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Date: 17 October 2022

Dear Sirs/Madams

Consultation response: Draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023

We write to you on behalf of Railways Pension Trustee Company Limited (RPTCL) in response to the DWP's consultation document on the *draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023* (the 'draft regulations').

We hope that the DWP has found our extensive engagement helpful as it developed its approach over the last couple of years, and we welcome the opportunity to provide further input on this very important set of regulations.

Within our response we highlight a number of key concerns, including:

- **Scheme closures due to higher costs** – contrary to previous assurances in the Houses of Parliament[1], the draft regulations could lead to significantly higher costs that risk forcing the closure of many of the UK's remaining open DB schemes, thereby substantially reducing the retirement incomes of many people across the UK.

- **Increase in systemic risk** – events in the pension industry over recent weeks have served as an example of the major systemic risks to which the UK economy can be exposed from pension scheme 'herding'. The draft regulations are more prescriptive than the existing funding regime, which we believe could exacerbate systemic risks to the UK economy.

- **Difficulties supporting Government's growth agenda** – we are concerned that the impact of the draft regulations could be contrary to the Government's growth agenda, as they will make it more difficult for schemes to increase (or even maintain) current levels of investment in long-term productive UK assets and to support the UK's transition to net zero.

We also note that pensions consultancies LCP[2] and WTW[3] have both raised material concerns about the draft regulations. We agree with the concerns raised.

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[1] Source: https://hansard.parliament.uk/commons/2020-11-16/debates/298AA028-D49E-4F07-A001-C483ADF38659/PensionSchemesBill(Lords)
[2] https://www.lcp.uk.com/media-centre/2022/10/new-pension-funding-rules-could-thwart-chancellor-s-pro-growth-agenda/
[3] https://www.wtwco.com/en-GB/News/2022/10/pension-funding-rules-should-be-sent-back-to-the-drawing-board

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About us

RPTCL is the corporate trustee of the principal pension schemes in the UK railway industry, including the Railways Pension Scheme (RPS), the British Transport Police Force Superannuation Fund (BTPFSF), the British Railways Superannuation Fund (BRSF), and the BR (1974) Pension Fund. Collectively, the schemes we support provide defined benefit pensions for over 350,000 members from almost 150 companies operating within the railway industry, with combined assets of over £35 billion.

These schemes serve as excellent examples of the variety of schemes that the draft regulations need to cater for within a truly flexible, scheme specific, funding regime. For example, the RPS is a sectionalised multi-employer scheme, having over 100 distinct sections that each carry out their own actuarial valuation under Part 3 of the Pensions Act 2004. Many of these sections operate on a shared cost basis, with contributing members paying 40% of the cost of benefit accrual and deficit contributions, if required, and employers paying the remaining 60% of this cost. Within the RPS and the BTPFSF, there are still over 100,000 active members accruing defined benefits for future service. Around 90,000 of these members belong to over 40 schemes/sections that remain open to new entrants and, in 2021, there were over 6,000 new entrants admitted to defined benefit membership in the RPS and the BTPFSF.

RPTCL is a proud supporter of collective pension schemes and the benefits they can bring to members, employers and society. In contrast to the significant amount of defined benefit ("DB") provision we still offer, the majority of the UK is now reliant on defined contribution ("DC") pensions. Although auto-enrolment has gone some way to improving member outcomes over recent years, research from the PPI suggests that over 90%[4] of these DC savers are facing an inadequate retirement. This is a major societal problem for the next generation of retirees and beyond, and makes it ever more important that people with access to well-run DB pensions are not forced to follow this path.

As pointed out in the consultation document, almost 10 million people across the country remain reliant on DB schemes, with around 65%[5] of these DB savers still in schemes that have some form of benefit accrual, and around 23%[2] in schemes that remain open to new members. To repeat the words of the ex-Minister for Pensions and Financial Inclusion in the Houses of Parliament, it is vital that the regulations:

"ensure that the requirement for all schemes to have a funding and investment strategy works appropriately for open schemes and ensures that immature open schemes are not prevented from taking appropriate investment risks where that is supportable."

We recognise that our schemes have characteristics that are not typical in the universe of UK DB schemes. However, our schemes are important, not simply to our members, but also to employers and the wider UK railway industry. It is essential that pension regulations allow members to continue to build up affordable and sustainable pensions, and that the Trustee remains able to pay these benefits over the long-term.

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[4] Pensions Policy Institute (2021) 'What is an adequate retirement income?'
[5] PPF 'The Purple Book 2021'

Key points in our response

We welcome and share the DWP's supportive comments about the need to make the draft regulations work for open schemes and the intention *"not to introduce a one-size-fits-all regime that forces immature schemes with strong sponsors into an inappropriate de-risking journey".* However, there are a number of areas where we believe the draft regulations will not achieve this objective.

We also have significant concerns that the DWP is consulting on the draft regulations before the revised Defined Benefit Funding Code of Practice ("revised DB CoP") has been published by TPR, and that no assessment of the potentially very significant impacts on employer and member costs has been carried out. This makes it extremely difficult to understand the full financial consequences of the draft regulations in the context of any additional member security they may bring, and we therefore intend to provide further comments to the DWP after reviewing the revised DB CoP and any accompanying impact assessment.

