Improving outcomes for members of defined contribution pension schemes

Government response to the February 2019 consultation 'Investment Innovation and Future Consolidation,' and further consultation on proposed measures to improve outcomes for Defined Contribution scheme members

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Contents

Contents

Introduction 6

About the Government response to the 'Investment Innovation and Future Consolidation' consultation 6

About this consultation on regulations and statutory guidance 6

Who this consultation is aimed at 6

Purpose of the consultation 6

Scope of consultation 7

Duration of the consultation 7

How to respond to this consultation 7

Government response 7

How we consult 8

Consultation principles 8

Feedback on the consultation process 8

Freedom of information 8

Ministerial Foreword 10

Chapter 1: Summary 12

Other related developments 12

Patient Capital and Authorised Funds 12

Updated Permitted Links Rules 13

Regulators' joint pensions strategy 13

Charge cap review 13

Chapter 2: Encouraging Consolidation 16

Background 16

Current position 16

February 2019 policy proposals 17

Overview of stakeholder responses 17

Stakeholder responses to detailed questions 18

Government Response 18

Proposed changes to regulations 27

Amendments to the Administration Regulations 27

Net Returns and Costs and Charges 28

Subsequent amendment to the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 28

Amendments to the Administration Regulations continued: 29

Administration and Governance 29

Amendments to the Register of Occupational and Personal Pension Schemes Regulations 2005 29

Chapter 3: Diversification, performance fees and the default fund charge cap 31

Background 31

Stakeholder responses 31

The use of performance fees in illiquid investments 31

Changes in the use of performance fees 32

Performance fees and the charge cap 32

Issues with the mechanism of charge cap compliance 33

Level of the charge cap 34

Other barriers to DC schemes paying performance fees 34

Other barriers to accessing illiquid investments 35

Proposed amendment to the charge cap compliance mechanism 36

Government response 38

Amendment to the charge cap compliance mechanism: an in-year adjustment to prorating performance fees 39

Further option for the charge cap compliance mechanism: creating a multi-year rolling calculation approach 40

Cost of holding physical assets 41

Non-exhaustive list of charges 43

Chapter 4: Using transparency as a prompt 44

Background 44

Stakeholder responses 44

Summary 44

Practical issues 44

Whether further measures are necessary 45

Undesirable consequences 46

Government response 47

Background ... 47
Definitions and reporting ... 47
Thresholds ... 48
Managing scheme liquidity and the illiquidity premium ... 48
Chapter 5. Updates to Statutory Guidance: Reporting costs, charges and other information ... 50
Background ... 50
Updates to the Statutory Guidance ... 50
Production of an Illustration ... 51
Publication of costs, charges and other information ... 51
Chapter 6: Other changes to legislation ... 54
Defaults with a "promise" and production of a default SIP ... 54
Background ... 54
Reporting costs and charges for funds which are no longer offered ... 56
Background ... 56
Wholly-insured Schemes ... 57
Annex A: List of respondents ... 59
Annex B: List of consultation questions ... 61
Annex C: Draft regulations ... 63
Annex D: Keeling schedules ... 70
Annex E: Statutory Guidance: Value for Money and Consolidation ... 87
Annex F: Non-exhaustive list of costs and charges ... 88
Annex G: Cost and charges statutory guidance ... 91
Background ... 95
About this Guidance ... 95
Expiry or review date ... 96
Audience ... 97
When this Guidance should be followed ... 98
Legal status of this Guidance ... 99
Compliance with this Guidance ... 99
Production of an illustration ... 100
Overview ... 100

Examples 101
Required elements 104
Savings pot size 104
Contributions 104
Real-terms investment return gross of costs and charges 105
Adjustment for the effect of costs and charges 106
Time 106
Optional elements 107
Publication of costs, charges and other information 108
Required elements 108
Presenting the information 108
Finding and accessing the information 110
Needs of disabled people 110
Storage or printing of the information 112
Optional elements 112

Introduction

This document contains the Government's response to the February 2019 consultation 'Investment Innovation and Future Consolidation.'

It also consults on further proposed measures aimed at improving outcomes for members of Defined Contribution (DC) pension schemes.

About the Government response to the 'Investment Innovation and Future Consolidation' consultation

We received around sixty detailed responses from a wide range of stakeholders. The views shared with us are outlined in the appropriate chapters of this document. We have continued to hold in depth and frank discussions on the broader issues and these together have resulted in the proposals set out in this document.

Our proposals include draft regulations and statutory guidance which seek to address key issues raised in the February 2019 consultation. This document therefore also serves as a consultation on those draft regulations and statutory guidance.

About this consultation on regulations and statutory guidance

Who this consultation is aimed at

- pension scheme trustees and managers;
- pension scheme members and beneficiaries;
- pension scheme service providers, other industry bodies and professionals;
- civil society organisations; and
- any other interested stakeholders

Purpose of the consultation

This consultation seeks views on proposed regulatory amendments and the extent to which these achieve their stated policy intent. It also seeks views on new statutory guidance on how to assess value for members and updates to existing statutory guidance on presenting cost and charges information and ways in which they could potentially be improved further. This consultation also seeks views on the development of an optional further easement to facilitate investment by DC schemes in illiquid assets such as venture capital.

Scope of consultation

This consultation applies to England, Wales and Scotland

It is envisaged that Northern Ireland will make corresponding regulations.

Duration of the consultation

The consultation period begins on 07 September 2020 and runs until 30 October 2020.

How to respond to this consultation

Please complete the online questionnaire which accompanies this consultation.

Alternatively, if you wish to submit information which cannot be provided via a web form, please send your consultation responses to :

E-Mail : pensions.investment@dwp.gov.uk

Electronic responses are preferred unless there is a clear reason not to do so. In that instance please send your responses to:

David Eaton

Department for Work and Pensions

DC Policy Team, Policy Group

Private Pensions and Arms Lengths Bodies Directorate

Zone A, 3rd Floor South

Quarry House

Quarry Hill

Leeds

LS2 7UA

Note: When responding please indicate whether you are responding as an individual or representing the views of an organisation

Government response

We will aim to publish the Government response to the consultation on the GOV.UK website. Where a consultation is linked to a Statutory Instrument, responses should be published before or at the same time as the Instrument is laid.

The report will summarise the responses.

How we consult

Consultation principles

This consultation is being conducted in line with the revised Cabinet Office consultation principles published in January 2016. These principles give clear guidance to government departments on conducting consultations.

Feedback on the consultation process

We value your feedback on how well we consult. If you have any comments about the consultation process (as opposed to comments about the issues which are the subject of the consultation), please email them to the DWP Consultation Coordinator. These could include if you feel that the consultation does not adhere to the values expressed in the consultation principles or that the process could be improved.

DWP Consultation Coordinator
2nd Floor
Caxton House
Tothill Street
London
SW1H 9NA

Email: caxtonhouse.legislation@dwp.gsi.gov.uk

Freedom of information

The information you send us may need to be passed to colleagues within the Department for Work and Pensions, published in a summary of responses received and referred to in the published consultation report.

All information contained in your response, including personal information, may be subject to publication or disclosure if requested under the Freedom of Information Act 2000. By providing personal information for the purposes of the public consultation exercise, it is understood that you consent to its disclosure and publication. If this is not the case, you should limit any personal information provided, or remove it completely. If you want the information in your response to the consultation to be kept confidential, you should explain why as part of your response, although we cannot guarantee to do this.

To find out more about the general principles of Freedom of Information and how it is applied within DWP, please contact the Central Freedom of Information Team:
Email: freedom-of-information-request@dwp.gsi.gov.uk

The Central Freedom of Information team cannot advise on specific consultation exercises, only on Freedom of Information issues. Read more information about the Freedom of Information Act.

Ministerial Foreword

The government has an aspiration that all DC scheme members should benefit from efficient and operationally resilient administration, first class investment governance, and access to innovative and diversified investment strategies. I want all scheme members to benefit from a broader range of assets to improve the returns they achieve, and to drive new investment in important sectors of the economy.

The UK has a world-class occupational pension system and the market is continuing to consolidate and to innovate in the interests of scheme members. But, there remain large numbers of smaller DC schemes many of which are poorly governed, have on average higher charges and do not have the scale to bring the benefits of investing across a broad range of asset classes.

I am determined to do more to ensure the Trustees of smaller schemes act in the best interests of their members. I am therefore bringing forward measures that will ensure that we tackle persistent underperformance and poor governance by accelerating the pace with which the market is consolidating. This will bring the benefits of scale to all scheme members including a greater capacity to take advantage of illiquid and other alternative investment classes.

The measures I am bringing forward in these draft regulations and statutory guidance clarify and strengthen what trustees must consider when assessing the value for members their scheme delivers. Schemes with total assets of less than £100M are required to assess the value they offer their members in a more holistic way.

Small schemes that are well run and offer superior benefits, as well as the larger schemes under this threshold that are performing well, are likely to be able to demonstrate they offer value in the way we set out. Where smaller schemes are not able to demonstrate value for members, Government's expectation is that they consolidate into a larger scale scheme that is able to provide better outcomes for those members.

Trustees' fiduciary duties require them to take account of all long term financially material considerations when deciding their investment policy. It remains Government policy not to direct the trustees of private trusts to invest in a particular way. As part of that, it is also Government's policy to ensure it is not putting up unnecessary or inadvertent obstacles to trustee decisions where these would limit trustees' ability to take full advantage of the broad range of asset classes available to them.

I am aspirational about ensuring schemes are able to invest in a broad range of assets such as technological, social and environmental infrastructure, and welcome the continued growth of investment in these assets by pension schemes. The

government could not be clearer in its support for pension funds investing in such products as part of a balanced portfolio. We thank all those who contributed to the consultation, and who have shaped the debate on these issues.

I set out measures to address issues raised with us in relation to illiquid investments such as venture capital and the charge cap on the default fund. I am enabling schemes to smooth the calculation of performance fees in year, which will remove potential barriers to these illiquid investments while ensuring members remain protected. I also announce my intention to create a further, multi-year smoothing option for the calculation of performance fees to facilitate access to less liquid assets such as venture capital. I am placing the fixed costs of investments on a statutory footing and have clarified issues around the definition of administration charges in the forthcoming Pension Schemes Bill.

These measures, together with the recent amendment to the Financial Conduct Authority's rules[1] on permitted link funds, seek to address any unjustified potential regulatory barriers to investment in some less liquid assets.

I believe the proposals set out will facilitate necessary consolidation within the market and enable trustees to take a long term approach to providing resilient and sustainable products for savers' retirement income, as well as the range of investments and strategies they can access to deliver that. In this way, members can be confident of achieving better outcomes from their DC pension scheme investments and their engagement in the wider UK economy, and greater benefit to the UK itself.

Guy Opperman MP

Minister for Pensions and Financial Inclusion

[1] https://www.fca.org.uk/publications/policy-statements/ps20-4-amendment-cobs-21-3-permitted-link-rules

Chapter 1: Summary

1. This document is the Government's response to the February 2019 consultation 'Investment Innovation and Future Consolidation'. It also consults further on changes to regulations and statutory guidance designed to improve DC pension scheme governance, promote the diversification of investment portfolios and signal our commitment to transparent disclosure to scheme members.
2. We address stakeholder responses to the consultation proposal to use increased transparency as a vehicle to further encourage larger schemes to broaden their investments into a range of different asset classes.
3. We address stakeholder feedback on the role the measurement of performance fees and the charge cap might play in limiting the ability of schemes used for Automatic Enrolment default funds to access less liquid investment classes such as venture capital for their members. We consult on a proposed legislative change to the way compliance with the charge cap is measured for performance fees to give trustees greater flexibility in these investment decisions, and we invite views on a proposal to further extend this flexibility with an alternative approach to measurement.
4. We consult on changes to legislation and some new statutory guidance to support and accelerate the process of consolidation in the DC market, and to extend access to a more diverse range of investment classes. Trustees of smaller schemes will be required to assess key elements of the value achieved by their scheme and to report on the outcome of that assessment. Where this assessment shows that members would achieve better value in a larger scheme they are expected to initiate wind up and consolidate.
5. We also consult on other changes to legislation and statutory guidance to improve DC pension scheme member outcomes in response to the February 2019 consultation, and these are set out in more detail in the following pages.

Other related developments

Patient Capital and Authorised Funds

6. The Financial Conduct Authority (FCA) maintained prescriptive diversification rules for retail funds in their Feedback Statement (FS20/2) on Patient Capital and Authorised Funds published in February 2020[2]. They reiterated the need for such rules to prevent concentration of investment in a narrow range of asset classes,

[2] Patient Capital and Authorised Funds - Feedback on DP18/10

and thus prevent exposure to the increased investment risks of such an approach.

7. Funds structured as Qualified Investor Schemes, however, allow for investments in a wider range of longer term assets, without the same diversification limits as imposed by other retail fund structures, allowing investors to diversify their portfolios when required. The feedback on professional and sophisticated retail investor access to long-term assets through Qualified Investor Schemes found that they are suitable for investment in long-term assets.

Updated Permitted Links Rules

8. The FCA outlined their amendment of COBS 21.3 permitted links rules in a consultation response[3] in March 2020. The new rules seek to address any unjustified barriers to retail investors investing in a broader range of assets including long-term investments.

9. We are encouraged to see that the FCA's final set of measures facilitates diversification of portfolios by removing some of the restrictions on investments in illiquid assets, while still preserving a sufficient level of protection for members. This change has the potential to deliver diversified returns to savers while facilitating investment in key assets such as housing, infrastructure, environmental protection and growth companies that lift the whole economy.

Regulators' joint pensions strategy

10. The FCA and The Pensions Regulator (TPR) continue to develop their joint pensions strategy, first outlined in October 2018[4]. The focus for the next five to ten years is on determining how to most effectively support different cohorts of scheme members to optimise their retirement savings. This support will involve setting and enforcing clear standards and using a range of regulatory interventions to improve value for money for members.

Charge cap review

11. We are reviewing the scope and operation of the charge cap for Automatic Enrolment default funds and will report towards the end of 2020. The review draws on stakeholder discussions about the operation of the cap as the DC market matures with the aim of ensuring continued financial sustainability for schemes, ensuring trustees are encouraged and enabled to invest in a wide range of assets, including illiquids, while maintaining clear and transparent protection for savers. A call for evidence on specific elements of the charge cap has recently closed and we are analysing the responses together with the data gathered in the 2020 Pension Charges Survey.

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[3] FCA Amendment of COBS 21.3 permitted link rules - final rules and feedback to CP18/40

[4] FCA and TPR joint strategy, October 2018 - https://www.thepensionsregulator.gov.uk/en/about-us/how-we-regulate-and-enforce/fca-and-tpr-joint-strategy

List of proposals within this document

Consolidation

Proposed amendments to The Occupational Pension Schemes (Scheme Administration) Regulations 1996 ("the Administration Regulations 1996"), Register of Occupational and Personal Pension Schemes Regulations 2005 and The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 would:

- Require all relevant schemes to report on the return on investments of default and member selected funds.
- Require schemes with assets below £100m to report on how their scheme presents value for members taking into account costs and charges, investment returns and various elements of governance and administration.
- Require schemes with assets below £100m that do not present value for members to report this outcome in their scheme return.
- Require all relevant schemes to report to the regulator the total amount of assets held in the scheme in the annual scheme return.

We propose to bring these amendments into force on 05 October 2021.

Diversification, performance fees and the default fund charge cap

- Amendment to The Occupational Pension Schemes (Charges and Governance) Regulations 2015 ("Charges and Governance Regulations 2015") to better enable schemes to pay performance fees.
- An additional amendment to the Charges and Governance Regulations 2015 to exclude costs of holding 'physical assets'.
- Update to charge cap guidance to clarify treatment of underlying costs in investment trusts.

We propose to bring these amendments into force on 05 October 2021.

Other changes to legislation

- Amendment to The Occupational Pension Schemes (Investment) Regulations 2005 ("the Investment Regulations 2005") to extend the requirement to produce a default Statement of Investment Principles to 'with profits' schemes.
- Amendment to the Administration Regulations 1996 to extend the costs disclosure requirements to funds which are no longer available for members to choose.
- Amendments to the Investment Regulations 2005 to exclude wholly insured schemes from some requirements of the Statement of Investment Principles.

We propose to bring these amendments into force 05 October 2021.

Updated reporting of costs, charges and other information: statutory guidance

- Amendments to the statutory guidance that supports The Occupational Pension Schemes (Administration and Disclosure) Regulations 2018. The amendments provide additional clarity on how costs and charges information should be set out.
- No changes are proposed to the regulations themselves.

Chapter 2: Encouraging Consolidation

Background

1. Chapter 3[5] of the February 2019 consultation made the case for a more consolidated defined contribution (DC) pensions market. We believe consolidation is the most effective way to ensure that all savers are receiving the best value from well governed schemes that can achieve economies of scale. Consolidation will also deliver greater opportunities for members to access a more diverse range of investment products and investment strategies to the benefit of both the pension saver and the broader UK economy.

2. The consultation considered measures to accelerate the existing rate of consolidation and sought feedback on those suggestions. This chapter summarises the responses we received and sets out our proposal to accelerate consolidation and improve both governance and access to a wider range of asset classes, including illiquids.

Current position

3. The market is continuing to consolidate, with a 12% fall in scheme numbers[6] in the past year. Employer switching is expected to continue at a rate of between 5 and 10% each year.[7] However, schemes at the smaller end of the market are consolidating more slowly, and it is these schemes that are the focus of our proposals.

4. Of around 3000 DC schemes[8] on the Pensions Regulator's (TPR) register, approximately 2150 have 100 members or less. Of these, approximately 850 have between 12 and 100 members and 1300 have less than 12 members.

5. In 2019, around 60% of schemes with less than 100 members did not meet any of the 5 Key Governance Requirements (KGRs) set by TPR.[9] Most smaller schemes are also paying higher charges than larger schemes, with average

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[5] Paragraphs 20-36
[6] The Pensions Regulator. DC Trust – presentation of scheme return data 2019-20
[7] Corporate Adviser. Workplace Savings Report. November 2019
[8] Excluding schemes commonly referred to as small self-administered schemes (SSAS) where the members are themselves trustees and executive pension schemes
[9] The Pensions Regulator Defined Contribution trust-based pension schemes research survey 2019 https://www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/dc-research-summary-report-2019.ashx

charges in smaller schemes nearly double that of the largest schemes.[10] Members of some of these smaller schemes are therefore likely to achieve better value in a larger scheme, and our February 2019 consultation explored ways in which this might most effectively be achieved within the market.

February 2019 policy proposals

6. In the *Investment Innovation and Future Consolidation* consultation we set out proposals intended to encourage and support those trustees who had not previously considered consolidation to now explore it as a course of action.

7. We proposed extending the scope of the current 'value for members' assessment in the Chair's Statement for smaller DC schemes. This revised and more holistic assessment would ask trustees of those smaller schemes to declare whether their scheme was achieving sufficient value for money for savers' retirement income, or whether it might be in scheme members' interests to move to a larger scheme or an authorised master trust.

8. We sought opinion on the size of schemes that should come into scope for this new assessment, how frequently it should be carried out, and the factors that should be considered as part of that assessment. We also asked for views on the appropriate reporting vehicle.

Overview of stakeholder responses

9. We received a total of 56 responses from a mix of organisations across the industry. A full list can be found at Annex A.

10. The proposals were broadly well received by the majority of respondents; only 8 were sceptical or cautious and 5 opposed. The majority of respondents agreed that an extended value for members assessment in the chair's statement would be a good way to get trustees to consider whether scheme members' interests would be better served by consolidating. There were caveats to their support, including that the requirements should not take effect immediately.

11. Respondents agreed that benefits of consolidation for scheme members included being part of a better governed scheme and having access to a more diverse range of investment opportunities, and in some cases to more competitive charges.

[10] Average annual charges for qualifying trust-based schemes broken down by number of members. 0.61% for schemes with 12-99 members and 0.37% - 0.44% for schemes with at least 1000 members. DWP Pension Charges Survey 2016, October 2017, https://www.gov.uk/government/publications/pension-charges-survey-2016-charges-in-defined-contribution-pension-schemes

Stakeholder responses to detailed questions

12. Some stakeholders felt that encouraging consolidation should wait until the master trust authorisation process had completed so that smaller schemes would have a well-established market to choose from.

13. Of those in support of the proposal, a few felt that consolidation should be for the purpose of increasing value for members only, and perceived the argument for access to illiquid investments as being less strong.

14. The most common reason given by those who were less enthusiastic about focusing on consolidation was that not all small schemes are badly run and therefore consolidation should not be an automatic requirement. For those that are badly run, effort should instead be focused on improving their standards of governance.

15. One respondent did not believe that it was within the remit of trustees to consider whether scheme members would be better off transferring elsewhere. It would be up to the employer to consider this option.

16. A couple of respondents raised concerns about the cost of wind up. A small number of others felt consideration of consolidation would not be an appropriate use of the trustee board's time and governance efforts.

