of core financial transactions; member-borne transaction costs and charges; how the trustees have met trustee knowledge and understanding requirements; and the assessment of value for members.

TPR produced a supporting Code of Practice (13) and guidance (both of which have been updated to reflect additional requirements stemming from new legislation) setting out what they expected to be covered in the Chair's statement. The Code of Practice is not a statement of the law and there is no direct penalty for failing to comply with it.

Statutory requirement to carry out a review of the regulations

Regulation 8 of the Occupational Pension Schemes (Scheme Administration) (Amendment) Regulations 2016 requires the Secretary of State to carry out from time to time a review of Part V (governance of relevant schemes) of the Occupational Pension Schemes (Scheme Administration) Regulations 1996. The first report must be published within 5 years of the Amendment regulations coming into force which will be 6 April 2021.

There are no financial implications connected with this review or proposed changes to existing legislation.

References

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2. What evidence has informed the PIR?

The review took the form of sending a letter to pension providers / representative bodies and scheme members' representative organisations with a short list of questions framed around the legal requirements of the review. These focused on whether the policy objectives are being delivered through these provisions; whether those objectives remain appropriate and if they could be achieved through a system that imposed less regulation. This was followed up with targeted discussions with responders with a view to informing and developing the evidence base of this PIR.

All the regulations in Part V were looked at as part of the review. The review has been informed by policy delivery relating to other ongoing pensions work across the Department for Work and Pensions (DWP) which included the 2020 pensions charges survey / consultation which looked at the types and levels of charges across DC trust-based and contract based workplace pensions schemes, and the evolution of the Master Trust supervisory requirements.

29 organisations were contacted and 22 responses were received. Follow-up discussions took place with 13 of the responders. Discussions have also been conducted with TPR to inform the review.

3. To what extent have the policy objectives been achieved?

Each of the provisions of Part V of the 1996 Regulations have been considered as part of this review. Some of the ongoing work of the Department including work around value for scheme members and requirements placed on Master Trusts which has been covered above, helped in determining if the regulations continue to meet the policy objectives.

Interested parties did not raise issues relating to all the provisions of Part V prior to or during the course of this review. The focus within and across the pensions industry - professional advisor and scheme member representative communities - was on the provisions relating to the Chair's statement. Whilst all the provisions of Part V were looked at as part of the review the strong feeling around the purpose and effect of the Chair's statement was a very important issue.

We are grateful for the evidence provided by interested parties which has informed the findings presented in this PIR as far as possible. This has particularly informed our assessment of whether the policy is meeting its objectives and whether there have been any unintended consequences.

The review has established that the policy objectives are being achieved in relation to the vast majority of the provisions. There was consensus from responders for the need for minimum government standards. The review considered the content of the Impact Assessment "Minimum Governance Standards for DC Trust Based Schemes" which suggested a legislative approach. This proportionate legislative approach has ensured that minimum governance standards are being met. The status quo should be maintained with no changes required to the existing regulations - Part V of the 1996 regulations.

The review has identified, however, that the policy objectives in relation to the Chair's statement are not being achieved within the current approach. In particular, using a single instrument – the Chair's statement – to try to achieve multiple policy goals, in respect of scheme governance and member engagement does not work.

The purpose of the statement was intended to act as part of a suite of measures to deliver better scheme governance standards and this review has identified it should be re-focussed to deliver that goal. In addition, the Government will continue to work with TPR to continue to improve governance standards in DC trust based schemes and to address some of the common themes which emerged in the responses and in follow-up discussions with responders. These included:

Who is the intended audience for the Chair's statement?

Testing and discussions with interested parties including trustees and service providers' voices revealed that industry understanding of the purpose and intended audience of the Chair's statement was unclear. There are several reasons for this.

The statement required under Part V of the 1996 Regulations was to ensure schemes were well governed and met the provisions of those Regulations. The Chair's statement invited trustees and scheme managers to carefully consider how they are meeting their governance obligations. Also, subsequent legislation has required certain parts of the Chair's statement to be made publicly available which provides greater accountability and transparency.

Some responders felt that completion of the Chair's statement is a tick box exercise. This could be an unintended consequence of the legislation which has driven a rigid interpretation or TPR's focus on compliance due to the mandatory nature of the penalty.

In the 2014 Better Workplace Pensions Consultation it notes that:

'We think the requirement to annually produce a Chair's statement on how the minimum governance standards have been met will help ensure that trustees are considering the most important aspects of running their scheme. We will not however be overly prescriptive in regulations about how trustees complete the Chair's statement. The onus will instead be on trustees to consider and report on how best to assess their scheme, taking into account the particular needs of their members. This flexibility will help ensure that reporting helps to drive effective behaviours.'

The pensions industry was consulted in 2014 on proposals to introduce minimum governance standards across workplace pension schemes as part of a range of measures to improve transparency of all costs and charges in workplace schemes. The feedback received indicated, that industry is not clear as to whether the Chair's statement is intended to be a governance compliance document or aimed at providing transparency by providing certain information to scheme members. It is currently operating as a document intended for multiple audiences.