Impact of draft regulations on viability of open schemes

We note that there is no mention within the consultation document or the draft regulations themselves of how the proposed duration calculation for significant maturity will work for open schemes. We are concerned that this implies an inbuilt assumption from the DWP that all schemes, including open, non-maturing schemes, will be able to calculate significant maturity, set a relevant date, and set an assumed path of de-risking towards a position of low dependency by this relevant date.

As discussed with the DWP throughout our engagement, this will of course not be the case for every scheme. In particular, schemes which have a material flow of new entrants may not be expected to mature over time, and may even be expected to become less mature in some cases. We are therefore concerned that the draft regulations will implicitly require that all schemes calculate their point of significant maturity on the assumption that no, or very limited, new entrants will join the scheme. This will lead to an inappropriate funding and investment strategy which could threaten the viability of open schemes, potentially damaging the retirement outcomes of many current and future pension savers.

The consultation does recognise that the relevant date for such 'non-maturing' schemes may need to be pushed out at each new valuation and the funding and investment strategy revisited. However, if this approach is predicated on the assumption that no, or few, new entrants join the scheme after the valuation date, that scheme is likely to need to plan for a very different (i.e. lower risk and lower expected return) investment strategy to one which would be intended to be followed if that scheme continued to assume a realistic flow of new entrants. This journey plan for the investment strategy would need to be reflected in the assessment of the discount rate for Technical Provisions, regardless of whether it is actually expected to be implemented in practice (because in practice, if new entrants continue to join, the start of any de-risking journey would be indefinitely delayed). This will lead to substantially higher Technical Provisions liabilities than would otherwise be the case and potentially a large increase in the cost of accrual for active members. Such a significant step change in the Technical Provisions and associated contribution requirements risks making open schemes unaffordable – we estimate this could increase Technical Provisions by around 50% and the cost of accrual by as much as 75% for an immature scheme with a strong employer covenant, depending on the detail of how this is implemented in the revised DB CoP. This presents very significant challenges for us, in particular given the shared-cost nature of the RPS.

In addition, for a number of RPS sections (such as the BTPFSF, Network Rail, and the sections of 27 train operating companies), such an unnecessary increase in employer contributions is in effect an additional cost to either the farepayer or the taxpayer, being the only two sources of funds available to meet these increased costs. Unnecessary demands on either of these groups appears to us to be contrary to current Government policy.

During our engagement with the DWP last year, we outlined an alternative approach which we believed would allow the DWP and TPR to regulate the wide range of schemes they are responsible for. This alternative approach is set out in Appendix 2.

We appreciate that the DWP may now find it too difficult to incorporate this alternative approach within the draft regulations without making substantive changes. Taking a simpler approach, we therefore suggest the draft regulations are amended to explicitly state that the Scheme Actuary can include a reasonable allowance for new entrants, and future accrual, when projecting a scheme's maturity into the future. Further amendments should then confirm that schemes which are not expected to mature over time, based on this calculation, are exempt from the requirement to set a low dependency target.

Employer covenant

In the 17 years since the current funding regime was introduced, the concept of the employer covenant has been well embedded, and the critical importance of reflecting the employer covenant of a scheme in its funding and investment strategy strongly appreciated.

The matters to be taken into account when assessing covenant are too narrowly defined in the draft regulations. These matters should instead take account of the complexity of the covenant assessment process, and be principles based. This would allow covenant assessment to continue to be based on the bespoke circumstances of the employer (and scheme), and take into account, for example, balance sheet and liquidity, other material liabilities, creditor priority and the expected outcome on insolvency.

The focus on risk of insolvency also appears misplaced. Whilst for more typical schemes, the insolvency of the employer could be viewed as a shorthand way of defining the risk of there no longer being an employer capable of supporting the scheme, the actual risk is that of the sponsoring employer entering insolvency and a section 75 debt becoming due and there being no rescue, leading the section to enter the PPF, or for less than full benefits to be secured with an insurer. In the case of the RPS, this could preclude the Trustee from taking account of matters that are fundamental to the covenant strength of many RPS employers e.g. the train operating companies.

The draft regulations point towards additional factors to be set out in the revised DB CoP. However, we are concerned that these will be aimed at smaller and less sophisticated schemes, and impose prescriptive requirements which will prevent trustees from taking a justified, scheme specific approach based on a scheme's and employer's individual circumstances.

Low dependency

The draft regulations should be less prescriptive when setting out the investment and funding requirements, both at, and on the journey to, low dependency. The narrow definition of the investment requirements for low dependency may lead to many schemes which choose to run off their liabilities to invest in suboptimal portfolios, as well as increasing the systemic risks

(that we have seen very recently) when all DB pension schemes invest in similar investment strategies. While we agree that schemes that have reached significant maturity should invest in such a way as to be likely to meet their ongoing cashflow requirements, there are many reasons why taking an alternative approach to that outlined in the draft regulations could be expected to lead to better member outcomes for some schemes.

For example, it could be appropriate for a scheme to take more investment risk at, and after, the point of significant maturity, where this can be supported by the employer covenant and / or appropriate high quality contingent assets. It is also overly prescriptive to require the scheme's investment strategy to be highly resilient to changes in market conditions, regardless of the funding position of the scheme on the low dependency basis. This might rule out potential asset classes that could still provide significant benefits to the scheme in the longer term. Schemes should not be prevented from taking these approaches, under a truly flexible, scheme specific funding regime.

We also note that the impact of the proposals could be contrary to the Government's growth agenda, as they will make it more difficult for schemes to increase (or even maintain) current levels of investment in long-term productive UK assets and to support the UK's transition to net zero.