Government Response

17. We were encouraged by the overall level of support for our proposals to encourage consolidation. We agree with the majority view on timing in relation to the master trust authorisation process and believe, now that process is complete and the supervision regime is a year into operation, that it is the right time to consult further on these proposals.

18. We acknowledge that not all small schemes are badly run and that many trustees of smaller schemes work diligently, often on a voluntary basis, to protect the interests of scheme members. There are also particular classes of smaller bespoke schemes that are highly regarded and offer valuable benefits. Schemes that are delivering value to their members will be able to demonstrate this under the proposed new assessment.

19. We are also aware that many smaller schemes struggle to achieve economies of scale and to access the services and investment strategies offered to the larger end of the market. Data from TPR [11] on the degree to which schemes are meeting Key Governance Requirements also shows that a majority of smaller schemes are struggling to govern effectively. All savers should enjoy the

[11] https://www.thepensionsregulator.gov.uk/-/media/thepensionsregulator/files/import/pdf/dc-research-summary-report-2019.ashx

benefits of well-run schemes that can deliver high standards of governance, efficient and effective charging structures and diverse investment strategies.

20. We do not agree that it is not within the remit of trustees to determine whether scheme members' interests would be better served by winding up and consolidating. Trustees would, in consultation with the employer, be expected to make a decision to consolidate where their own assessment shows that their scheme is unable to effectively deliver value for money. TPR also has the power to wind up a pension scheme in certain circumstances, including if to do so would be in the interests of the generality of members.

21. We therefore propose that where smaller schemes do not demonstrate value for members under the new assessment, trustees should take immediate steps to wind up the scheme and consolidate members into a larger scheme, unless in exceptional circumstances they can improve both rapidly and cost effectively. We set out which smaller schemes this proposal would apply to in the section on Scope, below.

22. We accept that some poorly performing schemes that fail to meet the standards under the new assessment may be able to improve sufficiently without needing to consolidate. We would expect, however, that such schemes would make these improvements before their assessment falls due.

23. Trustees of schemes that do fail to demonstrate value for money under the new assessment should weigh up the time, skills, capacity and costs of making sufficient improvements. They should be confident that they can raise standards to meet and continue to meet the ongoing demands of managing savers' money over the long term. We believe that wind up and consolidation into a larger, better value scheme is still likely to be the best option for members.

24. Only in exceptional instances where trustees have solid reason to believe that they can make all required improvements cost-effectively and efficiently, despite having failed to demonstrate this at assessment, would we expect trustees to seek to improve rather than to initiate wind up. Schemes that attempt to improve are expected to achieve these improvements within a reasonable period of time, and if they do not, they should take action to wind up and consolidate without further delay to prevent continued detriment to scheme members.

25. It is not acceptable for savers to be enrolled in arrangements that do not deliver value in terms of costs, investment returns or secure and resilient governance. Government would expect trustees acting in the best interests of their members to take appropriate action to wind up and consolidate without TPR needing to exercise its powers.

26. TPR has the power to order schemes to wind up if it is in the best interests of the generality of scheme members to do so. TPR also has the power in certain circumstances to remove or appoint trustees, and to order trustees or third parties that are causing breaches of pensions legislation to make specific improvements to be made within a certain period of time.

27. We do not propose that the costs of winding up the scheme would be a factor to consider when completing the value for members assessment as it is not a metric that impacts the value achieved by the scheme while it is in operation. These costs do of course need to be taken into account once trustees are considering consolidation. Trustees will also need to consider the role of the employer in winding up and selecting a new scheme, as well as the costs associated with the wind up process, including any exit charges, and whether there are any existing guarantees that might be lost.

Summary

It is proposed that these regulations will come into force on 5 October 2021.

If the trustees of a smaller scheme consider that the scheme is not delivering good overall value following its value for members assessment, Government expects trustees to wind up the scheme and consolidate.

In circumstances where trustees are realistically confident that required improvements can be made, and/or where the wind up and exit costs may exceed the costs of making such improvements, and/or where there are valuable guarantees that would be lost on consolidation, the scheme may seek to improve. If the trustees fail in this attempt to improve they will be expected to wind up the scheme and consolidate the members into a scheme that offers better value.

Trustees must report their proposed approach to TPR. TPR has the power to issue an order to wind up the scheme, to remove trustees in certain circumstances, or to appoint new trustees to properly manage the scheme's assets.

Scope

28. In the consultation we suggested that these proposals should apply to schemes with fewer than 1000 members, or with less than £10m in money purchase benefit assets. The majority who responded to this question felt that the total amount of assets should be used as a threshold rather than number of members.

29. The majority of respondents agreed with our suggested £10M threshold, although there were some suggestions that the threshold should be higher, to include poor value larger schemes, or lower to help ensure well run smaller schemes could continue to operate. One respondent felt that that there should be no size requirement and that all schemes that are less well governed should improve or consolidate.

30. Some respondents felt that schemes established within the last three years should be allowed to grow and should therefore be exempt from these requirements.

Government Response

31. We note the majority agreement with our suggestion of a threshold for schemes with assets of less than £10M. We also note that the picture for schemes with

assets above £10M is more mixed, but that schemes of a slightly larger scale do still experience difficulties with governance, operational resilience, or with accessing economies of scale and a diverse mix of assets. We are therefore consulting on regulations that set a threshold of £100m to complete the new and more holistic value for members assessment, having regard to new statutory guidance. A draft of this guidance is attached at annex E.

32. We believe that setting the threshold at this level will encourage further economies of scale and lead to more diverse investments, including illiquid assets.

33. We acknowledge that new schemes take time to establish and grow. We agree that schemes that have been in operation for less than three years at the time that the assessment falls due should be exempt from the new requirements.

34. Achieving value for members is important for all occupational pension schemes, regardless of their size or duration. All schemes that fall outside the scope of the draft regulations must still assess value for members in relation to their charges and transaction costs under the existing regulations as explained in TPR's Code and Guidance.[12] [13] They may also choose to have regard to the new assessment, if they wish to do so.

Summary

Scope: We propose that the new value for members assessment applies for schemes with less than £100m in total assets that have been operating for at least 3 years at the end of the previous scheme year from when their chair's statement falls due.

Metrics to assess value for members

35. We suggested that charges, investment performance and governance and administration should be included when assessing value for members, and we sought views on whether there should be a reference scheme for comparison.

36. The majority of respondents thought that all of these suggested factors should be considered in the value for members assessment. Some respondents stated that costs should not be considered on their own but assessed in relation to the returns obtained - a small scheme with high costs could still produce high returns and therefore deliver value for its members.

37. One respondent indicated that exit penalties and existing guarantees should also be considered, while a small number of respondents expressed the view that

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[12] http://www.legislation.gov.uk/uksi/1996/1715/regulation/23

[13] https://www.thepensionsregulator.gov.uk/en/trustees/managing-dc-benefits/5-value-for-members#1e5967776f854875b6cb77349846e2e8

factors such as the level of member engagement and the quality and frequency of communication with scheme members should also be considered because this impacts members' decumulation decisions.

38. Other factors raised included the level of employer support, fund switch capability, fund range and flexibility at retirement, and trustee knowledge and understanding. Two respondents were concerned that any form of prescriptive reporting would place additional resource burdens on schemes, and one argued that administration and governance factors are too subjective to compare easily.

39. There was little support for the idea of having a single reference scheme as a comparator. One respondent commented that this would have to be reviewed or updated regularly and another that only an automatic enrolment master trust with a "one size fits all" proposition would be appropriate.

40. Some respondents suggested that a couple of market based reference schemes could be used, and there was a preference for comparing against what is available in the market rather than against a model scheme.

41. Many respondents raised the need for additional guidance for trustees in completing the assessment.

Government Response

42. We agree that while costs and charges have a significant impact on member outcomes they are best understood in the broader context of what the scheme delivers. The net returns received is a crucial factor in measuring value for members. Therefore, alongside information about costs and charges, we propose that trustees also consider the level of net investment returns as part of the assessment, for various age cohorts where applicable.

43. We are consulting on regulations that will require **all** relevant[14] schemes, regardless of size, to publish net returns for their default and self-selected funds. This will not only assist with completing the Value for Members assessment but will also provide greater transparency to members. Draft regulations are at Annex C and draft revisions to the statutory guidance on the reporting of costs and charges is at Annex G.

Summary

We propose that in order to provide greater transparency to members **all** relevant schemes, regardless of size, must publish net returns for their default and self-selected funds in the annual chair's statement. We welcome your

[14] http://www.legislation.gov.uk/uksi/1996/1715/regulation/1

views on how this information might be most usefully calculated and reported on in question Q1 below.

44. We agree that a single reference or model scheme should not be used. We propose that smaller schemes should compare themselves to at least three other larger schemes in the market. Of the three schemes, trustees should have reason to believe that at least one of them would accept the smaller scheme should it decide to wind up and consolidate

45. We propose producing statutory guidance in response to the view that trustees would benefit from additional support to in carrying out their value for member assessment. A draft of this guidance is available for review at Annex E.

46. The quality of scheme governance and administration is a significant part of a schemes' overall value proposition. We propose that our statutory guidance include a breakdown of what we expect trustees should consider when looking at the quality of the administration and governance of a scheme. These criteria are:

- quality of record keeping,
- promptness and accuracy of core financial transactions,
- quality of communication with members,
- appropriateness of the default investment strategy and
- the quality of investment governance.

47. We also propose that trustees consider their skills, knowledge and understanding, and the effectiveness of their conflict of interest management. Smaller schemes will not be expected to use any external comparator for this element of their value for money assessment. Instead, we propose that they assess the value offered by their administration and governance on an absolute basis. In conducting this assessment, trustees should have regard to TPR's education, guidance and Codes of Practice on this subject as set out in its 21st Century Trusteeship initiative[15], and to the additional statutory guidance we propose to publish.

48. Where an employer subsidises the running costs of the scheme, as is often the case with administration charges, we suggest that this will need to be taken into consideration when assessing value.

49. We agree that the benefits of existing guarantees should also be considered when making the overall holistic assessment of whether a small scheme provides value for members.

50. We have not proposed scheme member engagement as a specific measure of the value offered by a scheme. We have proposed member communication, as it is important that members have clear, accurate and timely information made available when they need to make decisions about their savings. We have also

[15] https://www.thepensionsregulator.gov.uk/en/trustees/21st-century-trusteeship

not proposed fund switch capability, fund range or flexibility at retirement as being main factors to consider in the assessment.

51. We do not envisage that consideration and reporting of the above factors is likely to significantly impact on trustee time, resources or scheme costs. These are matters that should be considered by trustees throughout the scheme year and should therefore be easily accessible. If trustees struggle to consider and report on such elements, this in itself should prompt them to consider the extent to which they feel they are able to effectively govern the scheme while still delivering value.

Summary

The proposed factors to be assessed are:

- Costs/Charges
- Net investment returns, and
- Measures of administration and governance which include:
    - promptness and accuracy of financial transactions,
    - appropriateness of default investment strategy
    - quality of investment governance,
    - quality of record keeping,
    - quality of communication with members
    - level of trustee knowledge, understanding and skills to run the scheme effectively and
    - effectiveness of management of conflict of interest

Costs, charges and net returns would be assessed relative to those of at least 3 other schemes while factors of administration and governance would be assessed absolutely within the scheme.

52. We also sought views on an appropriate reporting vehicle and suggested the reporting requirement be added to the value for members assessment which forms part of the DC chair's statement. All respondents felt that the DC chair's statement was a suitable vehicle for reporting on the more detailed value for members assessment. One indicated that it would be suitable provided that it did not make the chair's statement long and burdensome.

53. One respondent went further to say that the assessment should be evidenced while another said there needed to be mandatory reporting to TPR and an action plan submitted where appropriate.

Government Response

54. The proposals are an extension of the existing mandatory requirements to assess and report on value for members in relation to charges and transaction costs in the chair's statement. The government would expect trustees to fully explain in the statement what they have done to demonstrate the value they deliver and how they have reached their conclusion on the outcome of the assessment.

55. We propose that schemes will be required to report the overall outcome of the assessment to TPR via the scheme return and indicate how they will proceed, should the scheme not provide good value for members. TPR will use its regulatory powers where necessary, including its power to wind up a pension scheme where to do so is in the interest of the generality of its members.

Summary

We propose that schemes in scope will complete the prescribed value for members assessment annually and report on it as part of their DC chair's statement. Trustees must also report to TPR, in their next annual scheme return, the outcome of the assessment and what intended action they will take, or have already started to take, in the event that the scheme does not present good value for members.

56. We asked for views on the appropriate frequency of the value for members assessment, suggesting at least every three years and after any significant change in size or demographic profile.

57. Of those who responded to this question, a majority agreed that a triennial basis was appropriate. A few respondents suggested reporting could be made more frequent during periods of change within the scheme. Others suggested triennial reporting was not frequent enough and that the assessment should be done annually or on alternate years.

58. One respondent thought that every 5 years was more appropriate, and another that the date of reviews should be staggered to ensure schemes have access to quality advice.

Government Response

59. We believe it would be appropriate for the assessment to be carried out annually, as part of the annual chair's statement. We do not believe this to be disproportionate as the factors to be assessed are those that trustees should be reviewing throughout the year.

60. We understand concerns about access to quality advice but are not convinced that it is necessary to stagger reporting. We do not propose to compel schemes to increase the frequency of assessment following changes within the scheme, such as to the demographic profile

Summary

We propose that the new value for members assessment will be conducted annually by the schemes in scope.

61. Finally, we asked what other indicators should be looked at to encourage schemes to consider consolidation. We suggested that trustee knowledge and understanding, open or closed status and member demographics may be appropriate.

62. For those who responded on trustee knowledge and understanding, while the majority considered it to be an important factor for any scheme, the responses as to whether it should be included as a measure were mixed. A narrow majority believed that it should be included. Comments included the difficulty of measurement and enforcement, and that assessment was very subjective.

63. One respondent who supported it as a measure commented that lack of trustee knowledge of investment may be limiting the quality of investment and decumulation choices made by members and that this was important to capture.

64. One respondent who felt that it should not be included commented that trustee knowledge and understanding should be enforced more rigorously by TPR, and that if TPR has concerns the scheme should be forced to consolidate. Another suggested TPR insist that schemes only recruit suitably qualified trustees.

65. Responses were evenly split as to whether it would be useful to take the open/closed status of a scheme into consideration. Some thought that this was irrelevant, with one commenting that some closed schemes were well run. Others believed that it made sense to consolidate closed schemes. One suggested that consolidation would be in the best interests of members in schemes where there is a greater proportion of deferred members to actives.

66. Only a small number of respondents commented on demographic factors and there was a fairly even split as to whether this should be a consideration. One commented that as value for money is dependent on so many different factors, no further prescription should be necessary. Another respondent felt that the degree of support from the sponsor for unexpected events should be considered, and one suggested that contribution levels should be considered.

Government Response

67. We will not include scheme status or demographic factors as part of the value for members assessment.

68. Trustee knowledge and understanding can have a significant effect on member outcomes and we propose that trustee knowledge and understanding is included as a measure of value for members. We note respondents' views that this area may be difficult to measure. We believe that providing more information in new statutory guidance, together with the existing education, guidance and codes of practice available from TPR, will assist schemes in this respect.

69. TPR will continue to regulate trustees' compliance with their legal duties, including the requirements for trustee knowledge and understanding. More broadly, TPR will use the information received via the scheme return about the value for members assessments as part of the intelligence they draw on when making decisions about their regulatory approach towards different segments of the market. TPR has made it clear that "If trustees cannot meet the standards we

expect, we believe they should wind up and consolidate savers into a better run scheme."[16]

70. TPR has also commented that "some trustees put a high value on the fact that they may know the members personally and can provide that recognition and familiarity. Those trustees have to take a step back and ask if that's actually what members value, and do they value it to the extent that they're paying more in charges than they should be, and that their funds aren't necessarily being invested in the best way that they can be."[17]

Summary

We propose that the level of trustee knowledge, understanding and skills within the trustee board as a whole will be used as a measure of value for members in the extended value for members' assessment.

Proposed changes to regulations

71. We propose to make amendments to the Administration Regulations 1996 and the Register of Occupational and Personal Pension Schemes Regulations 2005.

72. This section summarises the changes which will be made to these regulations by the draft Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021 which can be found in annex C.

73. We are seeking further views on two issues relating to these draft regulations which are set out in questions Q1 and Q2 below.

Amendments to the Administration Regulations

74. The proposed regulations would extend the requirements of the value for members assessment for relevant[18] occupational pension schemes which have been running for at least three years and have money purchase assets of less than £100m. Amendments to Regulations 23 and 25 of the Administration Regulations would require trustees of those schemes to complete the more detailed assessment on an annual basis and report on the results as part of their chair's statement.

[16] https://www.thepensionsregulator.gov.uk/en/media-hub/press-releases/badly-run-schemes-need-to-improve-or-consolidate

[17] https://blog.thepensionsregulator.gov.uk/2019/07/02/why-were-pushing-pension-schemes-out-of-the-market/?_ga=2.108791754.910796229.1593677552-1141885925.1584531551

[18] "relevant scheme" as defined by Regulation 1(2) of the Occupational Pension Schemes (Scheme Administration) Regulations 1996 – broadly, defined contribution schemes.

75. Further statutory guidance about what trustees should have regard to when completing this assessment will be provided.

76. We propose that the Regulations require trustees to assess value for members across three areas:

- Net returns (investment performance)
- Costs and Charges
- Administration and Governance

Net Returns and Costs and Charges

77. Net returns and levels of costs and charges have a significant impact on the value of a pension over the period it is invested.

78. These factors are to be assessed relatively in comparison to those of at least three other 'large' occupational or personal pension schemes[19] of which at least one would be willing to accept the members from the smaller scheme should the trustees decide after assessment to wind up and consolidate. We are proposing that a 'large' scheme is one with £100 million or more total assets.

79. A relative comparison of costs and charges can be achieved using the information on costs and charges that schemes are already required to disclose. To facilitate effective comparison of net returns, as well as improving transparency across the market, we also propose extending the requirement for disclosures on net returns.

Net return disclosure for all relevant schemes

80. We also propose to require that **all** relevant schemes, regardless of size, publish net returns for their default and self-selected funds. We propose advising in statutory guidance that net return figures be shown as annual geometric averages and that figures for returns be shown for investment performance from 2015 onwards, where possible. Smaller schemes in scope will then be able to complete a relative assessment of their returns in comparison.

Subsequent amendment to the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013

81. As a consequence of the amendment to the Administration Regulations in relation to the reporting of the scheme's net returns on investments, we propose that our amending regulations will also amend Regulation 29A (2) of the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 to require the return on investments information to be made publicly available free of charge on a website.

[19] A personal pension scheme which is not an investment-regulated pension scheme within the meaning of paragraph 1 of Schedule 29A to the Finance Act 2004;

Question 1: We would welcome your views on the reporting of net returns - how many past years of net returns figures should be taken into consideration and reported on to give an effective indication of past fund performance?

Amendments to the Administration Regulations continued:

Administration and Governance

82. We propose to regulate that certain factors of administration and governance be used in measuring value for members.

83. Regulations would require an absolute assessment to be made within the scheme of how it meets the various criteria of good administration and governance standards. Schemes would not be required to assess this element against three larger schemes as it is more difficult to establish comparable and quantifiable metrics across our diverse DC landscape.

84. The criteria we propose to be assessed are:

- Promptness and accuracy of core financial transactions
- Quality of record keeping
- Appropriateness of the default investment strategy
- Quality of investment governance
- Quality of communication with members
- Level of trustee knowledge, understanding and skills to operate the scheme effectively
- Effectiveness of management of conflict of interest

85. Based on assessing the three areas of i) net returns, ii) costs and charges and iii) administration and governance we propose that the scheme will be required via Regulation 23(1)(c)(b) to report overall in the chair's statement the extent to which the scheme represents value for scheme members. The outcome should be a holistic one but made with regard to government's statutory guidance.

Amendments to the Register of Occupational and Personal Pension Schemes Regulations 2005

86. The proposed amending regulations will also amend Regulation 3 of the Register of Occupational and Personal Pension Schemes Regulations 2005 to provide that in the annual scheme return ALL schemes regardless of size must confirm their scheme's monetary value of total assets.

87. For those schemes with assets of less than £100m and running for at least three years, we propose further amendments to Regulation 3 which will require the trustees or managers to state in their annual return whether they consider, on the basis of the most recent assessment carried out under the Administration Regulations (and the previous year's assessment, where applicable) that their scheme provides good value for members. Where the trustees have stated that

they do not consider that the scheme provides good value for members, then on the annual scheme return we propose that the trustees must indicate whether they plan to wind up the scheme and, if not, their reasons for not doing so and the improvements they plan to make to the scheme.

Question 2: Do you think that the amending regulations achieve the policy aims of encouraging smaller schemes to consolidate into larger schemes when they do not present good value for members?

Question 3: Do you believe that the statutory guidance increases clarity about the minimum expectations on assessing and reporting on value for members for specified schemes? Are there any areas where further clarity might be required?

