EXPLANATORY MEMORANDUM TO

THE OCCUPATIONAL PENSION SCHEMES (INVESTMENT) (EMPLOYER-RELATED INVESTMENTS BY MASTER TRUSTS) (AMENDMENT) REGULATIONS 2022

2022 No. 827

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument amends regulations which restrict the extent to which occupational pension schemes can make certain investments with links to the employers who use the scheme, defined in the Pensions Act 1995[1] as "employer-related investments". The instrument will update the Occupational Pension Schemes (Investment) Regulations 2005[2] to reflect the current defined contribution (DC) Master Trust pension system following the introduction of automatic enrolment. The instrument relaxes the restrictions on employer-related investments for DC Master Trust pension schemes which are authorised by the Pensions Regulator and have 500 or more participating employers ("large Master Trusts"). This delivers the original policy intent of preventing malpractice at the top of the scheme's governance structure whilst removing outdated unnecessary restrictions which limit the ability of large Master Trusts to invest freely in best the interests of their members.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is Great Britain, save for regulations 1 and 5, where the territorial extent is the United Kingdom.

4.2 The territorial application of this instrument is Great Britain, save for regulations 1 and 5, where the territorial application is the United Kingdom.

4.3 It is anticipated that the Department for Communities will be making corresponding legislation for Northern Ireland, save in relation to regulation 5.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

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[1] Pensions Act 1995 (legislation.gov.uk)
[2] The Occupational Pension Schemes (Investment) Regulations 2005 (legislation.gov.uk)

6. Legislative Context

6.1 This instrument amends existing secondary legislation relating to employer-related investments by narrowing the scope of investments that come within the definition of employer-related investments for large Master Trusts.

6.2 Existing regulations are amended as follows:

- The Occupational Pension Schemes (Investment) Regulations 2005[3] ("the Investment Regulations") are amended so that the restrictions on employer-related investments by large Master Trusts only apply to investments relating to the scheme funder, the scheme strategist and persons connected to or associated with the scheme funder or the scheme strategist. The definitions of the different types of employer-related investments that will remain subject to restrictions for large Master Trusts closely follow the definitions already used to describe employer-related investments in section 40 of the Pensions Act 1995 and in regulation 11 of the Investment Regulations.
- The Occupational Pension Schemes (Requirement to Obtain Audited Accounts and a Statement from the Auditor) Regulations 1996[4] are amended so that the accounting requirements for large Master Trusts reflect the updated provisions on employer-related investments that apply in respect of those schemes.
- The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013[5] are amended so that the information that must be disclosed on request to members of large Master Trusts reflects the updated provisions on employer-related investments that apply in respect of those schemes.
- Consequential amendments are made to the Application of Pension Legislation to the National Employment Savings Trust Corporation Regulations 2010[6] to remove a provision which is no longer needed as a result of the changes made by this statutory instrument.

7. Policy background

What is being done and why?

7.1 In the 1990s, legislation was introduced to restrict the extent to which trustees of occupational pension schemes could make employer-related investments. This was to reduce the risk of an employer misappropriating the scheme's funds through loans and investments from the pension scheme to the employer or to companies associated with or connected to the employer.

7.2 This legislation was drafted based on the most common type of pension provision available at the time, single employer, defined benefit occupational pension schemes. The regulations were designed to address the further risk that a large portion of a scheme's assets could be invested in the single employer and/or in persons associated with or connected to that employer, such as subsidiaries, who might have influence

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[3] The Occupational Pension Schemes (Investment) Regulations 2005 (legislation.gov.uk)
[4] The Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 (legislation.gov.uk)
[5] The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (legislation.gov.uk)
[6] The Application of Pension Legislation to the National Employment Savings Trust Corporation Regulations 2010

over the investment approach of a pension scheme. Exercise of this influence in an inappropriate way could lead to a concentration of investment risk for pension scheme members which could ultimately result in them losing their pension savings.

7.3 The pensions landscape has evolved significantly since the introduction of the original regulations relating to employer-related investments. The intervening years have seen the success of automatic enrolment into workplace pension schemes, the closure of the majority of defined benefit pension schemes, with the consequent rise of defined contribution (DC) schemes and the emergence of the Master Trust market.

7.4 Master Trusts are authorised multi-employer occupational pension schemes that developed to respond to demand from employers to meet their legal obligation to automatically enrol their eligible employees into a workplace pension scheme. They provide a solution for employers who seek the advantages of a trust-based scheme without the cost and time of setting up and running their own arrangement. They must usually be authorised by the Pensions Regulator.

7.5 No changes have been made to the employer-related investment legislation to reflect the introduction of Master Trusts.

7.6 The impact of the current legislation means that Master Trusts must monitor each investment to ensure they do not breach the employer-related investment restrictions by investing in any of the participating employers using their scheme. This includes ensuring they are not investing in any companies associated with or connected to those participating employers. This can stretch into the tens or even hundreds of thousands of potential employers, associates and connected persons. Nest, the largest Master Trust currently has just under one million participating employers using their scheme.

7.7 DC Master Trusts must therefore spend time and pension savers money monitoring any changes to the governance, operations and ownership of companies that could relate to the scheme's participating employers against the underlying holdings of the scheme.