Furthermore, we are concerned that the very inflexible requirements will make it very difficult for some schemes – in particular those with weak sponsors and who are relatively poorly funded – to find any funding and investment solutions which comply with the draft regulations.

Recovery plans

The draft regulations introduce a new legal requirement for any recovery plan to be met "as soon as the employer can reasonably afford" and the DWP is consulting on whether this requirement should have primacy over the existing factors that can be taken into account. This could lead to inappropriate recovery plans which do not take sufficient account of other key factors. These factors include member affordability within shared-cost arrangements and the impact on an employer's plans for sustainable growth, and therefore employer covenant strength. This might lead to an overall detrimental impact on member security.

The regulations should therefore retain the flexibility to appropriately tailor recovery plans to both scheme and employer circumstances. The regulations should not give employer affordability primacy over other factors.

Investment powers

The draft regulations require trustees to specify within the funding and investment strategy, the intended proportion of assets to be allocated to different categories of investments at the relevant date, and aspects of the journey plan to this allocation. Noting that the funding and investment strategy requires agreement with the employer, this is potentially a significant shift in the balance of powers between trustees and employers in the investment strategy process.

Under current legislation, the power for setting investment strategy rests solely with the trustees. We consider that this is appropriate, works well, and should be retained. Making a change in this area is unlikely to be in the best interests of scheme members. Trustees should be required to agree the way in which pensions and other benefits under the scheme will be provided over the long-term, but trustees should retain as much flexibility and independence as possible to determine the appropriate investment strategy to achieve this. We suggest it

may therefore be more appropriate and proportionate for Part 1 of the Statement of Strategy to include the intended target return at the relevant date and an overview of the anticipated de-risking steps, rather than full details of the intended proportion of assets to be allocated to different categories of investments. This is already a common approach for schemes that have agreed their ultimate objective with their employer (be it buy-out, run-off, etc) and would appear consistent with 221A(2)(b) in the Pension Schemes Act 2021, which requires the funding and investment strategy to specify "the investments the trustees or managers intend the scheme to hold on the relevant date or relevant dates".

Lack of transitional arrangements for mature schemes

The draft regulations do not mention any transitional arrangements for schemes that are already at, or near, a position of significant maturity. For some of these schemes, a sudden and sharp shift to a requirement to fund to a position of low dependency, together with the new requirements for Recovery Plans, could lead to a material increase in contributions. If the employer cannot afford these contributions, it could increase the risk of employer insolvency, reducing the security of member benefits, and increasing the likelihood of a call on the PPF. The lack of flexibility in both timescales and investment strategy, means it is unclear how compliance is possible, if the employer cannot afford to resolve the deficit immediately.

We recommend that the option of a reasonable transition period is factored into the draft regulations or the revised DB CoP to help support these schemes.

Our full response to the consultation is set out within Appendix 1. Railpen would welcome the opportunity to meet with you to discuss our response.

Yours faithfully

Christine Kernoghan
Chair – RPTCL

Enc. Response to consultation questions

Appendix 1: Consultation questions responses to Draft Occupational Pension Schemes (Funding and Investment Strategy and Amendment) Regulations 2023

Question 1: Draft regulation 4(1)(b) provides that a scheme reaches significant maturity on the date it reaches the duration of liabilities in years specified by the Pensions Regulator's revised Defined Benefit Funding Code of Practice.

i. **Do you think that it would be better for the duration of liabilities at which the scheme reaches significant maturity to be set out in the Regulations rather than the Code of Practice?**

No.

The measure of maturity used to determine the point at which a scheme reaches significant maturity should not be set out in the regulations. There are two key reasons for this:

- The duration of liabilities, calculated using the low dependency basis, will be sensitive to changes in the underlying discount rate. For example, when long-term gilt yields increase significantly, this will reduce the duration of scheme liabilities and bring schemes closer to, or even beyond, the threshold for significant maturity. This in turn could trigger significant changes to asset allocations across the industry, despite there being no actual change to scheme maturities in reality (for example, as measured by cashflow projections). To put this in perspective, a scheme with a liability duration of around 18 years at the start of 2022 will now have a liability duration of around 14 years, following the material increases in long-term gilt yields experienced this year to date (all else being equal). It would therefore be appropriate to retain the flexibility of moving the point of significant maturity following any significant shifts in market conditions, rather than hardcoding the point of significant maturity within the regulations. Taking into account the very large changes in yields experienced in recent weeks, we are of the view that it is critical that TPR have the means to very quickly change the duration when warranted by changes in market conditions.

- Liability duration is just one measure of maturity. Although liability duration is likely to be the preferred measure for the majority of schemes, there may be valid reasons for favouring an alternative approach. For example, schemes may wish to follow a more bespoke approach that examines the point at which the scheme's investment strategy, on a standalone basis, would not be expected to deliver its benefit promises after suffering a significant downside event. Under a truly flexible, scheme specific funding regime, schemes should not be prevented from taking these approaches.

ii. **If you think that the point of significant maturity should be specified in Regulations, do you agree that a duration of 12 years is an appropriate duration at which schemes reach significant maturity?**

As set out in our response to Q1i), we do not think that the point of significant maturity should be specified in the regulations, and fixing the point of significant maturity introduces a somewhat arbitrary cliff edge.