Conclusion

We believe that the proposed measures outlined in this chapter will improve outcomes for savers by encouraging trustees to consider consolidating to ensure savers are in well-run schemes that deliver good value for members and that have the scale to invest in a diverse range of asset classes, including illiquids.

The government views accelerating the consolidation of the DC market into fewer, larger schemes as a priority. For this reason, the efficacy of any amendments made to regulations such as the current proposals will be kept under review. If any new requirements do not drive consolidation at sufficient pace, the Government will develop legislation to mandate consolidation.

Chapter 3: Diversification, performance fees and the default fund charge cap

Background

1. Chapter 4 of the 'Investment Innovation and Future Consolidation' consultation considered the interaction between the charge cap for default arrangements[20] used for Automatic Enrolment, illiquid investments and performance fees. It also proposed a new method for charge cap compliance to give trustees more flexibility to pay performance fees.
2. Here, we summarise the feedback we received to that chapter. We set out the details of proposed amendments to the charge cap to accommodate performance fees in order to facilitate investment in illiquid investments, and to put the exclusion of physical assets on a statutory footing. We also announce our intention to develop a further alternative option for schemes to use in calculating performance fees, to facilitate investment in less liquid assets such as venture capital.
3. We also propose updates to the non-exhaustive list of charges for charge cap guidance which indicates what we consider to be in or out of scope of the cap.

Stakeholder responses

The use of performance fees in illiquid investments

4. We asked about the extent to which performance fees are used or required for funds which offer illiquid investments, and whether market practice is changing. Responses to this question presented a mixed picture. It was clear that schemes can access illiquid investments without paying performance fees. However, respondents explained that the prevalence of performance fees varies depending on the type of underlying asset.
5. Those respondents that elaborated further generally agreed that performance fees are most common in private markets, such as venture capital, private equity and growth equity. They are less common in infrastructure and are rare in

[20] Introduced in April 2015 by The Occupational Pension Schemes (Charges and Governance) Regulations 2015 (SI 2015/879)

property investments. A couple suggested that this variation was due to the differing investment strategies associated with certain asset classes.

6. A few respondents working in the venture capital or alternative investments industry suggested that performance fees are necessary for those types of investments. Reasons given focused on their use having been accepted practice globally over a long time, alignment of interests between investors and investment managers and the level of skill needed from investment managers. Other respondents stated that, in practice, the terms of performance fees are not always effective at aligning the interests of investors and investment managers.

7. Several of the large scale pension schemes and master trusts that responded are already invested in illiquid investments, within the existing charge cap, and without paying performance fees. One large master trust stated that they have been investing in direct illiquid UK property for years. Their scale has enabled them to negotiate access for competitive base fees, at the level needed to keep costs within their investment cost constraints, which are significantly below 30bps, without paying performance fees.

8. One respondent stated that the majority of their illiquid assets have no performance fee and that it is possible to find managers who are willing to manage illiquid assets on an ad valorem basis, while still being within the charge cap. They also emphasised that when considering illiquid assets, the issue of an illiquidity premium and alpha should not be confused. Trustees should seek to harvest diversified illiquidity premia for scheme members, rather than pay for alpha which may not exist.

Changes in the use of performance fees

9. On the question of whether practices are changing, several respondents pointed out that the scale of assets in DC is still a fraction of those in the DB market. Private market funds are often over-subscribed, meaning that there has been little need for managers to adapt their charging structure to attract DC investment.

10. However, pension schemes and their advisers told us that as the DC market matures, they are seeing more options for accessing illiquid investments without performance fees. Some pointed out this has the potential to create a higher annual management charge than if it were alongside a performance fee.

Performance fees and the charge cap

11. There is a charge cap on the default arrangements of DC schemes used for Automatic Enrolment[21]. Double defaulters - individuals who make no choice when they are automatically enrolled about joining a pension or the fund to which they contribute - will be put in to a default arrangement. The cap was introduced to

[21] Introduced by The Occupational Pension Schemes (Charges and Governance) Regulations 2015 (SI 2015/879)

protect these members from excessive charges and to present a straightforward offering to those new to financial services.

12. The charge cap is 0.75% of the funds under management each year, or an equivalent combination charge. It includes most charges, but excludes transaction costs (the costs of trading) and the costs associated with holding and maintaining assets whose value is based on their physical form, such as property and infrastructure. There is guidance for trustees of occupational pension schemes on how the charge cap works[22].

13. There are currently two options for trustees to measure charges for funds under management to confirm they are compliant with the cap. Both methods apply over a calendar year, referred to as a charges year. The first option requires the value of the members' fund to be measured at regular reference points throughout the year and the average of those figures calculated at the end of the year. The sum of charges throughout the year is then assessed as a percentage of that average fund value. The guidance refers to this as the retrospective method.

14. The second option requires the scheme to have a predictable charges regime. Because the level and frequency of charges are known in advance trustees can confirm at the beginning of the charges year that no member will be charged more than the cap. The guidance refers to this as the prospective method.

15. Both methods for measuring charges require that the maximum permitted charge is pro-rated when the cap applies to a member for less than a full charges year. This can happen when a member leaves or joins during the charges year.

Issues with the mechanism of charge cap compliance

16. We asked whether complying with the charge cap acts as a barrier to accessing funds which charge a performance fee and whether, in turn, this acts as a barrier to accessing certain asset classes. Several respondents from across the investment industry, pension schemes and their service providers told us that the way that the charge cap is calculated does act as a barrier to paying performance fees. There were two issues identified with the mechanism of charge cap compliance:

17. The first issue identified was the requirement to pro rate the cap for scheme members who are invested for less than a charges year. The charge cap of 0.75% of assets under management applies to scheme members invested for the full charges year. A scheme member invested for four months, or a third of a year, would have a cap of 0.25%, a third of the annual cap.

18. As performance fees are based on investment returns and are likely to vary throughout the year, trustees would find it difficult to ensure that for any combination of leaving and joining date within a charging year, no scheme

[22] The charge cap: guidance for trustees and managers of occupational schemes - https://www.gov.uk/government/publications/the-charge-cap-guidance-for-trustees-and-managers-of-occupational-schemes

member will pay more than the prorated charge cap. One response explained that, even where their fund had applied a cap on maximum permitted performance fees within the charges year, the pro rating requirement meant that compliance could not be guaranteed.

19. The second issue identified with the mechanism related to the interaction between a fixed charge cap and an uncapped performance fee. A couple of responses suggested that in order to avoid a breach of the cap, trustees will want to leave enough headroom for any potential performance fee. This leads in turn to a lower allocation than might be preferred.

Level of the charge cap

20. Although not the mechanism for compliance, several respondents did mention the level of the cap as a potential barrier to investing in certain asset classes. This concern arose where the assets under consideration may have higher management costs than traditional equities due to the need for more intensive, specialised management. Although the view that this made them inaccessible within the cap was not universal it was a perception held by several respondents.

12. Further issues were raised about the level of the charge cap. A few respondents suggested that trustees would be reluctant to increase spending on investment to make use of the unused headroom in the charge cap. We are reviewing the scope and operation of the charge cap, and part of the aim of that review is to ensure trustees are encouraged and enabled to invest in a wide range of assets, including illiquids, while maintaining clear and transparent protection for savers. We will publish that review towards the end of 2020.

Other barriers to DC schemes paying performance fees

21. The ‘Investment Innovation and Future Consolidation’ consultation identified that there are specific considerations about how performance fees work in relation to DC schemes. Members of DC schemes can leave and join funds at any time, including during a period over which a performance fee is assessed. It may not be possible to accurately distribute performance fees levied on a pooled fund to the scheme members who benefited from the investment growth. This concern was shared by some respondents.

22. A couple of respondents went further and pointed out that many of the features of a well-structured performance fee do not work as intended when scheme members can transfer in or out during the lifetime of the fund. Examples of such features include high watermarks, which prevent investors paying for the same performance multiple times as the value of the fund fluctuates, and hurdle rates, which require a minimum level of return before any performance fee is paid. If a scheme member joins after the high watermark has been passed, they may not pay a performance fee on the returns they receive in the future. If a scheme member joins after a hurdle rate has been passed, they will not benefit from its protection.

23. Several of the responses from the investment industry described how traditional multi-year funds, which are most common across venture capital and growth and private equity, are structured. They explained that performance fees, or profit sharing as they are sometimes called, are only fully known at the end of the fund's life once all of the investments have been realised. This extended assessment period ensures that the fees are accurately calculated at fund level, and is designed to encourage sustained performance. However, it exacerbates the difficulties with fairly allocating fees to the appropriate members, as is necessary in DC.

24. In addition, a couple of respondents suggested that investment platforms specifically struggle to incorporate funds with performance fees because of difficulties with fairly apportioning them, raising concerns that they may create Treating Customers Fairly issues.

25. Whilst no one presented a definitive solution to these concerns about fairness, a couple of ways of minimising the impact were suggested.

26. First was the regular calculation and accrual of the performance fee, which was discussed in the consultation and incorporated into the proposal we put forward in 2019.

27. The other suggested approach was for funds to have monthly or annual share classes within which the performance fees were assessed. Once the performance fees had been levied, the share classes could be merged in to a single fund. One respondent acknowledged the additional administrative burden this presented.

28. The consequential effects of paying a variable fee were also discussed. This included, most notably, the costs disclosure framework which applies to DC schemes and how to communicate performance fees in a way that allows members to assess value. Additional burdens for schemes in comparing the costs of different funds and monitoring how performance fees have been applied were also raised.

Other barriers to accessing illiquid investments

29. Some respondents identified other barriers to DC schemes accessing illiquid investments as being more pressing than the charge cap and performance fees. The most prominent barrier put forward was that the investment platforms which the vast majority of DC schemes use are often only compatible with investments which are priced daily. This means DC schemes may struggle to gain access to the existing products.

30. Several respondents raised behavioural reasons that meant those running schemes were reluctant to spend more on investment. They told us that competition between schemes is mainly based on costs and schemes were concerned that by investing in a more expensive investment strategy, they would appear to offer worse value for money than other, cheaper schemes.

31. A couple of respondents identified that - in times of market stress - schemes with exposure to more illiquid investments may find it difficult to rebalance the portfolio to keep charges within the cap.

Proposed amendment to the charge cap compliance mechanism

32. The ‘Investment Innovation and Future Consolidation’ consultation proposed an additional method of charge cap compliance to make it easier for trustees to invest in funds which levy performance fees.

33. The proposed method required that schemes first use the existing prospective method of assessment to establish that the charges, excluding performance fees, are compliant with the charge cap for any combination of joining or leaving date. Then, just for scheme members invested for the full year, the difference between the charges for the full year and the charge cap would be calculated. This difference is the budget that can be spent on performance fees.

34. If a default arrangement has a charges regime that would result in members invested for a full year paying 0.5% of the value of their pot in fees then, under the proposed method, that arrangement could pay performance fees of up to 0.25% over the charges year.

35. By only considering the performance fees in relation to scheme members invested for the full charges year, this method avoided the prorating issue. As long as the maximum potential performance fees, plus the % funds under management fees would be compliant with the charge cap for scheme members invested for a full year, and the % funds under management fees would be compliant with the prorated cap for partial year members, then the charges regime would be permitted.

36. We sought views on whether this additional method of charge cap compliance should be permitted, whether it was likely to lead to problems with complying and whether it may disadvantage members.

Minimising the potential for disadvantage to individual members

37. The consultation identified the risk that members of DC schemes could pay performance fees which are not related to the investment returns they have received.

38. In simple terms, this is because the performance fee is typically levied on a pooled fund, but passed on to individual scheme members’ pots. As scheme members of a DC scheme may transfer in and out of the fund at any time, their period of membership may not align with the time period over which the performance fee is assessed.

39. To reduce the potential impact of this unfairness, the consultation proposed that statutory guidance could specify that DC schemes should only accommodate

performance fee structures which accrue[23] the performance fee each time the value of the investment fund is calculated. Although the consultation did point out that trustees would want to consider the frequency with which those performance fees are paid out to the managers and whether that might encourage short term decision making.

40. It also proposed that the additional flexibility around performance fees only be permitted alongside a funds under management charge and not alongside combination charges, which include either a contribution charge, or a flat annual fee. This reflected one of the principles set out when the charge cap was introduced to simplify charging so that scheme members are able to compare the value of different schemes.

41. The additional method of assessment received broad support and the majority of respondents who answered this question thought we should go ahead.

42. Respondents did, however, identify some problems with introducing the additional method of assessment. The fact that it relies on a capped performance fee which is not standard practice was raised. As the additional method is linked to the prospective method of charge cap compliance, it would require trustees to confirm at the beginning of the charges year what the maximum possible performance fee would be. It was pointed out that capping performance fees could mean that the full charge cap budget is rarely used in practice because the headroom has to be reserved for potential high returns.

43. We spoke with pension lawyers and service providers who challenged the view set out in the consultation that most schemes use the prospective method of assessment. They pointed out that where schemes pay any ad hoc fees within the year, such as paying for auditing services, they do not operate a regular charges regime. A charges regime is the basis of the prospective method of assessment. The use of the retrospective method is, therefore, much more common in practice than we first realised and those schemes would not benefit from the flexibility offered by the proposed additional method.

44. Of those respondents who disagreed with the proposal, the reasons given were split. A couple from the investment industry raised the point that the method does not reflect the way that many performance fees are charged, in that it would only permit capped performances. The others, from pension schemes and a trade union, argued that the change is not necessary and may encourage performance fee use, which they considered to be inappropriate for DC schemes.

45. There was also broad support for the proposal that statutory guidance be produced which would require performance fees to be accrued each time the investment is valued. The proposal to limit the additional method to schemes which use a single charge structure was also well supported as a means to

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[23] By accrual we mean that the fees are calculated and the value of the fund is adjusted to reflect them. They are not necessarily banked (crystallised) by the investment manager at this point. The fees would however constitute a charge, unless they are refunded to departing members.

reduce complexity for members and trustees. There were a couple of concerns that this would restrict two of the largest master trusts, who do use combination charges, from making use of the additional method. One respondent argued that even where a combination charging structure is being used, the performance fee would be reported within the funds under management charge and so would not add a third type of charge for scheme members.

Government response

46. The evidence we received demonstrated that trustees can develop a well-diversified portfolio without paying performance fees. The investment industry is beginning to develop charging models which reflect the structure of DC schemes and it is realistic that this will continue as the DC market grows and consolidates.

47. It seems that the extent to which the charging models are changing does vary based on the underlying asset class. However, we have not seen any evidence to indicate that there are asset classes which are inaccessible to DC schemes due to the charge cap

48. Closed-ended investment trusts are pooled investment vehicles which invest in a portfolio of assets and issue shares which can be traded on a stock exchange, like a listed company. Because there is a fixed number of shares, investors can only cash out of the trust by selling their share. This means that the trust itself does not have to be able to offer redemptions and can, therefore, invest in illiquid assets, but the investors can trade the shares like any other equity. This characteristic can make investment trusts an attractive option for DC schemes seeking exposure to less liquid asset classes.

49. We looked at available investment trusts in the infrastructure, renewable infrastructure and venture capital sectors and found that they all had options both with and without performance fees[24]. One of the seven listed infrastructure trusts and one of the 12 listed renewable infrastructure trusts each levied a performance fee. Of the ten largest venture capital trusts, six levied a performance fee. Of the three sectors, it was only in infrastructure where the highest 5 year returns were from a fund with a performance fee.

50. The fact that competition between schemes is based mainly on the level of charges may well lead to a perception that cheapest means best value. This is not a new phenomenon. Before the introduction of the charge cap, when employers did compare pension schemes it was likely that they would prioritise low charges rather than scheme quality or governance[25]. We want to make it

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[24] Analysis carried out on Morningstar Closed-end Fund Screener website, August 2019 - http://tools.morningstar.co.uk/uk/cefscreener/default.aspx?Site=UK&Universe=FCGBR%24%24ALL&LanguageId=en-GB

[25] Defined contribution workplace pension market study, September 2013 - https://webarchive.nationalarchives.gov.uk/20140402194810/http:/www.oft.gov.uk/shared_oft/market-studies/oft1505

clear that good value for money is about more than just low fees, and that investment returns must always be considered as part of assessing value. This is why we are proposing that net returns are included in the updated value for members assessment. Detail of this proposal is covered in chapter 2.

51. Where the trustees of large DC schemes decide to invest the default in illiquid assets, they will generally make up no more than 10-15% of the portfolio. Therefore, we are satisfied that a diversified portfolio can be achieved by blending those assets with lower cost ones to keep overall costs within the cap.

52. We understand that trustees may be cautious about making use of the available headroom in the charge cap while there is a review of the level of the cap pending. We are reviewing the level of the charge cap this year, as well as considering the permitted combination charging structures and the treatment of transaction costs. In reporting on that review, we will seek to give trustees sufficient assurances so that they are able to make appropriate long term investment decisions.

Amendment to the charge cap compliance mechanism: an in-year adjustment to prorating performance fees

53. While we are satisfied that schemes can access a broad range of investments without paying a performance fee, it is for trustees to decide whether a performance fee represents best value for their members. We also understand that the current charge cap compliance mechanism restricts the performance fees which schemes can pay and that greater flexibility could be afforded to trustees, while maintaining member protections. After considering responses to the consultation we plan to proceed with an amendment to the way that compliance with the charge cap is measured.

54. The requirement to prorate the charge cap works for charges which are spread evenly throughout the charges year. However, we recognise that for performance fees, which can significantly vary throughout the year, the requirement to be able to meet the prorated cap level for any combination of joining or leaving date is difficult to satisfy. Our proposed draft regulations will provide an easement to the requirement to prorate performance fees when assessing compliance with the charge cap.

55. We initially proposed an additional method of compliance which would only apply to the prospective method of assessment. As we are now aware that the retrospective method of assessment is widely used by schemes, we have adapted the proposal so that it will apply to both.

56. Where a scheme member is in the default arrangement for only part of the charges year, we propose that trustees will still have to calculate a prorated charge cap based on the length of time they have been a scheme member. The effect of the proposed policy change will be that when assessing the charges that scheme members have paid against the prorated cap, trustees will exclude the

performance fee element[26]. This only applies to partial year membership. When considering a scheme member who is in the default arrangement for the whole of the charges year, the performance fee would be assessed against the charge cap.

57. This proposed easement will not apply to all performance fees; the draft regulations only allow trustees to exclude a performance fee from the calculation where it is accrued each time the value of the investments is calculated[27]. This prevents a situation where a scheme member joins an arrangement after an investment has increased in value and ends up paying a performance fee on the growth which occurred before they joined.

58. We propose that a performance fee which is accrued less frequently than the tradeable value of the investment is calculated would still be subject to the prorating requirement.

59. We propose that it is more appropriate to put the accrual condition into regulations rather than statutory guidance as we previously suggested.

60. The draft regulations are available at Annex C- Regulation 6 makes amendments to the Occupational Pensions (Charges and Governance) Regulations 2015. A Keeling Schedule, indicating how the Charges and Governance Regulations will read once updated is available at Annex D.

61. We propose that the easement for performance fees would apply to the first charges year which begins after 5th October 2021[28].

Question 4: Do the draft regulations achieve the policy intent of providing an easement from the prorating requirement for performance fees which are calculated each time the value of the asset is calculated?

Further option for the charge cap compliance mechanism: creating a multi-year rolling calculation approach

62. Some stakeholders have suggested that DC schemes may require further flexibility in how they calculate performance fees within the charge cap, and that they should be given the option to calculate such performance fees over a multi-year rolling period. It's suggested that a multi-year option would be necessary to facilitate access to venture capital and growth equity assets that determine the performance element of their fees (known as a 'carry') over multiple years. A five year rolling average has been suggested by the British Business Bank[29] as a suitable period.

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[26] "performance fee" is defined in regulation 6(2)(a)(iii) of the draft regulations.

[27] Regulation 6(2)(c) of the draft regulation.

[28] Regulation 1(5) of the draft regulations.

[29] https://www.british-business-bank.co.uk/research/the-future-of-dc-pensions-enabling-access-to-venture-capital-and-growth-equity/

63. We therefore propose developing a multi-year approach to calculating performance fees as an alternative option for schemes that believe a long smoothing period is required to enable them to access a wider range of illiquid assets. Such an approach would amend the calculation methodology to align with the multiyear structure by which these "carry" payments are assessed. Our proposal is that schemes will be able to select whether to use the in-year approach set out in our draft regulations or to use a multi-year approach.

64. We seek views on how a workable mechanism for enabling a rolling calculation over a number of years might best be constructed. There is a balance between creating a framework that can allow schemes to reflect the complexity of performance fees across multiple years without making that calculation overly burdensome. We are keen to hear views from stakeholders about how such an measure might best be achieved in order to facilitate DC scheme access to the less liquid products that charge in this way.

65. We are also particularly interested in input from asset managers and distributors about ways in which their charging structures might be adapted to better fit the needs of DC schemes as customers.