7.8 The impact of the cost of ensuring compliance makes it more difficult for schemes to invest in private markets where the information on investor/investee firm connections and associations is less easy to ascertain and subject to change. Maintaining a regulatory system that limits access to as full a range of assets as possible could put achievement of optimal retirement outcomes for savers at risk.

What did any law do before the changes to be made by this instrument?

7.9 The Pensions Act 1995 provides that trustees or managers of an occupational pension scheme must comply with any restrictions on employer-related investments that are set out in regulations. The detailed restrictions are set out in the Investment Regulations.

7.10 The restrictions at present are:

- A ban on most types of loans of a pension scheme's assets to an employer that participates in the pension scheme.
- A limit on trustees and managers investing more than 5% of a scheme's assets in employer-related investments.
- For multi-employer schemes, a limit on trustees and managers investing more than 5% of a scheme's assets in any one participating employer with a cap of

20% on the total amount of a scheme's assets that may be invested in employer-related investments.

7.11 The restrictions on employer-related investments extend to investments in 'associates' and 'connected persons' of any participating employer using the definitions set out in the Insolvency Act 1986[7].

7.12 Breach of the restrictions is a criminal offence and as such can potentially lead to a fine and/or imprisonment.

7.13 The Occupational Pension Schemes (Disclosure of Information) Regulations 2013 require trustees to provide a statement in their annual report, identifying any employer-related investments made in a scheme year.

7.14 In addition to the above, the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996 place a requirement on schemes to included details of any employer-related investments in their accounts.

7.15 The Application of Pension Legislation to the National Employment Savings Trust Corporation Regulations 2010 modifies the restrictions on employer-related investments applying to the National Employment Savings Trust (Nest).

Why is it being changed?

7.16 Changes are being made to update the Investment Regulations to reflect the current pensions landscape, in particular the development of the Master Trust market.

7.17 The current restrictions when applied to large Master Trusts go beyond the initial policy intent.

7.18 It is anticipated that the changes being introduced by this instrument will remove a regulatory burden from large Master Trusts and facilitate greater investment in private markets by large Master Trusts.

What will it now do?

7.19 This instrument will amend the employer-related restrictions that apply to large Master Trusts, so that the restrictions will only apply to investments in the scheme funder, the scheme strategist and any persons associated with or connected to the scheme funder or the scheme strategist. It will also update the disclosure and accounting requirements and the specific regulations applying to Nest, to reflect the new regime for large Master Trusts.

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 Informal consolidated text of instruments is available to the public free of charge via 'the National Archive' website legislation.gov.uk.

[7] Insolvency Act 1986 (legislation.gov.uk)

10. Consultation outcome

10.1 The government conducted a public consultation “Facilitating investments in illiquid assets”[8] between 30 March 2022 and 11 May 2022 on draft regulations to lift certain employer-related investment restrictions for large authorised defined contribution Master Trusts. 28 responses were received from a variety of stakeholders including pension scheme trustees and managers from defined contribution Master Trusts, pension scheme service providers, industry bodies and professionals and interested stakeholders. The majority of the responses were supportive and welcomed the proposed changes. A minority of the respondents suggested minor changes to the draft regulations and we have made amendments that we considered appropriate.

11. Guidance

11.1 These regulations are deregulatory for those Master Trusts in scope of these Amendment Regulations. Guidance is therefore unnecessary.

12. Impact

12.1 The impact on business, charities or voluntary bodies is principally on the pensions industry, specifically authorised Master Trusts (“multi-employer” defined contribution schemes) with 500 or more participating employers. Costs principally stem from requiring pension schemes in scope to familiarise themselves with the change in regulations. Pension schemes in scope will benefit from cost-savings from a reduction in administrative tasks and reporting requirements following the removal of some employer-related investment restrictions.

12.2 Equivalent annual net direct cost to business is estimated at £0.0 million over a 10-year period.

12.3 There is no, or no significant, impact on the public sector.

12.4 An Impact Assessment is submitted with this memorandum and published alongside the Explanatory Memorandum on the legislation.gov.uk website.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 The Department for Work and Pensions will work closely with its stakeholders, including industry bodies and employer organisations, to keep these regulations under review and should any issue arise with these policies, it will assess the evidence and if appropriate, consider whether any changes may be necessary.

14.2 Guy Opperman MP, Parliamentary Under-Secretary of State for the Department for Work and Pensions, has made the following statement under section 28(2)(b) of the small Business, Enterprise and Employment Act 2015.

14.3 “Having had regard to the Statutory Review Guidance for Departments published under section 31(3) of the Small Business, Enterprise and Employment Act 2015, in my view, it is not appropriate to make provision for review in the Occupational

[8] Facilitating investment in illiquid assets by defined contribution pension schemes - GOV.UK (www.gov.uk)

Pension Schemes (Investment) (Employer-related investments by Master Trusts) (Amendment) Regulations 2022.

15. Contact

15.1 Des Healy at the Department for Work and Pensions. Telephone: 07585882834 or email: des.healy@dwp.gov.uk can be contacted with any queries regarding the instrument.

15.2 Joanne Gibson, Deputy Director for Automatic Enrolment and Defined Contribution Pensions Policy, at the Department for Work and Pensions can confirm that this Explanatory Memorandum meets the required standard.

15.3 Minister for Pensions and Financial Inclusion (Parliamentary Under-Secretary of State), Guy Opperman MP at the Department for Work and Pensions can confirm that this Explanatory Memorandum meets the required standard.