We note that a liability duration of 12 years is broadly consistent with the indicative range of significant maturity (12-14 year liability duration) set out by TPR in its first consultation on the revised Defined Benefit Funding Code of Practice. However:

- These figures were calculated during a period of very low, and relatively stable, nominal and index-linked gilt yields.
- As noted in response to Q1i), the duration of a scheme's liabilities is sensitive to market conditions, in particular the discount rate. Long-term nominal government bond yields have increased by over 4% pa since TPR's first consultation was published in March 2020, and so this range may need to be revised downwards, or be flexible enough to allow adjustment for the level of bond yields.
- We note that TPR's indicative range of significant maturity was derived to be consistent with the point at which a scheme's benefit cashflows are broadly 5%-6% of its liabilities. This in turn was derived from anecdotal evidence that this is the point at which a typical scheme's investment time horizon, and magnitude of benefit cashflows in relation to assets, are such that the scheme should be fully funded on a position of low dependency. Given the importance of this parameter, we believe the point of significant maturity should be based on rigorous analysis of a wide range of schemes, rather than anecdotal evidence.

Further, many schemes will have already determined a date by which they are aiming to achieve a long term objective. It might be preferable for these schemes to be able to retain any end date they have already set, and for the regulations to include sufficient flexibility for the date to remain constant over time. It might not be helpful or productive for the end date of a long term plan to be moved by a year or two at each valuation, just because of changes in market conditions.

Question 2: Do you think that the definition of low dependency investment allocation provided by draft regulation 5 is appropriate and will it be effective?

We note that the proposed definition of a low dependency investment allocation is even stronger than previous definitions proposed in TPR's first consultation on the revised DB Funding Code of Practice e.g. TPR noted that *"Being funded on this basis would mean a scheme could expect to provide member benefits with very limited future support from the employer and, if such support is required, it would be expected to be small relative to the size of the scheme."*

This is very different to draft Regulation 5, which sets out that a scheme should be invested such that:

1. Further employer contributions are not expected to be required to make provision for accrued rights to pensions and other benefits under the scheme;
2. Expected cashflow from investments is broadly matched with the payment of pensions and other benefits; and
3. The value of assets relative to the value of the scheme's liabilities is highly resilient to short-term adverse changes in market conditions.

We believe the proposed definition in draft Regulation 5 is too prescriptive. For example, point 2 above could imply that schemes will be required to implement a cashflow driven investment strategy. While this may be an appropriate approach for some schemes, there are valid reasons why this may not be the preferred approach for all schemes – for example, we believe

a well hedged portfolio, with an appropriately sized allocation to a diversified range of growth assets, could be an appropriate approach for some schemes.

It is also overly prescriptive to require the scheme's investment strategy to be highly resilient to changes in market conditions, regardless of the funding position of the scheme on the low dependency basis. This rules out potential asset classes that could still provide significant benefits to the scheme and its members in the longer term.

To achieve full funding at this level of investment risk, there is also a risk of trapped surplus within the scheme. This would be very unattractive to employers, and as such a structure that would allow the scheme unrestricted access to funds (such as through escrow) without those funds being held in the Trust, may be advantageous.

Furthermore, we note that, without growth assets targeting a return above the discount rate, there is a good chance that a deficit could appear due to non-investment risks such as longevity, or the mismatch between the inflation exposure of the assets and the liabilities. From a member's perspective, it may therefore be less risky overall for a scheme to be permitted to take more investment risk (where this can be supported) to manage adverse non-investment experience, and the regulations should allow schemes the flexibility to adopt this approach where appropriate.

Given the requirement to hold assets with suitable liquidity is stated elsewhere and 5(2)(b) covers the needs to have assets which are well matched, we believe 5(2)(a) could be removed. However, given the complexities in defining a low dependency investment allocation, we suggest that it may be more appropriate to leave the entirety of this definition to the revised DB CoP, where more detail regarding methods of assessing risk and return can be included.

Question 3: Do you think that the definition of low dependency funding basis provided by draft regulation 6 is appropriate and will it be effective?

It is questionable whether significantly mature schemes should be forced to fund to a low dependency target, with a low dependency investment allocation, where the strength of the employer covenant would otherwise support investment in a wider range of asset classes. There are also scenarios in which aiming for such a high target would lead to worse outcomes for both members and employers (see Q5).

Question 4:

i. **Do you agree with the way that the strength of employer covenant is defined?**

No.

We welcome the decision to include reference to employer covenant within the draft regulations, given its importance in investment and funding decisions and strategies, as commented upon within the consultation document. However, given the diversity of employers, the diversity of schemes and the complex interactions between employers and schemes, any attempt to define employer covenant that goes further than on a "principles" basis, risks limiting the factors that trustees should take account of. This would be to the detriment of the employer, the scheme and ultimately the security of members' benefits. This is particularly relevant for atypical situations, which the current scheme-specific regime can deal with.

The security of members' benefits depends on the ability of the employer to put cash into the scheme as and when required, against a risk backdrop of there ceasing to be an employer to support the scheme. Whilst the insolvency of the employer could be viewed as a shorthand way of defining the risk of there no longer being an employer, the actual risk is of the sponsoring employer entering insolvency and a Section 75 debt becoming due and there being no rescue and the section entering the PPF.

ii. Are the matters which trustees or managers must take into account when assessing it, as provided by draft regulation 7, the right ones?