Question 5: What should we consider to ensure a multi-year approach to calculating performance fees works in practice?

Question 6: We are proposing a five-year rolling period. Is this appropriate or would another duration be more helpful?

Question 7: We are proposing offering a multi-year option as an alternative to an in-year option for schemes. Do you have any suggestions for how to improve this offer?

Question 8: To what extent will providing a multi-year smoothing option give DC trustees more confidence to invest in less liquid assets such as venture capital?

Cost of holding physical assets

66. The costs of holding physical assets, such as real estate or infrastructure, are not included within the charge cap. This is already set out in the charge cap guidance[30] but we propose to take this opportunity to put that exclusion on a statutory footing.

[30] The charge cap: guidance for trustees and managers of occupational schemes, see paragraph 12, page 6, October 2016 - https://www.gov.uk/government/publications/the-charge-cap-guidance-for-trustees-and-managers-of-occupational-schemes

67. The draft regulations carve the costs solely attributable to holding physical assets out of the charge cap[31]. They define physical assets[32] and provide a non-exhaustive list of costs[33] which are excluded.

- **Physical assets** are defined as: an asset whose value depends on its physical form, including land, buildings and other structures on land or sea, vehicles, ships, aircraft or rolling stock, and commodities
- Within that, **commodities** are defined as: any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products and energy such as electricity, but not including cash or financial instruments.

- The non-exhaustive list of costs is:
  - the costs of managing and maintaining the asset;
  - fees for valuing the asset;
  - the cost of insuring the asset in question;
  - ground rent charges, rates and taxes incurred in relation to the asset.

68. The following are examples of charges that we would consider to be solely attributable to holding physical assets, and therefore excluded from the charge cap:

- Costs of maintenance, repair, improvement and development of properties and other physical assets, including project management and contractor costs;
- Costs of holding the physical assets including business rates, insurance, utilities, void costs, valuation fees;
- Property management fees paid to third parties for day to day management.

69. This proposed update to the Charges and Governance Regulations would come in to force on 5th October 2021.

[31] Regulation 6(2)(a)(i) of the draft regulations.

[32] Regulation 6(2)(a)(ii) and (iii) of the draft regulations.

[33] Regulation 6(2)(b) of the draft regulations.

Question 9: Do the draft regulations achieve the policy intent? Do you have any comment on the definitions used?

Non-exhaustive list of charges

70. The 'Investment Innovation and Future Consolidation' consultation included a non-exhaustive list of costs and charges and whether Government considered each to be in or out of scope of the charge cap[34]. This was provided to support trustees in understanding the Government's policy intent.

71. The updated list of cost and charges was overwhelmingly welcomed as providing greater clarity on the policy intent.

72. We received one substantive query from a couple of respondents. This was in relation to the costs incurred in underlying firms and when trustees should 'look through' to those costs.

73. We have always been clear that trustees should look through to underlying costs in investment funds, for example in fund of fund structures. However, where the firm in which the scheme is invested is a commercial company rather than an investment company, for example a supermarket, the underlying costs of running the supermarket would not be considered when calculating charges for the cap.

74. In order to determine when trustees should look through to underlying costs, we had proposed that they do not look through to the costs 'incurred by investee firms which have a general commercial or industrial purpose'. Two responses asked for further clarification on how trustees can make this assessment, particularly in relation to the treatment of real estate investment trusts (REITs).

75. In response to this request for further clarification, we have amended the list of costs and charges (see annex F). We propose that schemes should look through all open-ended funds and all UK listed closed-ended investment funds and international equivalents. The vast majority of securities which are listed in the UK appear on the Financial Conduct Authority's Official List[35]. For the purpose of the list, securities are categorised. If a company is categorised as a **closed ended investment fund,** then schemes should look through to the underlying costs.

76. Whether a firm is a REIT does not determine the need to look through to underlying costs. If a UK-listed REIT is classified as a closed ended investment fund, then there should be look through. If it is classified as a commercial company, then there is no look through.

77. Where a security is not so explicitly categorised either because it is listed in another country or it is not on the Official List, trustees will want to continue with the current practice of considering their own legal advice on the status of underlying charges.

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[34] See annex to Investment Innovation and Future Consolidation

[35] The Official List - https://marketsecurities.fca.org.uk/officiallist

Chapter 4: Using transparency as a prompt

Background

1. We proposed[36] that 'Relevant schemes' (broadly, schemes offering money purchase benefits other than from AVCs alone) with 5,000 or 20,000 or more members, or alternatively £250m or £1bn assets to provide for money purchase benefits, be required to report their policy in relation to illiquid investments, in their Statement of Investment Principles (SIP)[37] and potentially their default SIP[38].

2. Schemes in scope would also be required to report annually, via the implementation statement, on their main default arrangements' approximate percentage holdings in illiquid assets, accompanied by a breakdown in holdings.

3. Our intention was to prompt larger schemes to consider the diversification benefits of illiquid investments.

Stakeholder responses

Summary

4. Stakeholder responses on the topic were split. A majority of respondents favoured some sort of transparency measure to prompt consideration of illiquid assets but this feedback was concentrated in a large number of responses by asset management firms specialising in illiquid assets.

5. Other respondents were opposed to the measure. A range of concerns were expressed around practicalities of the measure, whether the measure was needed to drive real change and whether implementing it would have undesirable or unintended consequences.

Practical issues

6. Stakeholders identified a number of practical issues, most prominent being the definition of illiquidity. Particular assets which are typically liquid may become

[36] Chapter 3, paragraphs 1-19 of Investment Innovation and Future Consolidation: A Consultation on the Consideration of Illiquid Assets and the Development of Scale in Occupational Defined Contribution schemes

[37] Required by section 35 of the Pensions Act 1995

[38] Required by Regulation 2A of the Occupational Pension Schemes (Investment) Regulations SI 2005/3378

illiquid at times of market stress, meaning that assets will move in or out of the definition, without any asset allocation decision on the part of the trustees[39]. Several respondents also emphasised this would lead to difficulty in accurately reporting holdings via the implementation statement.

7. It was suggested that a feasible definition would need to rely on an assessment of whether the assets were traded on public or private markets. But this would come with additional complexity and perverse consequences, which we cover in the Government response below.

8. Many respondents highlighted the long time horizon of DC savers, suggesting that the benefits of a longer-term tie in to illiquid assets should follow. However, others also highlighted that members will wish to transfer and decumulate, and the timing of such flows cannot be exactly predicted. This is likely to require some form of unitisation of the assets to ensure that both savers who depart and those who remain invested get 'their' assets.

9. One respondent to the consultation also highlighted the impact of "gating" open-ended funds on member transfers (blocking member withdrawals, whilst some of the assets are sold), which became a wider concern later in 2019, and again in 2020 in response to covid-19. This risks being problematic in a default arrangement where the member has made no choice of fund.

10. Respondents pointed to other liquidity challenges. Smaller schemes which had invested in illiquid assets would find it more difficult to consolidate or wind-up into master trusts. Master trusts with large participating employers would also be vulnerable to a liquidity crunch if those employers sought to switch. These are real considerations as we are keen to increase the pace of consolidation further. There has been a 12% fall in scheme numbers[40] in the past year and employer switching is expected to continue at a rate of between 5% and 10% each year.[41]

11. In relation to reporting holdings, a range of practical impediments were raised, including the need to avoid conflict with investor confidentiality clauses, and the need for "look through" of assets, potentially over multiple layers.

Whether further measures are necessary

12. Stakeholders raised a number of concerns about the necessity of additional reporting.

13. Several highlighted that comparable SIP requirements already exist, meaning that a more granular disclosure in relation to one asset class may not add particular value. Existing requirements include the trustees' policies in relation to the kinds

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[39] In any case, respondents highlighted that it is not the illiquidity of the asset *per se* which automatically adds value – assets do not automatically gain value on becoming illiquid. We cover this point more below.

[40] The Pensions Regulator. DC Trust – presentation of scheme return data 2019-20

[41] Corporate Adviser. Workplace Savings Report. November 2019

of investments to be held, the balance between different kinds of investments and the expected return on investments. The annual implementation statement, by which schemes will report their implementation of their SIP policies, is intended to cover all aspects of the SIP, meaning that disclosures of actual practice in relation to these policies will also be made public.

14. Other respondents suggested that some form of 'nudge' via transparency was unlikely to drive change. Trustees were well aware of the existence and potential of alternative assets and where they had not invested, there were good commercial or fiduciary reasons for their decision. These included concerns about the cost, value, risk or return of available products; the lack of functionality on the part of many investment platforms to host assets which are traded less frequently than daily; and, for smaller schemes, an awareness that they lacked the scale or governance capability to access or evaluate such assets. We have set out our proposals on ways to drive consolidation in chapter 2.

Undesirable consequences

15. Stakeholders identified several undesirable or perverse consequences from the proposal. These covered the impact of a reporting threshold, the focus on one asset class above others, and the perceived conflation of public policy and fiduciary goals.

16. We suggested that schemes with 5,000 or 20,000 or more members, (or alternatively £250m or £1bn assets) should be required to state their policy. Whilst an asset based threshold of perhaps £250m was most widely favoured, a small number of respondents queried the use of such a threshold. They suggested it might well stifle or stymie innovation amongst smaller schemes who would perceive a message from Government that they were not able to invest in a broader range of assets.

17. Clearly, this is not the case – with sufficiently low administration costs, such schemes can invest in Real Estate Investment Trusts (REITs), other closed-ended investment companies specialising in real assets or venture capital and in open-ended funds such as those invested in property.

18. Many stakeholders queried the focus on one asset class above others. Some respondents argued that there is no more an automatic premium in less liquid assets than in any other type of asset. Any illiquidity premium can be diminished and ultimately eliminated by an excess flow of funds seeking to gain advantage from it and a few stakeholders suggested that this was already happening in illiquid assets.

19. Some highlighted that schemes should be free to invest in members' interests rather than in accordance with Government steer, and asked why Government was not also mandating schemes to state their policies on emerging market debt, smaller companies, or other asset classes which appeared to offer attractive returns.

20. More broadly, there were concerns that investment in any assets should remain a fiduciary decision, not one which is perceived to be driven by public policy. The proportion of illiquid assets in a portfolio was said to be no more a measure of social goods than the volume of liquid assets.

Government response

Background

21. We thank stakeholders for their constructive challenge on this proposal. Whilst many respondents – not solely confined to firms with a commercial offering in this space – favoured the proposals and thought that they may help to offer a "nudge", support for the proposals was relatively soft.

22. Stakeholders suggested that it might start a conversation, or prompt trustees to think about such investments. They did not point to other ongoing or complete proposals in the UK or abroad where such interventions had been successful.

23. We agree with the view put forward by some stakeholders that the situation in respect of consideration of Environmental, Social and Governance (ESG) risks and opportunities is different. In that instance, there was clear evidence of conflation of factors which could well be financially material – consideration of which is wholly aligned with trustees' fiduciary duties – and purely ethical considerations. There is also is no requirement that trustees report on percentage holdings invested in a 'green' or 'climate-friendly' way – only that trustees take account of the opportunities and risks these factors present.

24. To date, we have not found any evidence of similar misunderstanding or conflation around illiquid investment opportunities in DC occupational schemes. As schemes grow in size, we are seeing consideration and selection of illiquid and real investments increase, suggesting that the barriers have predominantly stemmed from a lack of scale and a lack of accessible products, both of which repress demand. We are consulting on actions to address both of these other points in this consultation.

25. Turning to the specific points made in stakeholder responses summarised above, we respond on definitions and reporting, the impact of a threshold, managing scheme liquidity and the liquidity premium.

Definitions and reporting

26. On the definition of illiquid assets, we accept that there are risks in a discussion around illiquid vs liquid assets being boiled down and reduced to a contest between the merits of public and private markets. Successful economies will generally have well-functioning examples of both.

27. The same assets can straddle both public and private markets. Investment Trusts (strictly closed ended investment funds[42]) are traded on public markets, but contain illiquid assets, such as commercial property.

28. It would appear contrary to classify REITs as illiquid based on the underlying assets, as they can be traded readily through public markets. But to classify them as liquid whilst open-ended property funds are deemed illiquid would also be at odds, if Government policy then sought to nudge trustees away from liquid readily-tradeable ways of holding a basket of assets and towards potentially less liquid ways of securitising exactly the same assets.

29. Reporting of asset allocation in default strategies is also already happening, via the reports produced by such firms as Corporate Adviser[43]. Requiring schemes via legislation to separately publish data which they are already freely giving to data aggregators may not be burdensome, but it might seem unnecessary.

Thresholds

30. Government policy has rarely imposed levels of membership or assets above which new duties apply. However, if we were to follow this logic and apply the duty to all schemes with more than 100 members, in line with some existing requirements which flow from the IORP directives, we would extend the scope of legislation from around 50 schemes to approximately 900. This would bring in schemes with very limited governance budgets or capability to invest and may begin to constitute an unwarranted burden.

Managing scheme liquidity and the illiquidity premium

31. We fully accept that decisions on liquidity to manage member transfers and switching, and the long term goals of the scheme should rest with trustees. We also acknowledge the risk that mandatory reporting of percentage holdings in illiquid assets, however defined, could become perceived as a race.

32. More broadly, stakeholder views around an illiquidity premium are mixed. Many agree on the presence of an illiquidity premium, while others have argued that much if not all of the premium can in some instances be explained by leverage and company-level risk.

33. There are clearly a range of considerations for trustees before they make a decision to invest. We are encouraged to see that schemes are already moving towards a broader range of assets, including illiquids and real assets, as they develop scale. This indicates that there is not a lack of understanding of fiduciary duties leading to market failure, or harm to member outcomes.

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[42] https://www.handbook.fca.org.uk/handbook/glossary/G2485.html

[43] See for example Workplace Savings Report (November 2019) and Master trust and GPP defaults report (June 2019) both accessible from https://corporate-adviser.com/research/

34. We have listened to the responses from stakeholders and reviewed the wider evidence in favour of this measure. We have concluded that taking forward this particular measure is not appropriate at the current time and we will, therefore, not be legislating for a SIP requirement in relation to illiquid assets. We will continue to monitor this as the market grows and consolidates and we will review diversification of investment approaches, especially amongst the largest defined contribution pension schemes.

35. We will also continue to explore with stakeholders and across government how we can best enable trustees to invest in a diverse range of assets, including less liquid products, to deliver the best outcomes for their members.

Chapter 5. Updates to Statutory Guidance: Reporting costs, charges and other information

Background

1. DWP has received queries and feedback on the production and presentation of compounding costs and charges illustrations. To provide clarification, we are proposing draft amendments to the statutory guidance on "Reporting of costs, charges and other information: guidance for trustees and managers of relevant occupational schemes." This is provided at Annex G.
2. Trustees are concerned that the reporting requirements are disproportionately burdensome for the value they offer to scheme members. We believe this to be a result of an unintended interpretation of the existing guidance and, consequently, the blurring of the policy intent. The intent is that trustees communicate the compounding effect of costs and charges on retirement funds to scheme members simply and clearly.
3. We acknowledge the concerns and accept the feedback that the statutory guidance could be updated in order to set out more clearly the minimum expectations required when producing these illustrations.
4. The statutory guidance is not intended to be wholly prescriptive. We continue to encourage trustees to present costs and charges illustrations in a way they believe to be most beneficial to their members. These proposed updates are concerned with preventing unintended interpretations of the guidance which result in unnecessary anxiety for trustees, and the production of information in levels of both complexity and volume that are not required, and may be unhelpful for scheme members.
5. We welcome views from trustees, scheme managers and other stakeholders on whether the proposed updates to the guidance will indeed provide greater clarity as to the minimum expectations with regards to the content of illustrations and the way in which they should be presented and published.

Updates to the Statutory Guidance

6. The main proposed updates and additions to the existing statutory guidance are covered below. Like the guidance itself, this list is not exhaustive.

Production of an Illustration

7. We have sought to draw out the distinction between schemes with a single price for scheme members of all employers, and schemes with multiple defaults and variable charges.

8. For schemes with a single price for all members, as a minimum, trustees simply need to identify the default arrangement(s), lowest charging and highest charging self-select funds in which members are invested, as shown in Figure 1 in the guidance.

9. A small number of stakeholders from schemes with both a large number of employers and a range of different charges for each of those employers are concerned that they must provide an illustration for every single fund offered by the scheme, leading to an onerous production task. This is not the case.

10. While we do expect an illustration to be produced for each individual employer's default fund, we propose that the scheme need only produce an illustration of: the default fund, the lowest charging self-select fund and highest charge self-select fund offered to the respective employer. An example of a minimum expectation for a scheme with multiple defaults is shown in Figure 2 in the guidance. For practical reasons we have shown an example of a scheme with just two default funds. Nonetheless, using this example as a principle guide, if the scheme had 20 different employer default funds, they would still only have to produce 20 illustrations in order to be consistent with the statutory guidance.

11. The examples in the guidance are not wholly prescriptive. We present them as a visual model of the minimum that may be required. We encourage schemes to disclose additional illustrations where they believe these would be useful to members. This may be especially useful for deferred members of the scheme. We are aware of numerous examples from stakeholders who already do this and we are supportive of further more personalised disclosure.

12. We have sought to provide clarity for schemes with multiple defaults or variable charges, in terms of presenting both savings pot sizes and real-terms investment return assumptions. We advise that the pot size used should be a median across the whole scheme, rather than producing a median for each default, or for each employer. Our intention in relation to the real-terms investment return is that this only needs to be shown for each fund or arrangement for which an illustration is provided.

Publication of costs, charges and other information

13. In updating this section of our original guidance we address the misinterpretation that trustees and scheme managers must contain all costs and charges information in a single, often very large, online document. Many stakeholders have told us that they fear they risk not complying with the Chair's Statement requirements if they split the material into multiple documents.

14. We want to make it clear that **all** the information - not just costs and charges compounding illustrations - under regulation 29A of the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013[44] can be published over a number of linked documents or pages.

15. We explicitly outline this fact in paragraph 77 of the new guidance, stating that: "The Statement of Investment Principles, the Chair's Statement (inclusive of charges and transaction cost information, value for money assessment and default SIP), and the relevant section of the Annual Report (the implementation statement) do not necessarily have to be produced as a single web-page or PDF document."

16. We also state that when the Chair's Statement is circulated in print format, it can simply be a collation of all the relevant documents.

17. We have added a diagram (Figure 3 in the guidance) to provide a visual representation of how documents can be produced as a series of interlinked documents which is compliant with regulation 29A. We included it here with accompanying illustration notes to further emphasise this point:

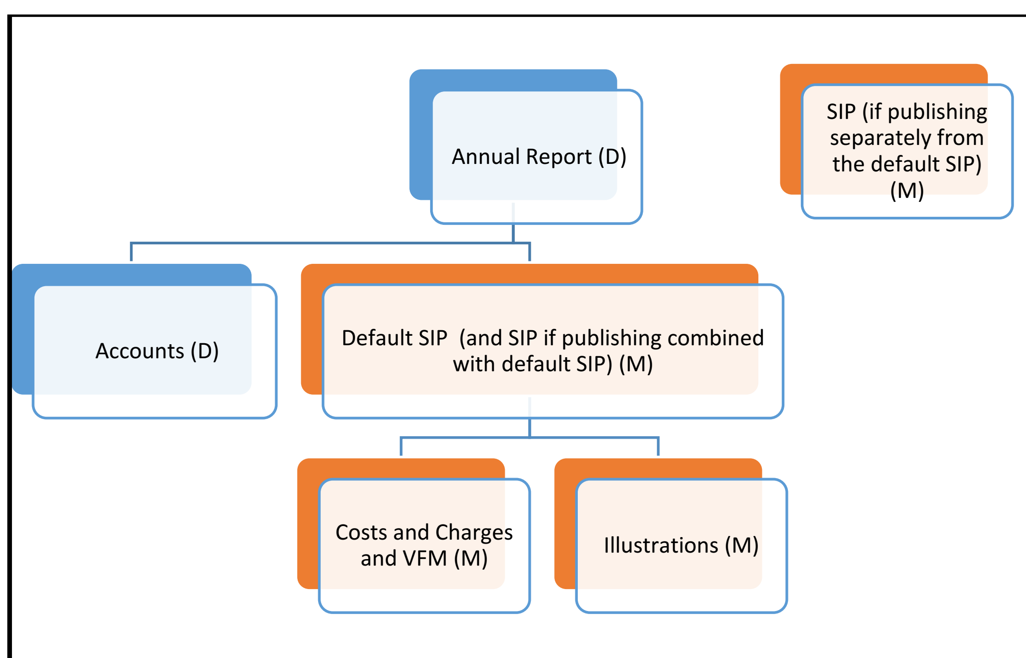

Figure 1 – Illustration of a document chain which is consistent with Regulation 29A

Illustration Notes

1. Figure 1 depicts a flow chart showing how the documents can be presented.
2. At the top of the flow chart is a box labelled 'Annual Report'.
3. Flowing out of this box is a box labelled 'Accounts' and a separate box labelled 'Default SIP (and SIP if publishing combined with default SIP)'.

