

New DC Code of Practice published for consultation

A. Overview

1. On 24th November, 2015, the Pensions Regulator published for consultation its draft Code of Practice 13: Governance and Administration of Occupational DC Trust-based Schemes (the “draft New Code”).
2. Code of Practice 13 (the “Old Code”) took effect on 21st November, 2013, along with guidance and the Regulator’s compliance and enforcement policy (together the “DC framework”). Since November 2013 there have been significant developments in the legislation governing occupational DC schemes. In particular, the DC framework does not reflect the following changes that took effect on 6th April, 2015:
 - 2.1 the new quality standards and associated governance measures,
 - 2.2 the restrictions on charges that may be levied on members in a default arrangement used for auto-enrolment, and
 - 2.3 the new flexible access options available when a member has reached age 65.
3. The draft New Code completely overhauls the Old Code and is 20 pages shorter. References to the Regulator’s 31 quality features have been removed from the Old Code on the basis that these are now “well established”.
4. The draft New Code distinguishes between legal requirements and the Regulator’s expectations. For the former, it says “the law requires ...”, while for the latter it says “we expect ...”. This replaces the use of “must”, “could” and “should” in the Old Code. Respondents are asked to comment on whether they agree with this approach.
5. As the draft New Code notes, Codes of Practice are not statements of the law and there is no direct penalty for failing to comply with them. But when determining whether legal requirements have been met, a court or tribunal must take any relevant provisions of a Code of Practice into account.
6. As with the Old Code, the draft New Code will apply to all occupational trust-based schemes with 2 or more members which offer money purchase benefits. This includes:
 - 6.1 money purchase AVCs within occupational DB schemes, and
 - 6.2 money purchase benefits with a DB underpin.
7. The draft New Code will not apply to:

- 7.1 schemes providing DB benefits only or to DB benefits in hybrid schemes, or
 - 7.2 work-based personal pensions, stakeholder schemes or other contract-based schemes.
8. The Code covers the following areas:
 - 8.1 the trustee board,
 - 8.2 scheme management skills,
 - 8.3 administration,
 - 8.4 investment governance,
 - 8.5 value for members (which the Regulator says is indistinguishable from the FCA’s preferred description of “value for money”), and
 - 8.6 communicating and reporting.
 8. Once finalised, the draft New Code will be supported by guidance that the Regulator intends to publish in draft in “Spring 2016”. It is not clear whether the Regulator will publish a new compliance and enforcement policy.
 9. The draft New Code, on which comments are invited by 29th January, 2016, is on the Regulator’s [website](#).

B. The Trustee Board

1. As in the Old Code, the draft New Code says it expects trustees to act honestly, with integrity, competence and capability, and financial probity, including in matters that arise outside their trusteeship. A new expectation is that professional trustees should be financially sound, not experiencing severe trading difficulties, and have indemnity insurance.
2. So far as the new legislative requirement to appoint a chair of the trustee board is concerned, although the legislative timescale for appointment is within 3 months of an existing chair resigning or being removed, the Regulator expects trustee boards to treat this timescale as a longstop and to try to appoint a chair as quickly as possible.
3. It expects trustee boards to have a “robust and documented” process in place for appointing a chair and that the process will consider the leadership qualities of candidates and their ability to drive good practice within the scheme.

C. Scheme Management skills

1. The Regulator says it expects trustee boards to spend

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an “appropriate” amount of time running their scheme, which will depend on:

- 1.1 the size of the scheme (or section of the scheme offering money purchase benefits),
 - 1.2 the complexity of the scheme rules and structure, and
 - 1.3 the complexity of any particular issues affecting the scheme.
2. So far as **managing risk** is concerned, as with the Old Code the Regulator expects trustee boards to record in a risk register the risks they identify, their evaluation of each risk, and how they are managing it. It also expects trustees regularly to review and monitor their exposure to both new and existing risks, and to keep their risk register up-to-date, including having plans with target dates for mitigating or closing risks.
3. It expects trustees regularly to discuss key risks and issues, and the extent to which the schemes meet the standards set out in the draft New Code.

Comment: The example risk evaluation model in the Old Code has been removed.