The definition of employer covenant strength includes reference to the upcoming revised DB CoP. Given that the revised DB CoP has not yet been published, it is very difficult to conclude on the appropriateness of the matters required to be taken into account when assessing covenant strength.

Our comments are as follows:

- We are concerned that the covenant definition is too narrow to take account of all scheme and employer circumstances. As drafted, covenant strength is limited to consideration of the employer's financial ability to support the scheme (based on its cash flow, likelihood of insolvency and the employer's prospects) and legally enforceable contingent assets, and in the context of either low dependency or solvency liabilities. Certain schemes have contractual, or other protections, that are not legally enforceable contingent assets, but serve to render the risk of the sponsoring employer entering insolvency and a Section 75 debt becoming due and there being no rescue leading to the section entering PPF assessment as negligible. These need to be taken into account for covenant assessment purposes. If the draft regulations seek to define employer covenant, they should at least include an additional consideration, to permit any other relevant factors to be taken into consideration when assessing covenant strength.

- The draft regulations set out that covenant should be assessed relative to the pension liabilities as calculated on a low dependency and solvency basis. For non-maturing open schemes, in our view it would be of more relevance to consider the ability of the employer to meet any inherent risk within an appropriate investment and funding strategy, as part of a journey plan, and we consider it important that the differing characteristics of open schemes are accommodated within these regulations.

- Currently, in transactional situations where a Type A event takes place, trustees will often refer to the solvency deficit when negotiating mitigation with an employer. We are concerned that an unintended consequence of these draft regulations could be that employers argue that low dependency is more relevant, which could weaken the trustees' negotiating position.

- We are concerned that the draft regulations use "employer insolvency" as a synonym for the scheme going into PPF assessment, whereas for a scheme to enter PPF assessment it requires an employer insolvency and a Section 75 debt becoming due and there being no rescue. This difference may appear subtle, but could have a material impact in the context of draft regulation 4(b).

We suggest that any matters or factors that need to be taken into account in assessing the strength of the employer covenant are left to TPR's revised DB CoP. In our view, setting these factors out in the regulations will inevitably mean that they are not broad enough to take account of the circumstances of all schemes and employers.

iii. **Does draft regulation 7(4)(c) effectively capture the employer's broader business prospects?**

We consider it will be important for the regulations and the revised DB CoP to provide the freedom for an assessment of the covenant strength to take into account any relevant factors and to not be overly prescriptive. Employers are complex and diverse in nature, as are schemes, and as are the interactions between employers and schemes. Therefore any attempt to define how employer prospects are taken into account that goes further than on a "principles" basis, risks limiting the factors that trustees should take account of, to the detriment of the employer, the scheme and ultimately the security of members' benefits.

Question 5: Does it work in practice to set a minimum requirement for the relevant date to be no later than the end of the scheme year that the scheme is estimated to reach significant maturity?

The position of non-maturing schemes

While we welcome and share the DWP's supportive comments about the need to make the draft regulations work for open schemes, we note that there is no mention within the consultation document or the draft regulations themselves of how the calculation of significant maturity and the setting of a relevant date will work for open schemes.

We are very concerned that this implies an inbuilt assumption from the DWP that all schemes will be able to calculate significant maturity, set a relevant date, and begin on an assumed path of de-risking towards a position of low dependency by this relevant date. As discussed with the DWP throughout our engagement, this will of course not be the case for every scheme. In particular, schemes which have a material flow of new entrants may not be expected to mature over time, and may even be expected to become less mature in some cases. These schemes will be expected to never reach a point of significant maturity, and will therefore be unlikely to be in a position to ever set a relevant date.

As currently drafted, we are concerned that the draft regulations implicitly require that all schemes calculate their point of significant maturity on the automatic assumption that no, or limited, new entrants will join the scheme, regardless of the expected flow of new entrants. This will lead to an inappropriate, overly prudent, funding and investment strategy which could threaten the viability of open schemes, damaging the retirement outcomes of many current and future pension savers.

We currently have around 90,000 active members in our schemes/sections that remain open to new entrants who could be detrimentally impacted by the approach, as currently drafted.

We note that the consultation does recognise that the relevant date for such 'non-maturing' schemes may need to be pushed out at each new valuation and revisiting of the funding and investment strategy. However, if this approach is predicated on the assumption that no, or limited, new entrants join the scheme after the valuation date, that scheme is likely to need to plan for a very different (i.e. lower risk and lower expected return) investment strategy to the one which is actually expected to be followed, reflecting a realistic flow of new entrants. The

investment strategy underlying this journey plan would need to be reflected in the assessment of the discount rate for Technical Provisions, regardless of whether it is actually expected to be implemented in practice, leading to substantially higher Technical Provisions liabilities than would otherwise be the case, and potentially a large increase in the cost of accrual for active members. Such a significant step change in the contribution requirement risks making an open scheme unaffordable – we estimate this could increase Technical Provisions by around 50% and the cost of accrual by as much as 75% for an immature scheme with a strong employer covenant.

During our engagement with the DWP, we outlined an alternative approach which we believe will allow the DWP and TPR to regulate the wide range of schemes they are responsible for. This alternative approach is set out in Appendix 2.

We appreciate that the DWP may now find it too difficult to incorporate this alternative approach within the draft regulations, without substantial changes. Taking a simpler approach, we therefore suggest the draft regulations are amended to explicitly state that the Scheme Actuary can include an appropriate allowance for new entrants and future accrual when projecting a scheme's maturity into the future. Further amendments should then confirm that schemes which are not expected to mature over time, based on this calculation, are exempt from the requirement to set a low dependency target.