[44] Regulations 29A was inserted by The Occupational Pension Schemes (Administration and Disclosure) (Amendment) Regulations 2018

4. This illustrates that trustees can provide a link to the Accounts and Default SIP from their Annual Report and present them separately.
5. Flowing out of the box labelled ‘Default SIP (and SIP if publishing combined with default SIP)’ are two additional boxes, one labelled ‘Costs and Charges and VFM’ and another labelled ‘Illustrations’.
6. This illustrates that trustees can provide a link to their costs and charges and VFM information and the compounding illustrations from their Default SIP and present them separately.
7. Directly to the right of the flow chart is a box labelled ‘SIP (if publishing separately from the default SIP)’.
8. This is to illustrate the SIP can be presented separately from the default SIP.
9. Collectively all the documents referenced in the separate boxes of the flow chart are the **Annual Report and Accounts**.
10. The boxes labelled ‘Default SIP (and SIP if publishing combined with default SIP)’, ‘Costs and Charges and VFM’, ‘Illustrations’ and ‘SIP (if publishing separately from the default SIP)’ all have an additional label (M).
11. (M) stands for ‘Mandatory publishing requirement’. All boxes with this label represent documents which collectively are the published parts of the **Chair’s Statement.**
12. The boxes labelled ‘Annual Report’ and Accounts’ have an additional label (D).
13. (D) stands for ‘Discretionary publishing requirement’. This illustrates that there is no legal requirement to publish the documents labelled (D).

18. We have used the labels ‘(D)’ and ‘(M)’ to clearly distinguish between the different publishing requirements for each of the documents. It is a mandatory requirement to publish the documents labelled ‘(M)’. Alternatively, for the documents labelled ‘(D)’ it is a discretionary requirement and they only need to be made available to members on request. We also want to make it clear that while acknowledging this distinction in the guidance, we do not seek to discourage the voluntary publication of additional documents.
19. We welcome comments on whether the proposed updates and additions to this guidance provide more clarity on the production and publication of costs and charges information, and if not, where further clarity is required. We are not seeking feedback on whether or not this information should be presented to scheme members.

Question 10: Do you believe that the proposed updates to the statutory guidance increases clarity about the minimum expectations on both the production and publication of costs and charges information?

Are there any areas where further clarity might be required?

Chapter 6: Other changes to legislation

Defaults with a “promise” and production of a default SIP

Background

1. When Government introduced new Charges and Governance requirements in April 2015 on occupational DC pension schemes, the range of measures included:

    - a charge cap – under regulation 6 of the Charges and Governance Regulations 2015[45], to ensure that “double-defaulters” – members of default arrangements in schemes used for AE – were protected from high charges;
    - a requirement – under regulation 2A of the Investment Regulations 2005[46], to produce a Statement of Investment Principles for the default arrangements used by the scheme (a default SIP) – to ensure that the default arrangement was appropriate for the membership, and the way in which this had been done was documented.

2. At the time of the introduction of both measures, a carve out was introduced in regulation 3(6) of the Charges and Governance Regulations 2015 to provide that an arrangement into which the member was automatically enrolled without making a choice of fund was not a default arrangement if before the benefits come into payment, it had a “promise” about the level of benefits from a third party. This meant that an arrangement with a promise which would otherwise meet the definition of a default was exempted from the cap on charges which applies to other default arrangements in qualifying schemes. This remains Government policy, in recognition of the cost of providing a pensions promise.

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[45]The Occupational Pension Schemes (Charges and Governance) Regulations 2015
http://www.legislation.gov.uk/uksi/2015/879/regulation/6

[46] The Occupational Pension Schemes (Investment) Regulations 2005
http://www.legislation.gov.uk/uksi/2005/3378/contents/made

3. In practice the only commonly found default arrangements which might arguably have guarantees such that they are, therefore, exempted from the charge cap – are older with profits policies.

4. Because of the way the regulations providing for a default SIP requirement were drafted, no scheme with a promise is required to produce a default SIP. This flows from the definition of “default arrangement” in regulation 1(2) of the Investment Regulations 2005, which was inserted by regulation 20(a) of the Charges and Governance Regulations 2015. Because the definition of default arrangement for the purposes of the Investment Regulations 2005 and the default SIP requirements does not omit paragraphs (6), (7) and (8) of regulation 3 of the Charges and Governance Regulations 2015, the carve out of arrangements with promises from the charge cap is also carried over to the default SIP.

5. This is not in line with our desired policy, which would be that schemes which offer a with profits fund as a default arrangement are required to document its aims and objectives; to explain how the selection of a with profits is intended to ensure that the assets are invested in the best interests of beneficiaries; and to regularly review its performance and appropriateness.

6. We are, therefore, consulting on a change in regulations which would require schemes for whom the default arrangement would (were it not for regulation 3(6) in the Charges and Governance Regulations) be a fund with a promise to be required to meet all the requirements in regulation 2A and produce a default SIP.

7. We also propose that the requirement to produce such a default SIP should apply with effect from 3 months following the end of the first scheme year to end after the coming into force date, in good time to be included in the first Chair’s Statement which is required to be produced after the coming into force date. This gives schemes a minimum of 3 months and up to 15 months in order to document a default SIP.

8. This proposed change is made in regulation 4(2) of the draft amending regulations.

Question 11: We propose that where the default arrangement includes a promise, the trustees of the scheme should be required to produce a default SIP.

We propose that this should be produced within 3 months of the end of the first scheme year to end after the coming into force date.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

Reporting costs and charges for funds which are no longer offered

Background

9. With effect from 6 April 2018 the Occupational Pension Schemes (Administration and Disclosure) (Amendment) Regulations 2018 ("the cost transparency regulations") have amended the Administration Regulations 1996 to require schemes to state the level of charges and transaction costs for the default arrangements offered by relevant schemes, as well as "self-select funds" – the funds which members are able to actively choose.

10. Our intention was that every member invested in the scheme would be able to identify the charges and transaction costs which they had paid for the funds in which they were invested.

11. The relevant drafting is in regulation 23(1)(c)(ii) of the Administration Regulations. Our rationale for the reference to "each fund which members are able to select" was to ensure that trustees who offer a default arrangement which is made up of several underlying funds, but which members cannot individually select, are not necessarily required to show the charges and transaction costs for each individual component fund – they are only required to state the level of charges and transaction costs applicable to the default arrangement, under regulation 23(1)(c)(i).

12. Our rationale for the reference to "in which assets relating to members are invested during the scheme year" was to cater for the situation where trustees have many fund offerings (sometimes more than 100) but some of these have not been selected by any of their beneficiaries.

13. However, we have been made aware of an alternate interpretation of "each fund which members are able to select". It has been argued that this means schemes are not required to show costs and charges for funds which members have previously actively selected, and in which those members remain invested, but are no longer offered to savers, and, therefore, are not able to be selected.

14. As this was never the intention, we are proposing to make an amendment to the Administration Regulations 1996 to require schemes to show the charges and transaction costs for each fund in which assets relating to members are invested during the scheme year and which members are able to select or have historically been able to select.

15. We are proposing that the regulations should "bite" on schemes with effect from the end of the first scheme year[47] to end after the coming into force date. As the Chair's Statement must be produced within 7 months of the scheme year end date, this means schemes will get a minimum of 7 months and a maximum of 19 months, depending on the scheme year end date, in which to publish costs and charges for each fund in which members are invested that they are or have been able to select.

16. This change is made in regulation 2(2)(b)(i) of the draft regulations.

Question 12:

We are proposing that, for relevant schemes, charges and transaction costs should be disclosed for any fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

Wholly-insured Schemes

20. Regulation 8 of the Investment Regulations 2005[48] upholds a long-standing exemption for wholly-insured schemes from sub-paragraphs (b) and (c) of regulation 2(3) of these regulations. As stated in the 2005 Investment Regulations Consultation,[49] wholly-insured schemes are exempt from these regulations, on the basis that a combination of scheme rules and the terms of the policies of insurance give trustees no discretion as to how the insurance company invests the scheme's funds.

21. Following the transposition of The Shareholders' Rights Directive (SRDII)[50], stakeholder feedback has highlighted that regulation 8(1)(a) of the Investment Regulations has not been amended to extend the exemption for wholly-insured schemes to new sub-paragraph (d) that was introduced through the SRD II regulations. This sub-paragraph [regulation 2(3)(d)] requires trustees to set out their policies in relation to their arrangement with any asset manager – including

[47] defined in regulation 1 of the Administration Regulations.

[48] The Occupational Pension Schemes (Investment) Regulations 2005

[49] PENSIONS: INVESTMENT REQUIREMENTS - Consultation on Draft Regulations 2005

[50] The Shareholders' Rights Directive (EU) 2017/828

references to matters covered in sub-paragraph 2(3)(b). TPR is aware of this issue and is not prioritising action in this area, pending these regulations.

22. Wholly-insured schemes are exempt from the need to produce most sections of the SIP. This is because typically a combination of scheme rules and the terms of the policies of insurance give trustees no discretion as to how the insurance company invests the scheme's funds. We therefore propose to amend regulation 8(1)(a) of the Investment Regulations to extend the long-standing exemption to cover regulation 2(3)(d) also. In our proposals published here, only wholly-insured schemes are in scope of the amendment to Regulation 8(1)(a).

23. However, we do still require trustees of DC schemes investing via unit-linked contracts to set out, in relation to the default fund or funds, in which the vast majority of members are invested, their policies in relation to choosing investments, the kinds of investments to be held, consideration of ESG risks including climate change, engagement, the exercise of voting rights and their arrangements with asset managers. This is because the trustees are free to enter different insurance contracts in order to change the investments which make up the default.

Question 13: Do you agree with this proposed change? Do you have any other comments on this topic?

Annex A: List of respondents

Aberdeen Standard Investments

ABI

ACA (Association of Consulting Actuaries)

Age UK

AIC (Association of Investment Companies)

AIM (Alternative Investment Management APPG)

AIMA and ACC (Alternative Investment Management Association and Alternative Credit Council)

Aon

AREF (Association of Real Estate Funds)

Association of Pension Lawyers

Aviva

B&CE

Baillie Gifford

Barnett Waddingham

British Business Bank

BGF

BioIndustry Association

Blackrock

BlueBay

BVCA (British Private Equity & Venture Capital Association)

Capital Cranfield

Gowling WLG

Hymans Robertson

ICAEW

IFoA (Institute and Faculty of Actuaries)

Independent Trustee Services

Investment Association

Investment Property Forum

JLT Employee Benefits

John Forbes Consulting

LCP

Legal and General

Mercer

Nest

Octopus

Partners Group

Pensions Management Institute

Phoenix Group

Pinsent Masons

PLSA

PPI

PRI (Principles of Responsible Investment)

Prudential

RBS Investment Executive Ltd

Redington

RPTCL (Railways Pension Trustee Company Limited)

Scottish Widows

SPP (Society of Pension Professionals)

Squire Patton Boggs

TRSP (Tesco Retirement Savings Plan)

UK Power Networks

UNISON

USS

Which

Willis Towers Watson

XPS

Annex B: List of consultation questions

Chapter 1: Summary

No questions

Chapter 2: Encouraging Consolidation

Q1: We would welcome your views on the reporting of net returns - how many past years of net returns figures should be taken into consideration and reported on to give an effective indication of past fund performance?

Q2: Do you think that the amending regulations achieve the policy aims of encouraging smaller schemes to consolidate into larger schemes when they do not present optimal value for members?

Q3: Do you believe that the statutory guidance increases clarity about the minimum expectations on assessing and reporting on value for members for specified schemes? Are there any areas where further clarity might be required?

Chapter 3: Diversification, performance fees and the default fund charge cap

An in-year adjustment to prorating performance fees

Q4: Do the draft regulations achieve the policy intent of providing an easement from the prorating requirement for performance fees which are calculated each time the value of the asset is calculated?

Creating a multi-year rolling calculation approach

Q5: What should we consider to ensure a multi-year approach to calculating performance fees works in practice?

Q6: We are proposing a five-year rolling period. Is this appropriate or would another duration be more helpful?

Q7: We are proposing offering a multi-year option as an alternative to an in-year option for schemes. Do you have any suggestions for how to improve this offer?

Q8: To what extent will providing a multi-year smoothing option give DC trustees more confidence to invest in less liquid assets such as venture capital?

Costs of holding physical assets

Q9: Do the draft regulations achieve the policy intent? Do you have any comment on the definitions used?

Chapter 4: Using transparency as a prompt

No questions

Chapter 5. Updates to Statutory Guidance: Reporting costs, charges and other information

Q10: Do you believe that the updated statutory guidance increases clarity about the minimum expectations on both the production and publication of costs and charges information? Are there any areas where further clarity might be required?

Chapter 6: Other changes to legislation

Q11: We propose that where the default arrangement includes a promise, the trustees of the scheme should be required to produce a default SIP.

We propose that this should be produced within 3 months of the end of the first scheme year to end after the coming into force date.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

Q12: We are proposing that, for relevant schemes, charges and transaction costs should be disclosed for any fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year.

(a) Do you agree with this policy?

(b) Do you agree that the legislation achieves the policy?

Q13: Do you agree with this proposed change? Do you have any other comments on this topic?

Annex C: Draft regulations

STATUTORY INSTRUMENTS

2021 No.

PENSIONS

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

Made - - - -	***
Laid before Parliament	***
Coming into force - -	***

The Secretary of State for Work and Pensions makes the following Regulations in exercise of the powers conferred by sections 113(1), (5), (6) and (7), and 182(2) and (3) of the Pension Schemes Act 1993([51]), sections 35 and 174(2) of the Pensions Act 1995([52]), sections 60(2)(h) and (3) and 315(2) and (3) of the Pensions Act 2004([53]) and sections 43 and 54(5) of, and paragraphs 1(2), 2(1), (2), (3) and (5) of Schedule 18 to the Pensions Act 2014([54]).

In accordance with section 185(1) of the Pension Schemes Act 1993, section 120(1) of the Pensions Act 1995, section 317 of the Pensions Act 2004 and paragraph 8 of Schedule 18 to the Pensions Act 2014, the Secretary of State has consulted with such persons as the Secretary of State considers appropriate.

In accordance with section 113(9) of the Pension Schemes Act 1993, the Secretary of State has consulted with the Financial Conduct Authority and the Treasury.

Citation, commencement and application

1.—(1) These regulations may be cited as the Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021.

([51]) 1993 c. 48. Subsection (1) has been amended by Child Support, Pensions and Social Security Act 2000, s. 52(1) and prospectively amended by the Pension Schemes Act 2015 (c. 8), s.38. Sections 113(5) to (10) were inserted by the Pensions Act 2014 (c. 19), s. 44(1), and section 113(5) is prospectively amended by the Pensions Scheme Act 2015 (c. 8), s. 38(6). Section 185 was amended by Schedule 3 (paragraph 46), Schedule 5 (paragraph 80) and Schedule 7, Part 1 to the Pensions Act 1995 (c. 26).

([52]) 1995 c. 26. Section 35 was substituted by s. 244 of the Pensions Act 2004 (c. 35).

([53]) 2004 c. 35.

([54]) 2014 c. 19.

(2) They come into force on 5th October 2021.

(3) The amendments made by regulations 2, 3(2)(b), 3(3) and 5 apply in relation to an occupational pension scheme from the day after the last day of the first scheme year of that scheme which ends after 5th October 2021.

(4) The amendments made by regulation 4(2) and (3) apply in relation to an occupational pension scheme from the date after the end of three months beginning with the last day of the first scheme year of that scheme which ends after 5th October 2021.

(5) The amendments made by regulation 6(2)(c) apply in relation to an occupational pension scheme from the day after the last day of the first charges year of that scheme which ends after 5th October 2021.

(6) For the purposes of this regulation—

"charges year" has the meaning given in regulation 2 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015([55]);

"scheme year" has the meaning given in regulation 1(2) of the Occupational Pension Schemes (Scheme Administration) Regulations 1996([56]).

The Occupational Pension Schemes (Scheme Administration) Regulations 1996

2.—(1) The Occupational Pension Schemes (Scheme Administration) Regulations 1996 are amended as follows.

(2) In regulation 23(1)([57])—

(a) after sub-paragraph (a), insert—

"(aa) report on the return on investments (after deduction of any charges or transaction costs relating to those investments), relating to—

(i) each default arrangement; and

(ii) each fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year,

having regard to guidance issued by the Secretary of State under section 113(2A) of the Pension Schemes Act 1993([58]);";

(b) in sub-paragraph (c)—

(i) in paragraph (ii), after "members are", the first time it appears, insert "(or were)";

(ii) for paragraph (iv), substitute—

"(iv) where the trustees or managers are required to assess the extent to which the charges and transaction costs borne by members represent good value for members, explain that assessment;";

(c) after sub-paragraph (ca), insert—

"(cb) explain the results of any assessment required under regulation 25(1A);".

(3) In regulation 25([59])—

(a) in paragraph (1), at the beginning of sub-paragraph (b), insert "unless the relevant scheme is a specified scheme,";

(b) after paragraph 1, insert—

([55]) S. I. 2015/879. There are amendments to regulation 2 which are not relevant to this definition.

([56]) S.I. 1996/1715. There are amendments to regulation 1(2) which are not relevant to this definition.

([57]) Regulation 23 was inserted by S.I. 2015/879 and amended by S.I.2016/427 and 2018/233.

([58]) Subsection (2A) was inserted by s.38 of the Pension Schemes Act 2015.

([59]) Regulation 25 was inserted by S.I. 2015/879.

"(1A) If the relevant scheme is a specified scheme, the trustees or managers of the scheme must, at intervals of no more than one year—

(a) assess the extent to which the scheme provides good value for members, and as part of that assessment, assess—

(i) the charges and transaction costs borne by members of the scheme by comparison with the charges and transaction costs borne by members of at least three schemes ("comparison schemes")—

(aa) each of which satisfy the conditions in paragraph (1C)(a), and

(bb) at least one of which satisfies the condition in paragraph (1C)(b),

(ii) the return on investments by comparison with the return on investments relating to—

(aa) the default arrangement, and

(bb) any funds which members are (or were) able to select and in which assets relating to members are invested during the scheme year,

for the three comparison schemes, and in each case the return on investments is to be calculated after deduction of any charges or transaction costs, and

(iii) how the administrative and governance criteria set out in paragraph (1B) are met by the scheme;

(b) in making the assessment required under sub-paragraph (a), have regard to any guidance issued by the Secretary of State under paragraph 2 of Schedule 18 to the Pensions Act 2014 in relation to that assessment.

(1B) The administration and governance criteria set out in this paragraph are—

(a) the promptness and accuracy of core financial transactions;

(b) the quality of the records kept by the trustees or managers;

(c) the appropriateness of the default investment strategy followed by the trustees or managers;

(d) the quality of the scheme's investment governance;

(e) the extent to which the requirements of sections 247 and 248 of the Pensions Act 2004([60]) are satisfied and the trustees or managers have the knowledge, understanding and skills to enable them properly to exercise their functions and to operate the scheme effectively;

(f) the quality of communication with the members of the scheme;

(g) the effectiveness of management of any conflicts of interest that might arise between or among trustees and managers, or between trustees, managers and third parties.

(1C) The conditions in this paragraph are that—

(a) each scheme used as the basis for the comparison is—

(i) an occupational pension scheme which on the relevant date held assets equal to or greater than £100 million; or

(ii) a personal pension scheme, which is not an investment-regulated pension scheme within the meaning of paragraph 1 of Schedule 29A to the Finance Act 2004([61]); and

(b) the trustees believe, on reasonable grounds, that one of the three schemes would be prepared to accept a transfer of members of the specified scheme if the specified scheme is wound up.

(1D) In this regulation—

"core financial transactions" has the same meaning as in regulation 24;

"default arrangement" has the meaning given in regulation 1 of the Investment Regulations;

([60]) 2004 (c. 35). Section 248 of the Pensions Act 2004 was amended by S.I. 2009/1941.

([61]) 2004 (c. 12). Schedule 29A was inserted by paragraph 13 of Schedule 21 to the Finance Act 2006 (c.25).

“default investment strategy” means the default strategy referred to in regulation 2A(1)(c) of the Investment Regulations([62]);

“the Investment Regulations” means the Occupational Pension Schemes (Investment) Regulations 2005([63]);

“specified scheme” means a relevant scheme which, on the relevant date—

(i) held assets worth less than £100 million, and

(ii) has been operating for three or more years;

“relevant date” means the last day of the scheme year preceding the year in which the assessment required by paragraph (1)(b) is made.”.

The Register of Occupational and Personal Pension Schemes Regulations 2005

3.—(1) Regulation 3 of the Register of Occupational and Personal Pension Schemes Regulations 2005([64]) is amended as follows.