4. So far as **trustee knowledge and understanding** is concerned, the Regulator expects the trustee board as a whole to possess or have access to, and maintain, the knowledge and understanding necessary properly to run the scheme and ensure sufficient standards of governance and administration.
5. As well as having a working knowledge of the rules relating to their scheme, the Regulator expects the trustee board to have a working knowledge and understanding of any **policies** in place, or **practices** that have been set by precedent, which may not be explicitly set out in the trust deed and rules (the example given is a policy limiting the number of uncrystallised fund pension lump sums a member can take within a given period of time).
6. The Regulator expects trustee boards regularly to review the appropriateness and suitability of any such policies, practices and relevant scheme rules.
7. The Regulator notes that trustee training may need to be scheme specific on occasions, and timely relative to the scheme lifecycle issues being faced by the trustees. It expects trustees to have training and development plans in place, and to maintain them.

Comment: We can provide customised trustee training to clients on legal issues to help comply with the trustee knowledge and understanding requirements. Please get in touch with your usual pensions contact here for more information.

8. So far as **appointing and managing relations with advisers and service providers** is concerned, the Regulator expects trustees to be able to demonstrate the ability effectively to manage commercial

relationships. In particular, it expects trustees to be familiar with, and understand the impact of, the terms and conditions of contracts with service providers, including:

- 8.1 the scope of services being provided,
 - 8.2 the cost of those services and the basis for calculating them,
 - 8.3 the arrangements, including notice periods, any fees or penalties, and procedures for releasing relevant information to trustees and new advisers, if the service provider is changed, and
 - 8.4 any limits on liability.
9. The Regulator expects a trustee board’s breadth of knowledge and understanding to enable it fully to understand any advice received, and to be able to challenge this and understand how it impacts on any decisions for which the trustees are legally responsible.

10. It expects trustees regularly to monitor the performance of service providers, and have controls in place to accommodate that monitoring, including requiring sufficient reports and relevant information from service providers to allow the trustees to be confident that the service providers are performing as expected. The Regulator expects this information to be analysed and regularly discussed at trustee board meetings. Trustees should regularly communicate with representatives from service providers carrying out key elements of the day-to-day running of the scheme and, where appropriate, invite them to attend trustee board meetings.

Comment: These expectations are largely in the Old Code, so compliance should be “business as usual” for trustee boards.

11. The Regulator expects trustees to work with and help **employers** to understand and carry out their responsibilities in relation to the pension scheme, with the processes and mechanisms that the employer uses to provide information being reviewed regularly.
12. Again, the section of the draft New Code dealing with **conflicts of interest** follows closely the Old Code, requiring internal controls that include as a minimum:
- 12.1 a written policy setting out the trustee board’s approach to dealing with conflicts,
 - 12.2 a register of interests (which should be reviewed at every regular board meeting),
 - 12.3 declarations of interests and conflicts made on the appointment of all trustees and advisers, and
 - 12.4 contracts and terms of appointment to require advisers and service providers to operate their own conflicts policy and disclose all conflicts to the trustee board.

Comment: The warning in the Old Code about sharing advisers (for example benefit consultants) with the employer has disappeared.

D. Administration

1. The Regulator expects the trustee board to consider administration as a “substantive” item at every regular meeting.

Comment: This is a new “expectation”.

2. The Regulator notes that trustee boards remain accountable for the quality of the scheme administration and all legal requirements that relate to it and so expects trustee boards to have a clear understanding of the scope of administrator responsibilities and the tasks which the administrator carries out.
3. There should be regular information or stewardship reports from administrators, allowing trustees effectively to monitor performance and ensure that all tasks delegated to the administrator are being carried out to a standard which allows the trustee board to be satisfied that, at a minimum, it can meet its legal obligations.
4. The Regulator expects trustee boards to adopt procedures to check that whoever carries out the scheme administration has the appropriate training and expertise. It says that trustees should have procedures in place to enable a “continuous and consistent service” in the event of a change of administrator personnel, or administration provider. For many schemes this is likely to include a manual that sets out the procedures to follow when administering the scheme.
5. The Regulator expects trustees to ensure they have an adequate business continuity plan and that this reviewed at least annually and tested as appropriate.
6. So far as compliance with the new governance requirement that **core financial transactions be processed “promptly and accurately”**, the Regulator expects trustee boards to treat all transactions relating to the handling of member and employer contributions, and assets relating to those contributions, once they have been received by the scheme, as “core financial transactions”.
7. Trustees should, where they have power to do so, regularly review processes that affect the time it takes to process a core financial transaction, including taking into account developments in technology. The Regulator does not expect trustee boards’ sign off processes to cause undue delay to processing a transaction. The example given is that, where trustees are required to sign paperwork to authorise a transfer out, the frequency of trustee

meetings should not cause the processing of the transfer out to be delayed.