The position of maturing schemes

Please see our response to Q1(i). We believe this requirement could be too rigid, if there is not sufficient flexibility in the determination of the point of significant maturity. It would therefore be appropriate to retain the flexibility of moving the point of significant maturity following any significant shifts in market conditions, rather than hardcoding the point of significant maturity within the regulations. Taking into account the very large changes in yields experienced in recent weeks, we are of the view that it is critical that TPR have the means to very quickly change the duration when warranted by changes in market conditions, and – further – to consider whether duration remains the most appropriate measure of the maturity of a pension scheme, noting the limitations exposed by recent market movements.

Transitional arrangements for mature schemes

Our other key concern is that the consultation and draft regulations do not appear to mention any transitional arrangements for schemes that are already at, or near, a position of significant maturity.

For some of these schemes, it may be necessary to retain some flexibility to set a relevant date which is beyond the end of the scheme year in which significant maturity is reached. This is particularly the case for schemes where a sudden and sharp shift to a position of low dependency could lead to a material increase in employer contributions (and member contributions in the case of a shared cost arrangement, like many sections of the RPS), that could threaten the security of member benefits.

We suggest that the option of a reasonable transition period (for example two valuation cycles) is factored into the regulations to help support these schemes.

Question 6: Does your scheme already have a long-term date and how is it calculated?

Some closed sections of the RPS currently operate a default investment strategy that de-risks over time as the profile of the section's membership changes, and a flexible discount rate structure corresponding with this investment strategy.

The default period over which a section's investment strategy and discount rates transition to their ultimate states broadly represents the time until the membership profile of that section is expected to be pensioner-only.

Question 7: Where the funding and investment strategy is being reviewed out of cycle with the actuarial valuation, would it be more helpful to require it to align with the most recent actuarial report?

We have interpreted this question as asking whether it would be more helpful to require the funding and investment strategy, and relevant date, to be reviewed using market conditions and scheme data as at the most recent actuarial report date, rather than the latest actuarial valuation.

We believe the regulations should give the trustee and employer the flexibility to determine an appropriate date for reviewing a funding and investment strategy outside of the triennial actuarial valuation cycle. For example, in many cases it would be simpler to do this at an actuarial report date because calculations will be undertaken anyway. However, there may be very good reasons why it should not align with an actuarial report date, for example, if the reason the review is taking place is because of a material change in market conditions or membership profile after the latest actuarial report date.

Question 8: Do you think that these minimum requirements are sensible and will provide additional protection for the accrued pension rights of scheme members?

Low dependency

As set out in our response to Q2 and Q3, we have material concerns over whether low dependency is an appropriate minimum target for all schemes, especially given the financial impact on employers and member benefit security have not been assessed. We are also very concerned that it has been defined too inflexibly, leading to significant potential adverse and unintended consequences for sponsors, members, and the UK financial system.

Transitional arrangements for mature schemes

Please note our comments in response to Q5 above in relation to transitional arrangements for mature schemes.

Setting minimum requirements relative to relevant date

We question whether it is appropriate to set these minimum requirements with reference to the relevant date, rather than the end of the scheme year in which a scheme is expected to reach significant maturity (or, noting part of our response to Q5 above, perhaps a reasonable transition period from the date the regulations come into force, for mature schemes). Using the relevant date as the reference point for minimum requirements could have the unintended consequence of having an adverse impact on schemes which are going above and beyond the objectives of the regulations, and targeting a position of low dependency well in advance

of significant maturity. Whilst these schemes would have the headroom to revise their relevant date, if a position of low dependency became unachievable within the timescales originally targeted, this might encourage some well-funded schemes to start from a more cautious position when setting their relevant date, stretching out the period over which they expect to rely on their employer covenant.

Question 9:

i. **Should such limited additional risk at and after significant maturity be permitted, if supported by contingent assets? If so, to what percentage of total liabilities should this be limited?**

Yes - additional risk should be permitted at and after significant maturity if this is supported, both by contingent assets and / or the strength of the employer covenant, irrespective of whether that strength arises from a contingent asset or just inherent covenant strength.

The consultation describes the importance of identifying risk and ensuring that it is supportable by the employer covenant. We consider this to be a sound principle, and believe this should remain an underlying principle at significant maturity. Placing a cap on the level of risk that can be taken feels arbitrary and unnecessary.

There could be good reasons for trustees and employers to want to continue to take some level of investment risk at significant maturity – for some schemes reaching significant maturity will be a point along a journey to buyout, rather than an end goal in itself, and it may therefore be desirable (and in members' best interests) to permit some investment risk to seek to bridge the path to buyout. Other schemes may wish to provide for discretionary pension increases. Once a scheme reaches full funding on a low dependency basis, it still retains some reliance on the employer covenant, and may have to wind up in the event of employer insolvency. It therefore may be in members' best interests to reach buyout in a reasonably short timeframe. This needs to be assessed on a case by case basis. In our view the regulations need to permit schemes to bridge the gap between low dependency and buyout through potential investment returns, rather than a reliance on additional employer cash payments. Preventing schemes from doing this could lead to fewer schemes reaching buyout (as the employer refuses to fund it purely with cash) and more instances of members' benefits not being paid in full.