(2) In paragraph (1)—

(a) after sub-paragraph (da), insert—

“(db) the value of the assets held by the scheme for the purpose of providing benefits to members, calculated on the last day of the scheme year which ended most recently;”

(b) after sub-paragraph (h), insert—

“(ha) in the case of a specified scheme—

(i) whether, on the basis of the assessment required by regulation 25(1A) of those Regulations (“value assessment”), the trustees or managers of the scheme consider that the scheme provides good value for members;

(ii) where a value assessment was carried out for the previous year, whether, on the basis of that value assessment, the trustees or managers of the scheme considered that the scheme provided good value for members;

(hb) in the case of a specified scheme where the trustees or managers of the scheme have stated under sub-paragraph (ha)(i) that they do not consider that the scheme provides good value for members—

(i) whether the trustees or managers propose to wind up the scheme and transfer its members into another scheme; and

(ii) if the trustees or managers do not propose to wind up the scheme—

(aa) their reasons for not doing so, and

(bb) what improvements they propose to make to the scheme to ensure that it does provide good value for members;”.

(3) In paragraph (4), after the definition of “recovery period”, insert—

““specified scheme” means an occupational pension scheme which is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 2005([65]) which, on the last day of the scheme year which ended most recently—

(a) held assets worth less than £100 million; and

(b) has been operating for three or more years.”.

([62]) Regulation 2A was inserted by S.I. 2015/897.

([63]) S.I. 2005/3378. The definition of “default arrangement” was inserted by S.I. 2015/879 and amended by S.I. 2016/427.

([64]) S.I. 2005/597. Sub-paragraph (da) was inserted into regulation 3 by S.I. 2015/879. There are other amendments to regulation 3 which are not relevant to these Regulations.

([65]) S.I. 1996/1715.

The Occupational Pension Schemes (Investment) Regulations 2005

4.—(1) The Occupational Pension Schemes (Investment) Regulations 2005([66]) are amended as follows.

(2) In regulation 1(2)([67]), in sub-paragraph (c) of the definition of "default arrangement", for "(3) and (4)" substitute "(3), (4), (6), (7) and (8)".

(3) In regulation 2A([68])—

(a) in paragraph (3), after "charges" insert "and transaction costs";

(b) after paragraph (5), insert—

"(6) For the purposes of this regulation, "transaction costs" has the meaning given in regulation 2(1) of the Occupational Pension Schemes (Charges and Governance) Regulations 2015([69]).".

(4) In regulation 8(1)(a), for "(b) and (c)" substitute "(b), (c) and (d)".

The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013

5. In regulation 29A(2) of the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013([70])—

(a) after sub-paragraph (a), insert—

"(aa) paragraph (1)(aa);";

(b) at the end of sub-paragraph (b), omit "and";

(c) at the end of sub-paragraph (c), insert—

"and

(d) paragraph (1)(cb).".

The Occupational Pension Schemes (Charges and Governance) Regulations 2015

6.—(1) The Occupational Pension Schemes (Charges and Governance) Regulations 2015 are amended as follows.

(2) In regulation 2—

(a) in paragraph (1)—

(i) in the definition of "charges", after sub-paragraph (e), insert—

"(f) costs solely attributable to holding physical assets;";

(ii) after the definition of "charges year", insert—

""commodity" means any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products and energy such as electricity, but not including cash or financial instruments (within the meaning of article 3 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001([71]);";

([66]) S.I. 2005/3378.

([67]) The definition of default arrangement was inserted by S.I. 2015/879, and amended by S.I. 2016/427.

([68]) Regulation 2A was inserted by S.I. 2015/879, and amended by S.I. 2018/988.

([69]) S.I. 2015/879. There are amendments to regulation 2 which are not relevant to these Regulations.

([70]) S.I. 2013/2734. Regulation 29A was inserted by S.I. 2018/233 and amended by S.I. 2018/982 and 2018/988.

([71]) S.I. 2001/544. The definition of financial instrument was inserted by S.I. 2006/3384, and amended by S.I. 2017/488 and 2019/632. There are other amendments to this Article which are not relevant to this instrument.

(iii) after the definition of "jobholder", insert—

""performance fee" means a fee which—

(a) is calculated by reference to the returns from investments held by the scheme, whether in terms of the capital appreciation of those investments, the income produced by those investments or otherwise; and

(b) is not calculated by reference to the value of the member's rights under the scheme;

"physical asset" means an asset whose value depends on its physical form, including land, buildings and other structures on land or sea, vehicles, ships, aircraft or rolling stock, and commodities;";

(b) after paragraph (1), insert—

"(1A) For the purposes of the definition of "charges", the costs solely attributable to holding a physical asset include—

(a) the costs of managing and maintaining the asset;

(b) fees for valuing the asset;

(c) the cost of insuring the asset in question;

(d) ground rent charges, rates, taxes and utilities bills incurred in relation to the asset."

(c) after paragraph (4), insert—

"(5) When a charge under a single charge structure is calculated on a pro rata basis under paragraph (3) and paragraph (6) applies, no account is to be taken of any performance fee charged within the period for which the calculation is made.

(6) This paragraph applies if the performance fee in question is calculated and deducted from the value of the investments to which it relates each time the value of those investments is calculated for the purposes of buying or selling units."

Signed by authority of the Secretary of State for Work and Pensions

Name
Minister of State
Department for Work and Pensions

Date

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the law relating to the administration of occupational pension schemes. Regulation 2 amends the Occupational Pension Schemes (Scheme Administration) Regulations 1996 (S.I. 1996/1715) to require trustees and managers to report on the return on investments their funds have achieved as part of the annual statement required on governance. It also requires the trustees and managers of schemes holding assets worth less than £100 million to compare the charges and transaction costs and the return on investments of their schemes with three other schemes and to assess the extent to which their schemes satisfy administration and governance criteria as part of their value for members assessment under regulation 25(1A) of those Regulations. Regulation 5 makes a consequential amendment to the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (S.I. 2013/2734).

Regulation 3 amends the Register of Occupational and Personal Pension Schemes Regulations 2005 (S.I. 2005/597) to require additional registrable information to be sent to the Regulator for inclusion in the register of occupational pension schemes and personal pension schemes.

Regulation 4 amends the Occupational Pension Schemes (Investment) Regulations 2005 (S.I. 2005/3378) to remove the obligation for the statement of investment principles of a wholly-insured scheme which is also a defined benefit scheme to include any information on the trustees' policy on asset managers.

Regulation 6 amends the Occupational Pension Schemes (Charges and Governance) Regulations 2015 (S.I. 2015/879) to exclude costs attributable to holding physical assets from the charges which are subject to the charge cap imposed under those Regulations and also ensures that no account is taken of certain performance fees in calculating a charge under a single charge structure.

A full regulatory impact statement of the effect that this instrument will have on the costs of business, the voluntary sector and the public sector is available from legislation.gov.uk. A hard copy of the impact assessment may be obtained from the Department for Work and Pensions, Caxton House, Tothill Street, London SW1H 9NA.

Annex D: Keeling schedules

**The Occupational Pension Schemes (Scheme Administration) Regulations 1996
as amended by**

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

From the day after the last day of the first scheme year which ends after 5th October 2021

Additions are underlined, and text to be omitted is struck through

Regulation 23 Annual statement regarding governance

(1) Subject to paragraph (3), the trustees or managers of a relevant scheme must prepare a statement within seven months of the end of each scheme year, and that statement must—

(a) in relation to the default arrangement—

(i) include the latest statement prepared in accordance with regulation 2A (default investment strategy) of the Occupational Pension Schemes (Investment) Regulations 2005 ("the Investment Regulations");

(ii) describe any review undertaken during the scheme year in accordance with paragraph (2) of that regulation;

(iii) explain any changes resulting from such a review; and

(iv) where no review was undertaken during the scheme year, give the date of the last review;

(aa) report on the return on investments (after deduction of any charges or transaction costs relating to those investments), relating to-

(i) each default arrangement; and

(ii) each fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year,

having regard to guidance issued by the Secretary of State under section 113(2A) of the Pension Schemes Act 1993([72]);

(b) describe how the requirements of regulation 24 of these Regulations (requirements for processing financial transactions) have been met during the scheme year;

([72]) Subsection (2A) was inserted by s.38 of the Pension Schemes Act 2015.

(c) in relation to the charges and transaction costs which the trustees or managers are required to calculate in accordance with regulation 25(1)(a) of these Regulations—

(i) state the level of charges and transaction costs applicable to each default arrangement during the scheme year;

(ii) state the levels of charges and transaction costs applicable to each fund which members are (or were) able to select and in which assets relating to members are invested during the scheme year;

(iii) indicate any information about transaction costs which the trustees or managers have been unable to obtain and explain what steps are being taken to obtain that information in the future; and

(iv) ~~explain the trustees' or managers' assessment, in accordance with regulation 25(1)(b), of the extent to which the charges and transaction costs represent good value for members~~ where the trustees or managers are required to assess the extent to which the charges and transaction costs borne by members represent good value for members, explain that assessment;

(ca) include, in relation to the charges and transaction costs which trustees or managers are required to calculate in accordance with regulation 25(1)(a) of these Regulations, an illustrative example of the cumulative effect over time of the application of those charges and costs on the value of a member’s accrued rights to money purchase benefits;

(cb) explain the results of any assessment required under regulation 25(1A);

(d) describe how the requirements of sections 247 and 248 of the 2004 Act (requirements for knowledge and understanding) have been met during the scheme year and explain how the combined knowledge and understanding of the trustees or managers, together with the advice which is available to them, enables them properly to exercise their functions as trustees or managers of the scheme; and

(e) be signed on behalf of the trustees or managers by—

(i) the chair; or

(ii) where the chair has ceased to hold office as chair for any reason and a replacement has not yet been appointed, a person appointed by the trustees or managers to act as the chair in the interim period.

(1A) In complying with the requirements imposed by paragraph (1)(c)(i), (ii) and (ca), the trustees or managers must have regard to guidance prepared from time to time by the Secretary of State.

(2) Where the first statement required to be prepared by the trustees or managers of a relevant scheme in accordance with this regulation relates to a scheme year which ends before 5th April 2016, this regulation applies to that statement as if references to “the scheme year” in sub-paragraphs (a) to (d) of paragraph (1) were to the part of the scheme year starting on 6th April 2015.

(3) Where the circumstances in paragraph (2) apply and the period to be covered by the first statement is three months or less, paragraph (1) does not apply to that

scheme year, but the statement required to be prepared in relation to the following scheme year must include information relating to the period of three months or less of the previous scheme year.

(4) In this regulation "default arrangement" has the same meaning as in the Investment Regulations.

Regulation 25 Assessment of charges and transaction costs

(1) The trustees or managers of a relevant scheme must, at intervals of no more than one year—

(a) calculate—

(i) the charges; and

(ii) in so far as they are able to do so, the transaction costs,

borne by members of the scheme; and

(b) unless the relevant scheme is a specified scheme, assess the extent to which those charges and transaction costs represent good value for members

(1A) If the relevant scheme is a specified scheme, the trustees or managers of the scheme must, at intervals of no more than one year—

(a) assess the extent to which the scheme provides good value for members, and as part of that assessment, assess—

(i) the charges and transaction costs borne by members of the scheme by comparison with the charges and transaction costs borne by members of at least three schemes ("comparison schemes")—

(aa) each of which satisfy the conditions in paragraph (1C)(a), and

(bb) at least one of which satisfies the condition in paragraph (1C)(b),

(ii) the return on investments by comparison with the return on investments relating to—

(aa) the default arrangement, and

(bb) any funds which members are (or were) able to select and in which assets relating to members are invested during the scheme year,

for the three comparison schemes, and in each case the return on investments is to be calculated after deduction of any charges or transaction costs, and

(iii) how the administrative and governance criteria set out in paragraph (1B) are met by the scheme;

(b) in making the assessment required under sub-paragraph (a), have regard to any guidance issued by the Secretary of State under paragraph 2 of Schedule 18 to the Pensions Act 2014 in relation to that assessment.

(1B) The administration and governance criteria set out in this paragraph are—

(a) the promptness and accuracy of core financial transactions;

(b) the quality of the records kept by the trustees or managers;

(c) the appropriateness of the default investment strategy followed by the trustees or managers;

(d) the quality of the scheme's investment governance;

(e) the extent to which the requirements of sections 247 and 248 of the Pensions Act 2004([73]) are satisfied and the trustees or managers have the knowledge, understanding and skills to enable them properly to exercise their functions and to operate the scheme effectively;

(f) the quality of communication with the members of the scheme;

(g) the effectiveness of management of any conflicts of interest that might arise between or among trustees and managers, or between trustees, managers and third parties.

(1C) The conditions in this paragraph are that—

(a) each scheme used as the basis for the comparison is—

(i) an occupational pension scheme which on the relevant date held assets equal to or greater than £100 million; or

(ii) a personal pension scheme, which is not an investment-regulated pension scheme within the meaning of paragraph 1 of Schedule 29A to the Finance Act 2004([74]); and

(b) the trustees believe, on reasonable grounds, that one of the three schemes would be prepared to accept a transfer of members of the specified scheme if the specified scheme is wound up.

(1D) In this regulation—

"core financial transactions" has the same meaning as in regulation 24;

"default arrangement" has the meaning given in regulation 1 of the Investment Regulations;

"default investment strategy" means the default strategy referred to in regulation 2A(1)(c) of the Investment Regulations([75]);

"the Investment Regulations" means the Occupational Pension Schemes (Investment) Regulations 2005([76]);

"specified scheme" means a relevant scheme which, on the relevant date—

(i) held assets worth less than £100 million, and

(ii) has been operating for three or more years;

"relevant date" means the last day of the scheme year preceding the year in which the assessment required by paragraph (1)(b) is made

([73]) 2004 (c. 35). Section 248 of the Pensions Act 2004 was amended by S.I. 2009/1941.

([74]) 2004 (c. 12). Schedule 29A was inserted by paragraph 13 of Schedule 21 to the Finance Act 2006 (c.25).

([75]) Regulation 2A was inserted by S.I. 2015/897.

([76]) S.I. 2005/3378. The definition of "default arrangement" was inserted by S.I. 2015/879 and amended by S.I. 2016/427.

(2) In this regulation (and in regulation 23), “charges” and “transaction costs” have the meanings given in regulation 2(1) of the Occupational Pension Schemes (Charges and Governance) Regulations 2015.

(3) In relation to a scheme which is not a money purchase scheme, this regulation applies only in relation to charges and transaction costs which relate to the provision of money purchase benefits.

The Register of Occupational and Personal Pension Schemes Regulations 2005

as amended by

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

From 5th October 2021 onwards

Additions underlined

Regulation 3 Registrable information

(1) The information prescribed for the purposes of section 60(2)(h) of the Act (registrable information — other prescribed information) is—

(a) the category of the scheme by reference to—

(i) whether the scheme is an occupational or a personal pension scheme,

(ii) whether the scheme is a public service pension scheme,

(iii) whether the scheme or any part of the scheme is protected by a Crown guarantee,

(iv) where the scheme is or is to be registered as a stakeholder pension scheme under section 2 of the Welfare Reform and Pensions Act 1999 (registration of stakeholder pension schemes), whether the scheme is a trust scheme or is established in accordance with regulation 2 of the Stakeholder Pension Scheme Regulations 2000 (manner of establishment);

(b) in the case of a personal pension scheme, the number of members of the scheme on the later of—

(i) the last day of the scheme year which ended most recently, and

(ii) the day on which the scheme became a registrable scheme;

(c) in the case of an occupational pension scheme, the numbers of active members, deferred members and pensioner members of the scheme on the later of—

(i) the last day of the scheme year which ended most recently, and

(ii) the day on which the scheme became a registrable scheme;

(d) in relation to the benefits provided under the scheme—

(i) whether any of those benefits are secured by a contract of insurance or annuity contract issued by an insurance company which provides administration services to the scheme, and

(ii) if so—

(aa) the name and address of the insurance company providing such a contract, and

(bb) the policy number of that contract or the insurance company reference number in relation to that contract;

(da) in the case of an occupational pension scheme which is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 1996, the name of the person for the time being appointed as the chair, within the meaning of regulation 1(2) of those Regulations;

(db) the value of the assets held by the scheme for the purpose of providing benefits to members, calculated on the last day of the scheme year which ended most recently;

(e) the nature of the business of any relevant employer;

(f) in the case of a trust scheme which is in the process of being wound up, the date on which the winding up commenced.

(g) in the case where an occupational pension scheme in respect of which a recovery plan has been prepared under section 226 of the Act begins to wind up during the recovery period, the date on which the winding up commenced.

(h) in the case of an occupational pension scheme which is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 1996, whether the trustees or managers of that scheme have prepared the statement that they are required to prepare in accordance with regulation 23 of those Regulations;

(ha) in the case of a specified scheme—

(i) whether, on the basis of the assessment required by regulation 25(1A) of those Regulations ("value assessment"), the trustees or managers of the scheme consider that the scheme provides good value for members;

(ii) where a value assessment was carried out for the previous year, whether, on the basis of that value assessment, the trustees or managers of the scheme considered that the scheme provided good value for members;

(hb) in the case of a specified scheme where the trustees or managers of the scheme have stated under sub-paragraph (ha)(i) that they do not consider that the scheme provides good value for members—

(i) whether the trustees or managers propose to wind up the scheme and transfer its members into another scheme; and

(ii) if the trustees or managers do not propose to wind up the scheme—

(aa) their reasons for not doing so, and

(bb) what improvements they propose to make to the scheme to ensure that it does provide good value for members;

(i) in the case of an occupational pension scheme in respect of which the requirements of Part 2 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015 apply to one or more of its members, whether the trustees or managers of that scheme have complied with those requirements in respect of each member to whom they apply; and

(j) in the case of an occupational pension scheme where the trustees or managers are approved under section 289 of the Act, the host EEA state as defined under subsection (6) of section 287 of the Act.

(2) The reference in paragraph (1)(f) above to the date on which the winding up of a trust scheme commenced is to be construed in accordance with Part 1 of the Pensions Act 1995.

(3) Where the scheme is a multi-employer scheme, for the purposes of sub-paragraph (1)(e), section 60(4) of the Act shall be modified so as to have effect as if for the words “the employer” in the definition of “relevant employer” there were substituted the words “an employer”.

(4) In this regulation—

“multi-employer scheme” means a trust scheme in relation to which there is more than one employer;

“recovery period” means the period specified in the scheme's recovery plan in accordance with section 226(2)(b) of the Act;

“specified scheme” means an occupational pension scheme which is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 2005 which, on the last day of the scheme year which ended most recently—

(a) held assets worth less than £100 million; and

(b) has been operating for three or more years.

(5) For the purposes of section 60(2)(g)(i) and of this regulation, “scheme year” means—

(a) a year specified for the purposes of the scheme in any document comprising the scheme or, if no year is specified, a period of 12 months commencing on 1st April or on such other date as the trustees select; or

(b) such other period (if any) exceeding six months but not exceeding 18 months as is selected by the trustees—

(i) in connection with the commencement or termination of the scheme, or

(ii) in connection with a variation of the date on which the year or period referred to in sub-paragraph (a) is to commence.

The Occupational Pension Schemes (Investment) Regulations 2005

as amended by

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

From 5th October 2021 onwards

Additions are underlined, and text to be omitted is struck through

Regulation 1 Citation, commencement and interpretation

…

(2) In these Regulations—

…

“default arrangement”, means an arrangement, within the meaning of regulation 3 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015 (default arrangement) which would be a default arrangement within the meaning of that regulation if that regulation were modified as follows—

(a) in paragraph (1)(a) omit “qualifying”, and for “relevant jobholders” substitute “workers”;

(b) in paragraph (2)(b) omit “subject to paragraph (3),”;

(c) omit paragraphs (3) ~~and~~, (4), (6), (7) and (8)[77] and

(d) in paragraph (9)—

(i) in the definition of “relevant date” omit the words after “regulation 1(2)”; and

(ii) omit the definitions of “relevant jobholder” and “staging date”;

…

Regulation 2A Additional requirements in relation to default arrangement

(1) The trustees or managers of a relevant scheme must prepare a statement of the investment principles governing decisions about investments for the purposes of the default arrangement, and that statement must be in writing and must cover at least the following matters—

[77] Amendment to sub-paragraph (c) applies from the date after the end of three months beginning with the last day of the first scheme year which ends after 5th October 2021.

(a) the aims and objectives of the trustees or managers in respect of such investments;

(b) their policies in relation to the matters mentioned in regulation 2(3)(b) and, if that scheme has 100 or more members, regulation 2(3)(c) and (d) in respect of the default arrangement; and

(c) an explanation of how the aims and objectives mentioned in sub-paragraph (a) and the policies mentioned in sub-paragraph (b) (together “the default strategy”) are intended to ensure that assets are invested in the best interests of the group of persons consisting of relevant members and relevant beneficiaries.

(2) The trustees or managers must review both the default strategy and the performance of the default arrangement—

(a) at least every three years; and

(b) without delay after any significant change in—

(i) investment policy; or

(ii) the demographic profile of relevant members.