Some responders suggested the multiple purpose of the statement is a consequence of interpretation of requirements by TPR borne out in their Code of Practice and supporting guidance which makes it go beyond governance and to include member focus. However, trustees are only required to comply with the legislative requirements. The Code and supporting guidance are intended to be documents which trustees can use if they find helpful. It was suggested that in the experience of trustees, the statement was read primarily by TPR, industry experts, consultants and potentially other trustees. Very few scheme members look at it.

Most responders agreed that the Chair's statement is a necessary document because it has forced trustees to focus attention to governance of schemes. However, there was unanimous opinion that a multiple purpose approach cannot be contained in one document. It does not work as a communications tool for members and there is little evidence that members know it exists. The reasons are covered later on in this report.

Clarity was requested from the Government and TPR on the purpose of the Chair's statement. There was general support for it to provide transparency and demonstrate good governance of the relevant scheme. Providing scheme information to members should be through other sources.

In the follow up discussions with interested parties a request was made that if DWP requires trustees to provide a member communication it must first determine what it wishes trustees or scheme managers to tell members about, and why.

A suggested solution was to split the Chair's statement into two distinct areas – governance and the information required in compliance with legislation and a very short document containing information of relevance to scheme members.

The Chair's statement is far too long, complex and costly to produce

Given the multiple purpose of the Chair's statement this has brought significant challenges to scheme providers particularly around the amount of information required to ensure both purposes are fulfilled. Is its completion simply a tick box exercise? One responder felt the stress and cost of compiling a Chair's statement contributed to a perceived "governance burden" for DC single trust based schemes which could be fuelling mass movement to Master Trust arrangements.

Questions were raised about scheme members engaging with the statement. They, generally, do not engage with their pensions until drawdown. It is recognised in the pensions world that this is an issue which is difficult to address given personal choice on interaction with a pension.

There is general concern about compilation of the statement. Interpretation of current requirements means the documents are very long (in some instances approaching 100 pages), extremely technical, too prescriptive and complicated if the requirement is to:

- raise trustee governance standards;
- enable TPR to oversee trustee compliance with statutory governance requirements;
- communicate with scheme members about costs and value (primarily to meet the requirement to publish on line and direct scheme members to it);
- increase transparency with the wider pensions industry – as a consequence of publication requirements.

Some responders raised concerns about duplication of information particularly under a new world of authorisation and supervision of Master Trust pension schemes administered by TPR. This came into effect in October 2018. They felt there was some overlap with the information authorised Master Trusts are required to provide in the Supervisory return and much of the compliance-focused content of the Chair's statement. This is time consuming and costly.

A suggestion was made to shorten the Chair's statement by providing links to other relevant documents. This would come with both pros and cons. For example, the supporting information in the links could be more up to date to reflect different reporting periods. However, links get updated and a document with links may become outdated.

The cost of producing the Chair's statement was a common theme from responders. One responder said it was not unusual for Chair's statements to cost in the region of £15k - £20k to produce, once fees for data collation, drafting, legal review and auditors are factored in. For more complicated schemes, and for commercial Master Trusts, this cost can be significantly higher.

The basis of this issue related to TPR having to impose fines for non-compliant statements and being unable to use discretion (no available powers) in the decision making process. This has made compilation of the Chair's statement resource and cost intensive (consultancy and legal review fees, staff time spent by in house pension teams and trustees) to ensure mandatory penalties are avoided. This cost ultimately falls on the scheme members. The issue of fines is covered in more detail below.

<u>So what should be in the Chair's statement?</u>

Differing interpretations of compliance between TPR and industry specialists and the fact that non-compliance results in a mandatory penalty can contribute to over-engineered and unnecessary lengthy statements. Some responders felt TPR's Guidance and Code of Practice (13) was a contributory factor. They felt that the language was difficult to follow and these products did not provide the assurances trustees were seeking. They felt that a full review of the content of both documents may be helpful with a view to making them more user friendly and provide some of the assurances responders are seeking.

TPR have reviewed their Codes of Practice to reflect the Occupational Pension Schemes (Governance) (Amendment) Regulations 2018 and have combined the content of the 15 current Codes of Practice to form a single, shorter code which is currently out for consultation (the consultation went live on 17 March and closes on 26 May 2021). In the roundtable discussions stakeholders offered to work with TPR on their guidance to address the concerns raised in this review and this may provide the opportunity to do so.

Some responders questioned the amount of information required in a Chair's statement. One responder felt the governance standards should be reviewed to ensure they remain relevant to include, for example, cybercrime and equality, diversity and inclusion considerations.

A request was made for the Chair's statement to be simplified to provide a high level annual review in the introduction to the financial accounts with links to online collateral required in the current regulations (e.g. URL's to the value for money assessment, default Statement of Investment Principles, Costs and Charges Disclosure, Trustee non-affiliation and recruitment policy). This would enable these documents to be updated in real time and not to meet the current disclosure cycle. Is there a need to attach lots of illustrations? Instead, require the trustees to include an electronic link to the appropriate illustrative examples of costs and charges.