In addition, many employers will be concerned about "trapped surplus" if the funding requirements are too prudent and too restrictive. They might therefore be reluctant to pay additional contributions to the scheme. Contingent asset solutions can be an attractive compromise in these situations – providing security for members but allowing any assets to be returned to the employer if they are not in fact needed over time. In some cases, these solutions can provide better outcomes for members than relying on scheme assets alone. However, cost might not make this an accessible solution for smaller schemes.

ii. **What additional risks to members' benefits might be posed as a result, and what safeguards should apply to protect members?**

If the risks are adequately supported, the risks to members' benefits should be minimal – and, as noted above, high quality contingent assets could actually improve member outcomes in some cases.

In terms of safeguards, we consider that contingent assets at significant maturity would need to be high quality, and include appropriate legally binding triggers requiring a flow of funds into the scheme (e.g. based on funding level).

Where employers can demonstrate continuing covenant strength for the medium to long term, with little or no risk to the security of members' benefits, we see no reason to ignore that this could lead to a better, more efficient, outcome for all concerned.

Question 10: Do you think that the provisions of paragraph 4 of Schedule 1 will allow appropriate open schemes to continue to invest in growth assets as long as that risk is appropriately supported?

No.

Paragraph 4(2)(b) implies that all schemes, including open, non-maturing, schemes will be able to determine a relevant date. As set out in our response to Q5, this is a major concern that could have a material impact on costs, forcing well-run open schemes to close, thus significantly limiting the ability to invest in growth assets. The lower level of demand for growth assets from DB schemes may, in turn, not align with the Government's growth agenda.

Our comments below relate to maturing schemes that can calculate significant maturity, and therefore set a relevant date.

Definition of employer covenant

We agree with the principles of paragraph 4(2)(a) but please note our comments regarding the definition of employer covenant in response to Q4(i).

Investment risk

We believe that paragraph 4(2)(a) is unnecessarily restrictive, and effectively requires all schemes to adopt a linear path of investment de-risking as they mature.

In our view, the consultation highlights a sound principle that risk should be identified and should be supportable by the employer covenant. We would be concerned if the revised DB CoP introduced narrowly defined levels of permissible investment risk on the path to low dependency, as it is important to maintain the current scheme specific approach to investment and funding strategy.

In our view there could be instances where the maturity of a scheme may not need to be directly linked to the investment strategy. For example, for very small DB schemes where the covenant strength is very strong (annual cash flow is many multiples of the Section 75 debt), a high percentage downside investment risk could remain supportable until significant maturity – and could be desirable for the trustees and the employer (and the members) as all parties seek to reach full funding on a solvency basis in a cost-efficient and timely way.

Question 11: Do you think that the principles in paragraphs 4 and 5 of Schedule 1, requiring funding risks and investment risks to be linked primarily to the strength of the employer covenant, are sensible?

We agree that employer covenant strength should be a key driver for funding and investment strategy. However, as currently drafted, employer covenant seems to be a secondary

consideration, which becomes less important as a scheme moves towards significant maturity, and is not taken into account at all once a scheme is significantly mature.

As noted in our response to Q9 and Q10, we believe that additional risk taking should be permitted at significant maturity where this is supported by contingent assets and / or employer covenant. We would also support some flexibility to allow for growth assets once schemes are significantly mature – both in the investment allocation and calculation of liabilities.

Question 12: Do you think that the new liquidity principle set out in paragraph 6 of Schedule 1 is a sensible addition to the existing liquidity requirement of regulation 4(3) of the Occupational Pension Schemes (Investment) Regulations 2005?

Yes – we agree this is a sensible addition. However, the principle should include allowance for expected cashflows into the scheme (for example, contributions), as well as the existing assets. We note that the draft regulations also set out that a scheme's Statement of Strategy will need to evidence that this principle is being met, which may be governance intensive for some smaller schemes.

Question 13: Will the matters and principles set out in Schedule 1 enable the scheme specific funding regime to continue to apply flexibly to the circumstances of different schemes and employers, including those schemes that remain open to new members?

No.

Notwithstanding the fact that, without the accompanying revised DB CoP, there remain significant gaps which make this question difficult to answer in full, there are a number of areas where we consider that the draft regulations, and Schedule 1 in particular, impose prescriptive requirements and principles which will prevent trustees from taking a justified, scheme specific, approach based on a scheme's individual circumstances.

The new regime will clearly be less flexible than the current regime, and significantly less flexible as schemes approach significant maturity, when very large additional costs might be imposed, and where the options for funding and investment will be extremely limited. There may be a subset of employers with mature schemes or with weak covenants, even if relatively immature, who may not be able to meet these costs, especially in the absence of a transition period, leading to a worse outcome for members than if schemes continued to run an appropriate level of investment risk supported by the employer covenant.

Crucially, more flexibility is required for open schemes which are not maturing – please see our response to Q5.

Question 14: Is the level of detail required for the funding and investment strategy by draft regulation 12 reasonable and proportionate?

We agree that draft regulation 12(a) is reasonable and proportionate, although we note that permissible funding and investment strategies must include the intention to continue running the scheme in an open state in perpetuity, for as long as a scheme is not expected to mature due to a reasonable and demonstrable flow of new entrants.

Draft regulation 12(b) is reasonable and proportionate for schemes which are maturing, and can therefore determine the point of significant maturity and set a relevant date. However, this is not reasonable or proportionate for schemes which are not maturing, and cannot therefore determine the point of significant maturity.