(3) The trustees or managers must, in particular, review the extent to which the return on investments relating to the default arrangement (after deduction of any charges and transaction costs[78] relating to those investments) is consistent with the aims and objectives of the trustees or managers in respect of the default arrangement.

(4) The trustees or managers must revise the statement prepared in accordance with paragraph (1) after every review unless they decide that no action is needed as a result of the review in paragraph (3).

(5) For the purposes of this regulation and regulation 4A, a person is a relevant member or a relevant beneficiary if assets relating to that member or, as the case may be, that beneficiary (as defined in regulation 4), are invested in the default arrangement.

(6) For the purposes of this regulation, “transaction costs” has the meaning given in regulation 2(1) of the Occupational Pension Schemes (Charges and Governance) Regulations 2015.[79]

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[78] Change to paragraph (3) applies from the date after the end of three months beginning with the last day of the first scheme year which ends after 5th October 2021.

[79] New paragraph (6) applies from the date after the end of three months beginning with the last day of the first scheme year which ends after 5th October 2021.

…

Regulation 8 Modification of regulation 2 in respect of wholly-insured schemes

(1) Where, on the preparation or revision of a statement of investment principles under regulation 2, a scheme is a wholly-insured scheme and the trustees do not consider that it should cease to be such a scheme—

> (a) sub-paragraphs (b), ~~and~~ (c) and (d) of regulation 2(3) shall not apply; and
>
> (b) the statement of investment principles must cover the reasons for the scheme being a wholly-insured scheme.

(2) In this regulation, “wholly-insured scheme” means a trust scheme, other than a stakeholder pension scheme within the meaning of section 1 of the Welfare Reform and Pensions Act 1999 (meaning of “stakeholder pension scheme”), which has no investments other than specified qualifying insurance policies.

(3) For the purposes of paragraph (2), “investments” shall not include—

> (a) cash held on deposit by the trustees or managers pending payment to the insurer or to members of the scheme;
>
> (b) cash held on deposit by the trustees or managers to meet accrued liabilities or administrative expenses; or
>
> (c) any investments arising from voluntary contributions.

The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013

as amended by

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

From the day after the last day of the first scheme year which ends after 5th October 2021.

Additions underlined

Regulation 29A Publishing charges and transaction costs and other relevant information

(1) Where the scheme is a relevant scheme within the meaning of the Occupational Pension Schemes (Scheme Administration) Regulations 1996, the information specified in paragraph (2) and, where that scheme falls within section 35 of the 1995 Act, paragraph (2A) must be made publicly available free of charge on a website in accordance with this regulation.

(1A) Where section 35 of the 1995 Act applies to a scheme which does not fall within paragraph (1), the information specified in paragraph (2B) must be made publicly available free of charge on a website in accordance with this regulation.

(2) The specified information is the information which must be included in the most recent statement prepared under regulation 23 (annual statement regarding governance) of those Regulations in accordance with the following paragraphs of that regulation—

(a) paragraph (1)(a);

(aa) paragraph (1)(aa);

(b) paragraph (1)(c); and

(c) paragraph (1)(ca).

(2A) The specified information is—

(a) the latest statement of investment principles governing decisions about investments prepared for the scheme under section 35 of the 1995 Act; and

[(b) the information which must be included in the most recent document prepared under regulation 12 in accordance with paragraph 30(f) of Schedule 3.[80]]

(2B) The specified information is—

(a) the latest statement of investment principles governing decisions about investments prepared for the scheme under section 35 of the 1995 Act; and

[80] Paragraph (2A)(b) comes into force on 1 October 2020.

[(b) the information which must be included in the most recent document prepared under regulation 12 in accordance with paragraph 30(ca) of Schedule 3.[81]]

(3) Where this regulation applies—

(a) a notification need not be given under regulation 27 in relation to the information on the website where information is given to the person in accordance with paragraph 5B(a) of Schedule 6 (statements of benefits: money purchase and cash balance benefits); and

(b) the trustees or managers of the scheme must have regard to guidance prepared from time to time by the Secretary of State concerning the publication of the information.

(4) Where a person requests the trustees or managers of the scheme to provide the information referred to in paragraph (2), (2A) or (2B) in hard copy form, the trustees or managers of the scheme must give that information to the person in hard copy form only where the trustees or managers are satisfied that it would be unreasonable for that person to obtain it from the website on which it is published.

(5) Where information is required to be given in hard copy form in accordance with paragraph (4), it must be given within two months of the date the request is made.

[81] Paragraph (2B)(b) comes into force on 1 October 2020.

The Occupational Pension Schemes (Charges and Governance) Regulations 2015

as amended by

The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2021

From 5th October 2021 onwards

Additions underlined

Regulation 2 Interpretation

2.—(1) In these Regulations—

"the 1995 Act" means the Pensions Act 1995;

"the 2008 Act" means the Pensions Act 2008;

"the Administration Regulations" means the Occupational Pension Schemes (Scheme Administration) Regulations 1996;

"adviser" is a person described in regulation 11A(3);

"annually" means per charges year;

"arrangement" means an allocation of contributions to—

(a) an investment; or
(b) more than one investment according to a strategy adopted by the trustees or managers;

"charges" means administration charges other than—

(a) transaction costs;
(b) where an order of the court provides for the recovery by the trustees or managers of costs incurred in complying with the order, the amount of those costs;
(c) charges permitted by regulations made under section 24 or 41 (charges in respect of pension sharing costs) of the Welfare Reform and Pensions Act 1999;
(d) winding up costs;
(e) costs solely associated with the provision of death benefits;

(f) costs solely attributable to holding physical assets;

"charges year" means a period of 12 months specified for the purposes of the scheme in any scheme document or, if no such year is specified, a period of 12 months commencing on—

(a) either 1st or 6th April as the trustees or managers may decide; or

(b) if no such decision is made, 1st April;

""commodity" means any goods of a fungible nature that are capable of being delivered, including metals and their ores and alloys, agricultural products and energy such as electricity, but not including cash or financial instruments (within the meaning of article 3 of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001;

"contributing member" is a member of a relevant scheme in relation to whom a contribution is being made to that scheme for the purposes of accruing money purchase benefits;

"contribution", in relation to a member, means a payment made by, on behalf of or in respect of that member;

"contribution percentage charge" has the meaning given in regulation 5(3);

"default arrangement" has the meaning given in regulation 3;

"employer" has the meaning given in section 99 of the 2008 Act;

"executive pension scheme" means a scheme—

(a) in relation to which a company is the only employer and the sole trustee; and
(b) the members of which are either current or former directors of the company and include at least one third of the current directors;

"existing rights charge" has the meaning given in regulation 5(3);

"flat fee charge" has the meaning given in regulation 5(3);

"jobholder" has the meaning given in section 99 of the 2008 Act;

"performance fee" means a fee which—

(a) is calculated by reference to the returns from investments held by the scheme, whether in terms of the capital appreciation of those investments, the income produced by those investments or otherwise; and

(b) is not calculated by reference to the value of the member's rights under the scheme;

"physical asset" means an asset whose value depends on its physical form, including land, buildings and other structures on land or sea, vehicles, ships, aircraft or rolling stock, and commodities;

"qualifying scheme" has the meaning given in section 99 of the 2008 Act;

"qualifying scheme employer" means an employer in relation to whom a scheme is a qualifying scheme in relation to at least one of its jobholders;

"relevant small scheme" means a scheme with fewer than 12 members, where—

(a) all the members are trustees of the scheme and either—
(i) the provisions of the scheme provide that any decision made by the trustees is made by the unanimous agreement of the trustees who are members of the scheme; or
(ii) the scheme has a trustee who is independent in relation to the scheme for the purposes of section 23 of the 1995 Act (power to appoint independent trustees), and is registered in the register maintained by the Authority (as defined in that Act) in accordance with regulations made under subsection (4) of that section; or
(b) all the members are directors of a company which is the sole trustee of the scheme and either—

(i) the provisions of the scheme provide that any decision made by the company in its capacity as a trustee is made by the unanimous agreement of the directors who are members of the scheme; or
(ii) one of the directors of the company is independent in relation to the scheme for the purposes of section 23 of the 1995 Act and is registered in the register maintained by the Authority (as defined in that Act) in accordance with regulations made under subsection (4) of that section;

"service provider" means a person who provides an administration service directly to the trustees or managers of a relevant scheme;

"single charge structure" has the meaning given in regulation 5(2);

"specified scheme" means a relevant scheme in which at least one qualifying scheme employer participates;

"transaction costs" means the costs incurred as a result of the buying, selling, lending or borrowing of investments;

"winding up costs" means the costs of winding up the pension scheme including (but not limited to) the cost of —

(a) legal advice;
(b) tracing, consulting and communicating with members;
(c) advice on exiting investments;
(d) selection of an alternative scheme or investments;

"worker" has the meaning given in section 99 of the 2008 Act;

"writing" includes electronic communication and 'electronic communication' has the meaning given in section 15(1) of the Electronic Communications Act 2000.

(1A) For the purposes of the definition of "charges", the costs solely attributable to holding a physical asset include—

(a) the costs of managing and maintaining the asset;

(b) fees for valuing the asset;

(c) the cost of insuring the asset in question;

(d) ground rent charges, rates, taxes and utilities bills incurred in relation to the asset.

(2) For the purposes of paragraph 1(5) of Schedule 18 to the Pensions Act 2014, "relevant scheme" means—

(a) an occupational pension scheme under which all the benefits which may be provided are money purchase benefits; or

(b) where some but not all the benefits which may be provided under an occupational pension scheme are money purchase benefits, that scheme in so far as it relates to those benefits,

other than a scheme with only one member, an executive pension scheme or a relevant small scheme.

(3) Where, in these Regulations, the circumstances require one or more of the calculations listed in paragraph (4) to be made in relation to a period of less than a charges year, that calculation shall be done on a pro rata basis.

(4) The calculations referred to in paragraph (3) are—

(a) a charge under a single charge structure;

(b) a flat fee charge;

(c) an existing rights charge.

(5) When a charge under a single charge structure is calculated on a pro rata basis under paragraph (3) and paragraph (6) applies, no account is to be taken of any performance fee charged within the period for which the calculation is made.

(6) This paragraph applies if the performance fee in question is calculated and deducted from the value of the investments to which it relates each time the value of those investments is calculated for the purposes of buying or selling units.

Annex E: Statutory Guidance: Value for Money and Consolidation

Please see separate PDF entitled “Annex E: Statutory Guidance: Value for money and consolidation”.

Annex F: Non-exhaustive list of costs and charges

In scope of the default fund charge cap:

Administration costs

- Set-up fees
- Costs of member communication services, e.g. statement costs, website, printing/ posting accounts
- Ongoing costs for running of scheme, e.g. IT, office and staffing costs, data management and record keeping, marketing and distribution
- Scheme-level entry fees; both on entry into, or on transferring in a pre-existing pot
- Scheme-level exit charges
- Banking fees
- Fees and expenses charged in relation to the creation or operation of any funds or collective investment schemes
- Scheme level payments to providers of professional services and other third parties, or fees for related services, e.g. administrators, advisers, actuaries, lawyers, auditors, accountants, compliance and litigation.

Governance and regulation costs

- Registration and regulatory costs and fees
- Fees paid to governance bodies, e.g. trustees, IGCs and others
- Governance charges and expenses, e.g. trustee insurance

Investment costs (except as permitted in relation to physical assets)

- Fund or investment management fees, including payments to investment consultants and fiduciary managers, underlying, separate and in-house fund managers, performance fees, research, engagement and proxy voting advisers
- Ongoing charges for underlying funds in investment portfolio, e.g. fee for holding units in a UCITS, NURS or QIS fund or investment trusts classified as closed-ended investment funds under listing rules
- Ongoing charges for unit-linked contracts of insurance
- Fees (excluding transaction costs) for non-member-initiated switching of funds
- Investment level payments to providers of professional services and other third parties or fees for related services, e.g. investment governance, advisers, audit and legal fees, valuation services, levies, compliance and litigation costs.
- Costs of third party financial guarantees e.g. capital guarantees
- Depositary fees and fees to the custody bank (excluding transaction costs)
- Platform fees

- Unrecoverable VAT
- (private equity) carried interest, unoffset monitoring fees and directors’ fees

Excluded from the default fund charge cap

Transaction costs

- Dealing commission and fees, including payments for other goods and services provided in return, e.g. research
- Transaction taxes, e.g. stamp duty and capital gains tax
- Spreads, e.g. bid-offer on bonds, foreign exchange (and associated costs such as commission)
- Dilution levy, fund-level spreads and the costs resulting from swing pricing
- Other charges embedded in the transaction price, e.g. payments incurred through financial derivative instruments
- Custodian transaction costs ('ticket fees')
- Deductions of expenses or fees from income earned by other transactions relating to the underlying assets, e.g. stock lending, foreign currency exchange
- Physical assets transaction costs e.g. lease renewal fees
- (private equity) unoffset transaction fees, including underwriting fees and success fees

Taxes

- Non-reclaimable withholding taxes on income, dividends and interest

Costs solely attributable to holding physical assets

- Property management and maintenance costs
- Valuation fees
- Void costs
- Insurance
- Ground rent charges
- Rates and taxes

Other exclusions

- Underlying costs of listed companies which are not classified as a closed-ended investment fund under listing rules, e.g. the wages paid to staff in a retail store
- Costs of winding up the scheme
- Costs incurred in complying with a court order
- Permitted charges in respect of pension sharing costs
- Costs solely associated with the provision of death benefits

Annex G: Cost and charges statutory guidance

Department
for Work &
Pensions

Reporting of costs, charges and other information: guidance for trustees and managers of occupational schemes

October 2020

DRAFT STATUTORY GUIDANCE ISSUED PURSUANT SECTION 113(2A) of THE PENSIONS SCHEME ACT 1993.

This guidance is produced for the purpose of consultation.

This updates previous statutory guidance for Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2020.

INDEX OF CHANGES

We have amended the text from the previous guidance in the following paragraphs:

3-4, 10, 14-15, 17-18, 20, 22-23, 31, 33, 34, 36, 44, 51, 53, 56, 58-63, 65, 67, 69, 71-72, 76, 80, 82

We have added the following paragraphs to the previous guidance:

5, 6, 16, 19, 28-30, 32, 37-43, 45, 70 77-79

Contents

Background 95

About this Guidance 95

Expiry or review date 96

Audience 97

When this Guidance should be followed 98

Legal status of this Guidance 99

Compliance with this Guidance 99

Production of an illustration 100

Overview 100

Examples 101

Required elements 104

Optional elements 107

Publication of costs, charges and other information 108

Required elements 108

Storage or printing of the information 112

Optional elements 112

[the page numbers in this table will apply to the published document. They do not apply to the page numbers in this annexe]

Background

About this Guidance

1. From 6 April 2018 the Occupational Pension Schemes (Administration and Disclosure) (Amendment) Regulations 2018 ("the 2018 Regulations") introduce requirements relating to the disclosure and publication of the level of charges and transaction costs by the trustees and managers of a relevant scheme[82].
2. The 2018 Regulations amend the Occupational Pension Schemes (Scheme Administration) Regulations 1996[83] ("the Administration Regulations") and the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013[84] ("the Disclosure Regulations") to reflect these new requirements.
3. From 1 October 2019 the Pension Protection Fund (Pensionable Service) and Occupational Pension Schemes (Investment and Disclosure) (Amendment and Modification) Regulations 2018 (referred to in this Guidance as "the Amending Regulations") introduce requirements relating to the disclosure and publication of the Statement of Investment Principles, alongside other related material. The Amending Regulations amend, amongst other Regulations, the Disclosure Regulations and the Occupational Pension Schemes (Investment) Regulations 2005[85].
4. Some of the duties inserted by the 2018 Regulations and the Amending Regulations, require trustees and managers to have regard to guidance issued from time to time by the Secretary of State in complying with the relevant requirements of those Regulations.
5. The Occupational Pensions Schemes (Investment and Disclosure) (Amendment) Regulations 2019 ("the 2019 Regulations") introduce requirements relating to the disclosure and publication of the Statement of Investment Principles and other

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[82] Relevant scheme is defined in regulation 1(2) of the Administration Regulations - http://www.legislation.gov.uk/uksi/1996/1715/regulation/1 - see paragraph 12 for more information about the scheme types which are excluded from the definition of "relevant scheme".

[83] http://www.legislation.gov.uk/uksi/1996/1715

[84] http://www.legislation.gov.uk/uksi/2013/2734

[85] http://www.legislation.gov.uk/uksi/2005/3378

related material for non-relevant schemes. The 2019 regulations amend the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 to reflect these new requirements

6. The Occupational Pension Schemes (Administration, Investment, Charges and Governance) (Amendment) Regulations 2020 ("the 2020 Regulations") introduce requirements relating to the reporting of investment performance and the assessment of value for members offered by a relevant scheme.
7. Apart from the elements described in this Guidance it is up to trustees and managers of occupational pension schemes to decide how, consistently with their legal obligations, to implement the requirements of the legislation based on the needs of their scheme's membership.

Expiry or review date

8. This Guidance will be reviewed as a minimum every 3 years, from the date of first publication, and updated when necessary.
9. This document makes reference to a range of assumptions used in Actuarial Standards Technical Memorandum 1 (AS TM1) issued by the Financial Reporting Council (FRC), and used by the Financial Conduct Authority (FCA) in the Conduct of Business Sourcebook (CoBS).
10. In broad terms, the intention is to allow schemes to use the current assumptions set out for the production of illustrations in:
    - CoBS[86] as at 6 April 2019, as amended by FCA Handbook Notice 51[87]; and
    - version 4.2 of AS TM1, published in October 2016[88]. Subsequent references to CoBS and AS TM1 in this Guidance should be taken to refer to these versions.
11. When relevant assumptions in AS TM1 or in CoBS are updated, our intention is to consult in good time to ensure that, where appropriate, alignment between this Guidance, AS TM1 and CoBS is maintained.

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[86] CoBS 13 Annex 2 Projections

[87] FCA Handbook Notice 51 confirmed that the FCA Board had approved revised assumptions for projections following consultation in Quarterly Consultation Paper No 18 (CP 17/32). These changes, which are listed in pages 113-115 of the CP17/32, will come into effect from 6 April 2019.

[88] Actuarial Standard Technical Memorandum: AS TM1 Current Versions

12. The Guidance does not take precedence over, or try to direct, CoBS or AS TM1 in relation to the production of other projections.

13. When we review the Guidance, we will also consider, for possible inclusion, lessons from established and emerging best practice and user testing of the way in which cost and charge information is presented.

Audience

14. This Guidance is for trustees and managers of relevant occupational pension schemes (broadly, money purchase schemes and non-money purchase schemes in relation to their money purchase benefits, in both the accumulation and decumulation phases). Trustees and managers of non-relevant schemes may also find this Guidance helpful when meeting their publication requirements.

15. None of the publication requirements of the 2018 Regulations or the 2020 Regulations apply to:

    - Schemes where the only money purchase benefits offered arise from Additional Voluntary Contributions (AVCs);
    - Relevant small schemes[89];
    - Executive pension schemes[90];
    - Schemes that do not fall within paragraph 1 of Schedule 1[91] (description of schemes) to the Disclosure Regulations – most commonly single member schemes, schemes which are not tax registered and schemes which provide only death benefits; and
    - Public service pension schemes, as defined by section 318 of the Pensions Act 2004[92].

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[89] Also known as 'Small Self-Administered Schemes (SSASs)', a relevant small scheme is an occupational scheme with fewer than 12 members where all the members are trustees of the scheme or all the members are directors of a company which is the sole trustee of the scheme

[90] Executive Pension Scheme means an occupational scheme in relation to which a company is the only employer and the sole trustee; and the members of which are either current or former directors of the company and include at least one third of the current directors

[91] http://www.legislation.gov.uk/uksi/2013/2734/schedule/1

[92] In practice, we are aware of no such schemes which meet this definition and offer money purchase benefits other than those attributable to AVCs.

16. In addition, the publishing requirements in the Amending Regulations and 2019 Regulations do not apply to:

- Schemes to which the 2018 Regulations do not apply;
- Schemes with fewer than 100 members;
- Schemes established under an enactment or guaranteed by a public authority; and
- Schemes not established under a trust.

When this Guidance should be followed

17. The amendments made by the 2018 and the 2020 Regulations require occupational pension schemes which offer money purchase benefits (subject to the small number of exceptions above at paragraph 15) to, among other things:

    - provide an illustrative example of the cumulative effect of costs and charges[93] incurred by the member as part of the Chair's Statement; and
    - publish that and certain other parts of the Chair's Statement (or all, if a scheme wishes to do so) on a website for public consumption.

18. The amendments made by the Amending Regulations require trustees of schemes with 100+ members offering money purchase benefits (subject to the exceptions in paragraph 16) to, among other things:

    - from 1 October 2019, publish the Statement of Investment Principles ("SIP");
    - from 1 October 2020, publish an implementation statement on how they acted on the SIP.