The DC Governance Group produced a free template which is hosted on the PLSA website. In recognition of this template David Fairs, TPR Executive Director of Regulatory Policy, Analysis and Advice, said: "*A Chair's statement is a basic requirement of good pensions governance and should be written clearly enough for members to understand and so I welcome any assistance provided to the trustees such as the PLSA's drafting template.*

"The template doesn't remove the need for trustees to carry out the fundamental analysis forming the foundation for a Chair's statement or consider how the statement requirements apply in the case of their scheme, but it should help in collating the information needed and help to present this clearly to savers."

There were differences of opinion on the need for a standard template which would probably be of more use to single employer providers. Some responders felt the template has been useful but does not address compliance issues - templates are helpful but do not constitute safe harbour and can be too prescriptive for certain schemes. A principle based approach would give greater flexibility. A change from mandatory fines to discretionary fines will also help to reassure trustees.

The Regulator imposing mandatory fines for non-compliance breaches

The role of TPR in ensuring the Chair's statement met compliance requirements and imposition of fines, in many cases for what responders considered minor non-compliance breaches, was raised by most of the responders and in response to many of the questions raised as part of this review.

TPR are required to apply a mandatory penalty where an annual Chair's statement has been prepared but it does not comply with all the regulatory requirements. They can decide to revoke the fine on review but only in exceptional or particularly compelling circumstances.

The clear message, in particular from pension providers, was to strongly advocate for TPR to have the power to use discretion about imposition of such fines. There was agreement from responders that fines should be imposed for significant or major failures to demonstrate good governance. However, most responders felt TPR have interpreted mandatory fines to mean they must be applied for any minor breach of what they interpret the Regulations to require. In informal discussions with TPR they highlighted that as the legislation stipulates a mandatory fine, they have no room for manoeuvre except in very exceptional circumstances. They would welcome the opportunity to review the legislation regarding the mandatory imposition of fines so that TPR could operate discretion.

The mandatory nature of the penalty has brought a number of concerns that fines are being imposed in a disproportionate way as it means a penalty must be imposed, even for minor breaches, can lead to reputational issues for scheme providers, particular if a fine is imposed, made public, and then rescinded. The reputational damage would have already been done

Also, has TPR's inability to use discretion when fining detracted from the purpose of the Chair's statement? It is being completed to avoid "minor" fines and at significant legal cost which could be passed onto scheme members. Indeed, different legal firms have different opinions on what constitutes compliance.

Imposing mandatory fines is not within the scope of this review as it is not derived from Part V of the 1996 Regulations but Part 4 of the Occupational Pension Scheme (Charges and Governance) Regulations 2015 (SI 2015/879). However, given the large number of concerns that were raised by industry representatives in this review about imposition of fines, this is something that DWP will look at with the aim of introducing a more risk-based approach to compliance / fines. We will do this at a time consistent with delivering on other priorities.

Conclusions

We are grateful to stakeholders for the time they have taken to provide input into this review. It is clear the Chair's statement is a subject on which responders hold strong views. Further work is required to address the concerns raised in this review whilst recognising some of the issues impact on other areas of ongoing work on pensions in DWP. The conclusions from the review are:

- **The Government and TPR should consider the audience and role the Chair's statement in relation to scheme governance and member communication**

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  It is clear that the current format the Chair's statement is not working as a document intended for multiple audiences – for the trustees to demonstrate good governance of a scheme whilst also serving as a provider of information to scheme members.

  Work is required between DWP and TPR to revisit this issue and to provide clarity to the pensions industry to remove collective confusion and ambiguity.

- **The information to be contained in the Chair's statement should be revisited**

  This will be determined once the intended audience of the statement has been clarified.

  There was agreement that the information that the Chair's statement seeks to capture should be set down. An area to explore is the balance between whether this should be in a single document which members have sight of or whether there is a need to divide the requirements into different documents. For example, this could be one for member facing and one to record the scheme's more regulatory activity.

We will consider whether the Chair’s statement should be used by trustees to disclose whether they have requested costs and charges information using the CTI templates, as part of our commitment from the review of the default fund charge cap and standardised costs disclosure, to drive up their use.

Further work will be required between DWP, TPR and industry representatives to ensure common agreement on content. This would enable the Chair’s statement to be shorter and more focused than the way it is implemented under current requirements.

Whilst not within the scope of this review, consideration should be given to the legislative requirement for TPR to issue mandatory fines in relation to the Chair’s statement and whether there should be an amendment to allow TPR to use discretion. Working proactively with scheme providers on shortfalls in the content of the Chair’s statement once received would align with how TPR works more generally with the pensions industry, for example on authorisation and supervision of Master Trusts.

Sign-off for Post Implementation Review: Minister for pensions and Financial Inclusion

I have read the PIR and I am satisfied that it represents a fair and proportionate assessment of the impact of the measure.

Signed: Date: 8/04/2021