8. The Regulator says that electronic means should be used to process financial transactions wherever possible. Payment of monies by cheque is appropriate only in exceptional circumstances. Trustee boards should also consider using services and platforms that facilitate the prompt transfer of funds.
9. Where the law sets out maximum timescales for certain tasks and transactions, the Regulator expects trustee boards to treat these as absolute maxima and not to consider them equivalent to “prompt”. **The Regulator says that in all cases, trustee boards should ensure that contributions to the scheme, including sums transferred in, are invested within a maximum of 3 working days following receipt of the contributions and completion of a reconciliation exercise.**

Comment: This is a new expectation: the Old Code merely sets out the statutory deadline. It reflects a recent determination by the Pensions Ombudsman¹. Previous determinations suggested that contributions should be invested within 5 days of receipt.

10. The Regulator expects trustee boards to carry out a data review exercise at least annually, and to make arrangements to ensure that contributions and investments, and the records relating to them, including member records, are reconciled at least monthly and that any discrepancies are resolved promptly. Similarly, total unit reconciliations should be carried out regularly with investment managers to ensure that the total investments recorded by the scheme are consistent with the investment managers’ records.

E. Investment governance

1. The Regulator expects trustee boards to understand the investment powers and duties they have under the scheme trust deed and rules and legislation and to ensure that decisions are taken by those with the skills, knowledge and resources necessary to do so effectively.
2. The Regulator expects trustee boards to ensure an appropriate choice of investment arrangements for those members who do not wish to invest in the default arrangement, and to apply good governance to all their scheme’s investments, notwithstanding that the additional legislative requirements apply only to default arrangements.
3. When setting investment objectives and strategies, trustee boards are expected to consider the interests of both active and deferred members and, where relevant, members who are in a decumulation phase

¹Determination in relation to Mr. Burton (PO-2447) on 29th May, 2015

within the scheme. Trustee boards should also take account of risks affecting the long-term financial sustainability of the investments.

4. So far as flexibility is concerned, the Regulator says it expects trustee boards regularly to take steps to engage with members about the date they may wish to take their benefits and any preferences they have about how to take them, and to consider any information provided when determining the investment options to offer to members and strategies for the scheme. It says this includes considering matters such as the likelihood of members wishing to gain flexible access to their benefits, and preferences for particular approaches to investments (for example sustainable funds).
5. Members should have access to enough information about the investment options available to make informed decisions about their investment choices and to understand the potential impact of those decisions on their pension savings.
6. The Regulator expects trustee boards to assess regularly the performance of each investment option, including any default arrangement, and consider evaluating performance by reference to industry benchmarks. The evaluation process should be documented and should take account of the total level of costs and charges levied on each fund, including transaction costs wherever possible.
7. Trustee boards should review regularly their membership profile and adjust their investment strategies as appropriate. This includes taking into account the number and risk profile of investment funds and/or arrangements offered to members as an alternative to the default strategy.
8. Where trustee boards are thinking about changing the scheme's investment funds or investment manager, the Regulator expects them to understand the transition options available and, having taken appropriate advice from a suitably qualified person, decide which is the most suitable and efficient for the scheme and membership.
9. Where investment options which are not admitted to trading on regulated markets are offered, the Regulator expects trustees to identify these as such in the statement of investment principles and explain why it was appropriate to include them. The Regulator also expects trustee boards to assess the extent to which, and in what circumstances, any loss of scheme assets might be covered by a compensation scheme such as the Financial Services Compensation Scheme, indemnity insurance or similar arrangement, and to communicate the overall conclusion about the security of assets to members and employers.
10. Additional governance requirements apply to default arrangements; when considering whether a particular arrangement is a "default arrangement", the Regulator says that, where scheme members

have expressed a choice in the past about where their contributions are invested, but now those are being paid into a different arrangement without members making a new choice, trustees need to consider whether the original choice extends to the new arrangement. Where this is not immediately obvious, trustee boards should seek professional advice.