19. The amendments made by the 2019 Regulations require trustees of pension schemes with 100+ members not offering money purchase benefits (subject to the small number of exceptions at paragraph 16) to:

    - by 1 October 2020, publish the Statement of Investment Principles ("SIP");
    - by 1 October 2021, publish an implementation statement on how they acted on the voting and engagement sections of the SIP.

[93] 'Transaction costs' and 'charges' are defined in the Occupational Pension Schemes (Charges and Governance) Regulations 2015 - http://www.legislation.gov.uk/uksi/2015/879

20. Trustees and managers of occupational pension schemes must have regard to this Guidance, where applicable, on meeting these legislative requirements.

Legal status of this Guidance

21. This statutory Guidance is produced under section 113(2A) of the Pension Schemes Act 1993 ("the 1993 Act").
22. This Guidance replaces the previous Reporting of costs, charges and other information: guidance for trustees and managers of relevant occupational pension schemes statutory guidance, which was published in September 2018, and was issued under section 113(2A) of the 1993 Act.

Compliance with this Guidance

23. For occupational pension schemes, The Pensions Regulator ("TPR") monitors compliance with the legislation and provides guidance about what employers and people running schemes need to do. The Department for Work and Pensions ("DWP") is responsible for answering questions about the policy intentions behind the legislation. Neither DWP nor TPR can provide a definitive interpretation of the legislation which is a matter for the courts.
24. Trustees and managers and service providers should consider the Regulations to determine whether the new requirements apply to them, taking further advice where necessary.
25. Where the trustees or managers do not comply with a relevant legislative requirement of the Administration Regulations or the Disclosure Regulations by virtue of a failure to have regard, or to have proper regard, to this Guidance, the Pensions Regulator may take enforcement action which includes the possibility of a financial penalty.
26. Enforcement of Part V of the Administration Regulations, including the production and content of the Chair's Statement, is currently provided for in Part 4 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015[94]. Regulation 5 of the Disclosure Regulations sets out the penalties for failure to comply with any other requirement under those Regulations, including any failure to publish costs, charges and other relevant information in accordance with regulation 29A of those Regulations.

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[94] http://www.legislation.gov.uk/uksi/2015/879

Production of an illustration

Overview

27. This section of the Guidance sets out the matters to which trustees and managers of relevant schemes must have regard when producing an illustration in accordance with regulation 23(1)(ca) of the Administration Regulations, as inserted by the 2018 Regulations.
28. The purpose of the illustrations is to communicate simply and clearly to members the impact of cost and charges on their pension pots, and the compounding effect of small differences in charges over the long term.
29. To show the effect of a range of charging levels, the illustrations should identify the default arrangement(s), lowest charging and highest charging self-select fund in which members are invested, and highlight to scheme members the difference in the compounding effect of the charges of each respective fund in which assets relating to members are invested during the scheme year.
30. **If the charging levels or the defaults vary by employer**, then each part of the scheme with a different default or charging levels should be treated as a separate scheme, and the three illustrations described above produced. This is to ensure that each employee who is interested can see the compounding effect of costs and charges on their default arrangement and a sample of other funds, regardless of the pension scheme's pricing model.
31. Trustees and managers should present the costs and charges typically paid by a member as a figure in pounds, or pounds and pence.
32. Illustrations should be produced for the following sections of the scheme:
    - Default/s (schemes with more than one default, or a default whose price varies with employer, should produce an illustration for each);
    - Lowest charging self-select fund, by employer;
    - Highest charging self-select fund, by employer.
33. The illustration should be produced having regard to the Guidance, providing realistic and representative figures for the following elements:

- savings pot size;
- contributions;

- real-terms investment return, gross of costs and charges;
- adjustment for the effect of costs and charges; and
- time.

34. The examples below do not seek to be wholly prescriptive. Schemes are free to go further in the disclosure of additional illustrations based on the characteristics and diversity of their scheme membership, the fund or arrangement offerings where they feel an inclusion of these characteristics will improve the quality of the illustration.

35. When trustees and managers are deciding how best to present this data, they should consider the needs and preferences of their membership. Schemes are free to use a variety of different approaches which they believe to be more suitable for particular groups of members.

Examples

36. An example of how an illustration can be prepared which is consistent with this Guidance is shown below. This example uses assumptions which are based on CoBS as at 6 April 2019.

Projected pension pot in today's money ----						
	Default arrangement		Highest Charging Employee Self Select Fund		Lowest Charging Employee Self Select Fund	
Years	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted
1						
3						
5						
10						
15						
20						
25						
30						
35						
40						

Figure 1.

Notes

1. Projected pension pot values are shown in today's terms, and do not need to be reduced further for the effect of future inflation.
2. The starting pot size is assumed to be £10,000 and contributions are £1000 per year.
3. Inflation is assumed to be 2.0% each year.
4. Contributions are assumed from age 22 to 68 and increase in line with assumed earnings inflation of 2.5% each year
5. Values shown are estimates and are not guaranteed
6. The projected growth rate for each fund or arrangement are as follows:

   Default arrangement: 2.5% above inflation
   Highest Charging Employee Self Select Fund: 2% above inflation
   Lowest Charging Employee Self Select Fund: 1% above inflation

37. An example of how an illustration can be prepared for schemes with **multiple defaults or variable charges** which is consistent with this Guidance is shown below.

Projected pension pot in today's money						
	Default – Employer Group A		Highest Charging Employee Self Select Fund – Employer Group A		Lowest Charging Employee Self-Select Fund – Employer Group A	
Years	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted
1						
3						
5						
10						
15						
20						
25						
30						
35						
40						

Projected pension pot in today's money						
	Default – Employer Group B		Highest Charging Employee Self Select Fund – Employer Group B		Lowest Charging Employee Self-Select Fund – Employer Group B	
Years	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted	Before charges + costs	After all charges + costs deducted
1						
3						
5						
10						
15						
20						
25						
30						
35						
40						

Figure 2.

38. This simple example is a scheme with only two default pricing structures. When producing the illustrations all defaults offered by the scheme must be included.
39. In relation to the self-select fund this example is of a typical scheme with variable charges which offer all the self-select funds at standard prices, less an employer specific discount. The identity of the lowest charging and highest charging self-select fund will typically, but not always, remain unchanged with the employer.
40. All members must be able to identify which employer group they are in, from their Annual Benefit Statement.
41. Members who didn't make an active choice which fund they have been placed in by their employer are bearing the costs of being invested in that respective fund. Therefore, it is essential that they are able to calculate what they paid in costs over a saving lifetime as a result. Members of schemes with multiple defaults or variable charges have the same right to this information as those with a single price for employees of all employers.
42. This simple example is a scheme with two default pricing structures. All defaults offered must be included in the illustrations.
43. However, the illustrations for each respective employer group do not need to be presented alongside each other in the Chair's Statement. Alternatively, Trustees

can provide members with a bespoke link to the illustration for their specific employer group.

Required elements

Savings pot size

44. Schemes should use one or more typical savings pot sizes to illustrate the long-term effects of charges. These sizes should be broadly representative of the actual pot sizes of members of the scheme. For example, if trustees and managers chose to use just one pot size, the median pot size in the scheme should be used as a benchmark by which to set the value of the savings pot used in the illustration.
45. For schemes with multiple defaults or variable charges this should simply be a median across the whole scheme rather than producing a median for each default, or for each employer using the scheme.
46. The pot size assumption should be clearly stated.

Contributions

47. Many members will be contributing to the pension scheme, and it is, therefore, often most meaningful for the illustration to show the effect of further contributions to the scheme. Contributions will generally increase in nominal terms, as they are typically a percentage of salary. Where salaries increase faster than inflation, there will be real-terms growth in contribution levels.
48. Where trustees and managers include further contributions to the scheme, the assumed initial future contribution level should be broadly representative of the overall level of contributions (including employer and employee contributions, and tax relief) and should be stated.
49. Where the product is being used for flexi-access drawdown, one or more expected representative future withdrawal rates should be assumed.
50. Future contribution level increases may currently be assumed to be zero in real (inflation-adjusted) terms, unless statute, scheme provisions or recognised practice require otherwise.
51. Real-terms contribution growth of 1.5% or more, taking into account expected real terms salary increases, may alternatively be assumed.

52. Where it is both disproportionately burdensome for schemes to show the effect of future contributions, *and* the scheme features no charges levied on contributions, trustees and managers may assume that no further contributions to the scheme will be made. This assumption should also be stated. Where the scheme levies a charge of any kind on contributions, at least one illustration including contributions should be shown.

Real-terms investment return gross of costs and charges

53. In line with AS TM1, we expect the real-terms investment return to take account of the expected returns, from the current and anticipated future investment strategy of each fund or arrangement over the period to the retirement date.
54. Alternatively, trustees and managers may, if they wish, use as a basis the intermediate rate real-terms investment return assumption currently permitted by CoBS.
55. An unrealistic expected rate of return should not be presented to the member, as this could distort the compounding effect of costs/charges. Schemes therefore should not use assumed rates of real terms investment returns gross of costs and charges which are higher than both those set out in CoBS or for AS TM1.
56. Both AS TM1 and CoBS refer to a category of costs named ‘dealing costs’. The CoBS investment return assumption is gross of charges, but the charges do not include dealing costs[95]. For schemes not subject to FCA rules on projections, the AS TM1 nominal investment return assumption is the ‘accumulation rate’ – the expected returns before the deduction of charges and other expenses – but again those charges and expenses exclude any dealing costs[96].
57. Neither the FRC nor the FCA define dealing costs, but for the purposes of producing these illustrations this Guidance treats them as equivalent.
58. Therefore, if the current CoBS investment return assumption is used, a maximum gross real-terms return of 3% plus the transaction costs is permitted.
59. If AS TM1 is used, a maximum gross investment returns of the ‘accumulation rate’ plus the level of transaction costs but minus the ‘inflation rate’ is permitted.
60. For the assumed level of transaction costs, see paragraph 63.

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[95] CoBS 13 Annex 2 paragraph 2.6 (1) and (2)

[96] C2.4 and C2.9 of Actuarial Standard Technical Memorandum 1

61. The real-terms investment return assumption only needs to be shown for each fund or arrangement for which an illustration is provided.

Adjustment for the effect of costs and charges

62. The effect of charges should be determined by an adjustment inclusive of all the charges, including performance fees, *and* transaction costs, which will have been taken from a member's pot.

63. The transaction costs, as defined in regulation 2(1) of the Occupational Pension Schemes (Charges and Governance) Regulations 2015, should be based on an average of the previous 5 years' transaction costs or, where data is available for less than 5 years, an average of transactions costs over the years for which data is available.

64. The charges (similarly defined in regulation 2(1) of the Charges and Governance Regulations) should be forward-looking and take into account all of those a client will, or may, expect to be taken after investment into the product. The percentage rate (or pound amount, in the case of flat fees) used should be stated.

65. Similarly, any change in flat fee in future should be taken into account. Where this is set to increase in line with inflation a figure of 2.0% (for Consumer Prices Index) or 3.0% (for Retail Prices Index) can be used.

66. Where trustees and managers choose to report the transaction costs associated with entering, exiting and switching between funds or arrangements, they should also show these effects in the illustration.

67. Where the scheme offers funds or arrangements set at a range of different charges/total charge and cost levels, trustees and managers should again use a representative range of charges and costs, illustrating the default(s), lowest and highest charging default(s) and self-select funds for each employer or group of employers.'. **It is not necessary to include every individual fund or arrangement offered by the scheme in the illustration.**

Time

68. The illustration should show the cumulative effect of the charges and transaction costs on the value of a typical member's savings pot over time. This should reflect the approximate duration that the youngest scheme member enrolled has saving until they reach the scheme's Normal Pension Age set out in scheme rules.

69. Trustees and managers are only expected to present one starting point as a minimum. However, if the presentation method allows this to be easily understood, a scheme may also choose to present additional starting points

depending on the generational demographic of the scheme membership. Trustees and managers should seriously consider presenting alternate start points if the level of costs and charges varies significantly by age – for example if younger members' contributions are invested in a low-cost allocation of assets, but those members pay significantly more the closer they are to retirement.

Optional elements

70. Trustees may choose to provide additional illustrations where they believe these would be useful for members – for example for different time periods or contribution rates.

71. They may also choose to add extra information to the illustration and to present data in a more disaggregated format.

72. Examples of additional information trustees and managers may provide include:

    - historic performance data about the funds or arrangements in which members are invested (although it should be made clear that this is no guide to the future);
    - future charges data, if charges are expected to change;
    - percentage of gross investment returns lost over time;
    - percentage of the pot lost to costs and charges compared with a situation where no costs and charges were incurred. Trustees should provide an explanation of 'negative transaction costs').

73. Examples of greater disaggregation which may be provided include:

    - a breakdown of charges into investment and administration costs;
    - a breakdown of transaction costs – for example into explicit costs (such as broker commission, settlement fees, and custody ticket fees) and implicit costs (slippage).

74. Where this additional or disaggregated information is provided, trustees and managers should carefully consider whether they believe that members would benefit from the information and whether it would prove distracting.

75. Provision of data in a more disaggregated form does not remove the expectation to also display it in aggregated form.

Publication of costs, charges and other information

76. This section of the Guidance sets out the matters to which trustees and managers of relevant schemes must have regard when publishing information under regulation 29A of the Disclosure Regulations, as inserted by the 2018 Regulations, and amended by the Amending Regulations, the 2019 Regulations and the 2020 Regulations. Trustees and managers of non-relevant schemes may also find this guidance helpful.

Required elements

Presenting the information

77. The Statement of Investment Principles, the Chair's Statement (inclusive of charges and transaction cost information, value for money assessment and default SIP), and the relevant section of the Annual Report (the implementation statement) do not necessarily have to be produced as a single web-page or PDF document.
78. The information under regulation 29A can be published over a number of pages. When circulated in physical print the Chair's Statement can then be a collation of these pages.
79. An example of how the documents in the annual report and accounts that can be presented as a series of linked web-pages or PDF documents which is consistent with regulation 29A is below:

[Figure 3 - illustration of a document chain which is consistent with Regulation 29A]

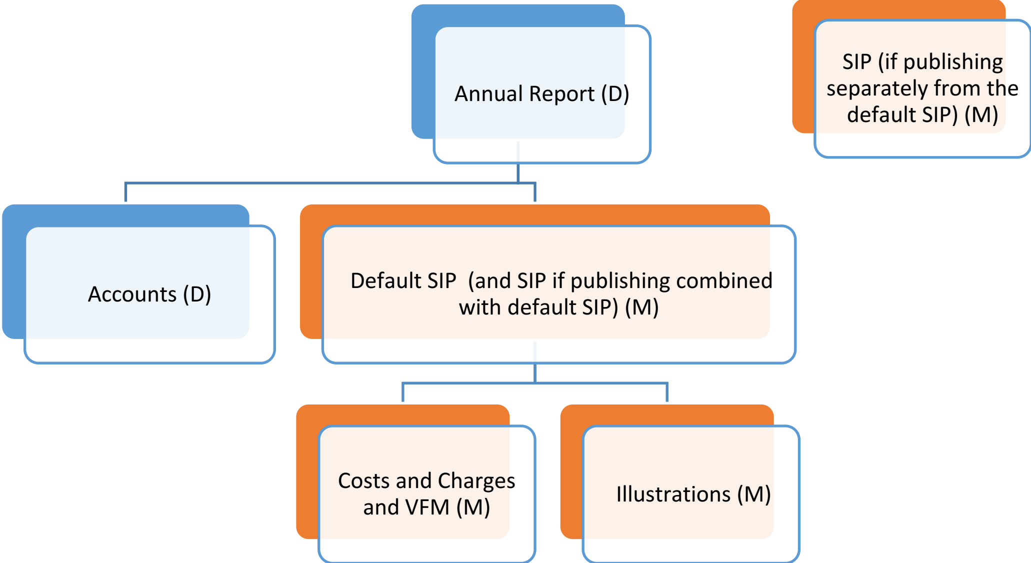

Illustration Notes

1. Figure 3 depicts a flow chart showing how the documents can be presented.
2. At the top of the flow chart is a box labelled ‘Annual Report’.
3. Flowing out of this box is a box labelled ‘Accounts’ and a separate box labelled ‘Default SIP (and SIP if publishing combined with default SIP)’.
4. This illustrates that trustees can provide a link to the Accounts and Default SIP from their Annual Report and present them separately.
5. Flowing out of the box labelled ‘Default SIP (and SIP if publishing combined with default SIP)’ are two additional boxes, one labelled ‘Costs and Charges and VFM’ and another labelled ‘Illustrations’.
6. This illustrates that trustees can provide a link to their costs and charges and VFM information and the compounding illustrations from their Default SIP and present them separately.
7. Directly to the right of the flow chart is a box labelled ‘SIP (if publishing separately from the default SIP)’.
8. This is to illustrate the SIP can be presented separately from the default SIP.
9. Collectively all the documents referenced in the separate boxes of the flow chart are the **Annual Report and Accounts**.

10. The boxes labelled ‘Default SIP (and SIP if publishing combined with default SIP)’, ‘Costs and Charges and VFM’, ‘Illustrations’ and ‘SIP (if publishing separately from the default SIP)’ all have an additional label (M).
11. (M) stands for ‘Mandatory publishing requirement’. All boxes with this label represent documents which collectively are the published parts of the **Chair’s Statement.**
12. The boxes labelled ‘Annual Report’ and Accounts’ have an additional label (D).
13. (D) stands for ‘Discretionary publishing requirement’. This illustrates that there is no legal requirement to publish the documents labelled (D).

Finding and accessing the information

80. Whether produced as one document or separated out, the Statement of Investment Principles, the relevant sections of the Chair’s Statement (inclusive of charges and transaction cost information) and the relevant section of the Annual Report (the implementation statement) must be published on a publicly available website. The information should be published in a manner which allows for the content to be indexed by search engines:
    - if published on the scheme’s or employer’s website, it should not include text which prevents the page from being indexed, and it should be linked to other pages which are found by web search engines;
    - if published via another website – for example, via a social media site, a blogging tool or a repository offered by a search engine provider – appropriate boxes should be selected to ensure that the document is public and can be indexed.
81. Persons wishing to view the information should not be required to do so by:
    - entering a specific user name and/or a specific password;
    - providing any other personal information about themselves.
82. The Disclosure Regulations also require that a specific web address for the location of the published materials on the internet be included in a member’s Annual Benefit Statement. The web address should be appropriately titled so that members can readily re-type it into a web browser, and should clearly describe the information to be found at the location.

Needs of disabled people

83. Trustees and managers should satisfy themselves that they have adequately taken account of the needs of disabled people in publishing the Statement of

Investment Principles, and relevant sections of both the Chair's Statement, and the Annual Report.

84. Examples of factors they should take into account include, but are not limited to:

- whether screen reading software used by visually impaired and blind people can read the content and in a logical sequence;
- whether the text can be enlarged, and whether the contrast in the pages is adequate so it can read by visually impaired people;
- whether the text is simply and clearly written for the benefit of cognitively-impaired users.

85. Standards which trustees and managers may wish to take account of, in verifying that the content takes account of the requirements of disabled people are:

- The web content accessibility guidelines (WCAG) 2.0[97], published by the Web Accessibility Initiative[98], established by the World Wide Web Consortium (W3C);
- BS 8878:2010 Web accessibility. Code of practice, published by the BSI Group.

86. Section 29 of the Equality Act 2010[99] makes it unlawful for service providers to discriminate against people with disabilities. The "Services, public functions and associations: statutory code"[100] published by the Equality and Human Rights Commission to accompany the Act highlights that websites may in themselves constitute a service covered by the Act, for example, where they are delivering information to the public.

87. Although this section of the Guidance is about publishing information, the attention of trustees and managers is drawn to new regulation 29A(4) of the Disclosure Regulations concerning the provision of information in hard copy. Where the person has a disability which means that they are less able to access information on a website, this should be a key factor in deciding to provide that information in a different format.

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[97] http://www.w3.org/TR/WCAG20/

[98] http://www.w3.org/WAI/

[99] https://www.legislation.gov.uk/ukpga/2010/15/section/29

[100] https://www.equalityhumanrights.com/sites/default/files/servicescode_0.pdf

Storage or printing of the information

88. The Statement of Investment Principles, and the relevant sections of both the Chair’s Statement and the Annual Report, whether published on a single page or across more than one page, should be published on a webpage in a way which enables the information displayed to be printed by the reader using widely used web browsers, using the menus available via the browser or functionality on the page itself.

89. In addition, the webpage on which the information is displayed should be such that the Statement of Investment Principles and any relevant sections of both the Chair’s Statement and the Annual Report should be capable of being downloaded and stored using a modern web browser, again either via the browser menus or the page’s functionality.

Optional elements

90. Pension schemes may additionally wish to publish the Statement of Investment Principles, and relevant sections of both the Chair’s Statement and the Annual Report in other locations, such as on the password-protected online servicing sections of their website. However, this does not remove the requirement to publish the information online in such a way that all can find the information without registration or entering any personal details.