F. Value for members

1. There is a statutory requirement for trustee boards to assess the extent to which charges represent good value for members and to explain this in the annual chair's statement. The Regulator says it expects this explanation to address how the trustees have carried out the assessment, and the conclusions they have reached. It also expects the evidence to be documented contemporaneously. In its view, charges and transaction costs are likely to represent good value for members where the combination of costs and what is provided for them is "appropriate" for the scheme membership as a whole, and when compared to other options available in the market.
2. In assessing **value for members**, the Regulator expects trustees to make efforts to understand the characteristics of their members and, where possible, their preferences and financial needs. Where direct member feedback is limited, the Regulator expects trustee boards to consider what alternative methods they can use to assess what represent value for their members, including using publicly available industry research reports to compare their scheme to similar schemes.
3. But trustee boards need only focus on elements of the scheme provision for which **members** bear the costs. Where an **employer** covers the total cost of distinct services provided to the scheme, trustee boards need only consider the extent to which the services for which members bear the cost offer good value relative to those costs.
4. The Regulator also expects trustees to be able to identify the various entities that hold the relevant information on value, and to have a record of the individual or department they use as a contact for each entity. Trustee boards should engage early with them and establish the lead-in time that is required to provide information about transaction costs.
5. So far as the **charge cap** is concerned, when calculating whether any default arrangement is compliant, the Regulator expects trustee boards to document the calculation process and, in all but the most straightforward cases, to seek professional advice. It also expects trustee boards to consider guidance which the Government has produced and may update from time-to-time (for example the DWP's guidance on charge caps published in April, 2015).

G. Communicating and reporting

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1. The Regulator expects trustees to ensure that all communications sent to members are accurate, clear, relevant and provided in plain English. Member communications should be reviewed regularly. When deciding on the format of communications, trustees should take account of innovations in technology that may be available to them and appropriate for their members.
2. Where the law requires certain information to be provided in a particular communication, the Regulator expects trustees to consider what additional information or explanation members might need in order to make informed decisions about their benefits. For example, when issuing an SMPi, the Regulator would expect trustees to consider making the member aware of their rights in respect of options for accessing flexible benefits.
3. So far as communications at retirement are concerned, the Regulator expects trustee boards to make members aware of their right to transfer their benefits to another scheme at any age, in order to access their benefits in a variety of different ways, other than by purchase of an annuity, regardless of whether or not the scheme itself offers flexible access to benefits.
4. Where members remain in the scheme having flexibly accessed some or all of their pension using options offered by the scheme, the Regulator expects the trustees to continue to communicate with those members so far as is “relevant and appropriate”.
5. So far as pension scams are concerned, the Regulator expects the trustees to carry out due diligence on the scheme to which the member wishes to transfer, to check whether that scheme can legally be paid a transfer value and also to consider whether any characteristics are present in that scheme that could indicate a pension scam.
6. Trustee boards should include clear information on how to spot a scam in all relevant communications to members, including within standard communication materials such as the retirement wake-up pack.
7. So far as the annual **chair’s statement** is concerned, the Regulator expects this to be written in such a way as to provide a meaningful narrative of how, and the extent to which, the governance standards have been complied with. It expects trustee boards clearly to set out the measures they have taken to achieve compliance and the details of how they reach their conclusions on the extent of compliance. Trustees should contemporaneously document and be able to evidence the actions described and explained in the statement although that documentation and evidence does not need to be included as part of the statement.
8. So far as the **scheme return** is concerned, the

Regulator expects trustee boards to review the information on the scheme return, including the declaration at the end, and be comfortable that the information provided is accurate.

H. Comment

1. The guidance, to be published in Spring 2016, will provide practical examples of how to meet the Regulator’s expectations as set out in the draft New Code. Until then it is difficult to assess the practical impact of the changes.
2. Trustees of schemes within the scope of the draft New Code may find it of interest pending publication of the final version
3. Remember, though, that trustees’ powers may be constrained by the terms of the trust deed and rules and the Regulator’s expectations in the draft New Code need to be read with that in mind.
4. Comments on the draft Code are invited by 29th January, 2016. The Regulator has provided an interactive form for responding. The consultation paper, and response form, are on the Regulator’s [website](#).

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