Draft regulation 12(c) would not seem reasonable or proportionate for an immature scheme which is a long way from its relevant date (or indeed a non-maturing scheme which will not have a relevant date). The ultimate investment strategy of such schemes is likely to change substantially over that period and the split between asset classes is likely to be of little value. It would seem more reasonable and proportionate to set out the target level of investment risk and return at the relevant date, leaving trustees the flexibility to take strategic or tactical steps to adjust the underlying asset allocation as needed.

Question 15: Do you think the requirement for high level information on expected categories of investments will impact trustees' independence in making investment decisions in the interests of scheme members?

Yes – we note that draft regulation 12(c), combined with the requirement for trustees to agree part 1 of the Statement of Strategy with the scheme's employer(s), is a significant shift in the balance of powers between trustees and employers in the investment strategy process. Such a shift is unlikely to be in the best interests of scheme members, particularly if the level of detail required to be agreed with the employer includes the proportion of assets to be held in each asset class.

Many trustee boards already find changing investment strategy a challenging, governance-intensive process, which makes it difficult to be nimble and seize opportunities as they arise. The requirement to agree the long-term strategic asset allocation with employers, and journey towards it, is only likely to make this process more challenging, and therefore lead to worse outcomes for scheme members.

For example, a scheme's trustees and employer may have agreed that they will target an interest rate and inflation hedging ratio of 90% at the relevant date, and recorded this in Part 1 of their Statement of Strategy. The scheme is currently 10 years away from its relevant date and the trustee is currently targeting an interest rate and inflation hedging ratio of 50%. Now, suppose a sudden improvement in market conditions, much like we have recently experienced, presents a short-term opportunity to increase interest rate and inflation hedging ratios to 100% (i.e. greater than the level agreed with the employer at the point the scheme reaches its relevant date). Under the draft regulations, would the trustees of this scheme be expected to agree a change to its funding and investment strategy with the employer before it could act on this opportunity? And is this in the best interests of members?

In our view, the requirement to agree the long-term investment strategy with the employer is an unnecessary change to a process which has worked well up until now. Trustees should be required to agree the way in which pensions and other benefits under the scheme will be provided over the long-term, but trustees should retain the flexibility and independence to determine the appropriate investment strategy to achieve this.

We also note that there are complexities in predicting future asset allocations, even at a high level. It may therefore be more appropriate and proportionate for Part 1 of the Statement of Strategy to include the intended target return at the relevant date and an overview of the anticipated de-risking steps, rather than full details of the intended proportion of assets to be

invested in various asset categories. This is already a common approach for schemes that have agreed their ultimate objective (be it buy-out, run-off, etc) and would appear consistent with 221A(2)(b) in the Pension Schemes Act 2021, which requires the funding and investment strategy to specify “the investments the trustees or managers intend the scheme to hold on the relevant date or relevant dates”.

Question 16: Are the requirements and timescales for determining, reviewing and revising the funding and investment strategy in draft regulation 13 realistic?

A period of 15 months could be very challenging for some schemes, particularly in the case of sectionalised arrangements, such as the RPS, where each section effectively carries out its own actuarial valuation and therefore will also be required to determine a funding and investment strategy within this timeframe. Part of this challenge will be due to the additional steps required to develop the funding and investment strategy (however, much of this is already considered), part will be due to the additional time taken to record the funding and investment strategy, and part will be due to the additional elements that will need to be agreed or consulted on with employers.

Question 17: Are there any other assessments or explanations that trustees should evidence in Part 2 of the statement of strategy?

No, we do not think any other assessments or explanations are required.

Question 18: Do you agree that these are the appropriate requirements for the scheme trustee board when appointing a chair? Are there any other conditions that should be applied?

Yes, we agree that these are appropriate requirements when appointing a chair.

Question 19: We would like to know if you think these requirements will work in practice?

We assume this question relates to the draft requirement for the actuarial valuation to include the actuary’s estimate of the level of the scheme’s maturity at both the effective valuation date and the relevant date; when the scheme is expected to reach significant maturity; and the actuary’s estimate of the funding level, on a low dependency funding basis as at the effective valuation date.

We note that these are also all required data points for either Part 1 or Part 2 of the Statement of Strategy, and we think they should all work in practice, albeit noting numerous previous comments regarding the inability of non-maturing schemes to determine a relevant date. We also note that projecting the development of a scheme’s maturity into the future is likely to be a new concept for many schemes and may not be a direct output from current actuarial valuation software, but we do not think this should be a challenging or intensive calculation for the actuary to perform.

We also note that the requirements for actuarial valuations and reports may have implications for items to be communicated within Summary Funding Statements, the requirements of which are covered in the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013 (as amended). It is important that Summary Funding Statements are easy for members to read and comprehend, so it would be appropriate for the DWP and TPR to

consider how any changes to the requirements for Summary Funding Statements will also support member understanding of them.

Question 20: Do you consider that the matters prescribed by regulation 8(2) of the Occupational Pension Schemes (Scheme Funding) Regulations 2005 remain relevant for trustees or managers to take account of when determining or revising recovery plans? If so, why and how are they relevant to the setting of appropriate recovery plans?

Yes – these all remain relevant factors for trustees to take account of when determining or revising recovery plans. For example:

- The asset and liability profile of the scheme may mean that the assets are expected to generate a return in excess of the discount rate which is expected to remove, or help to remove, the deficit over the recovery period. This is a very common feature of recovery plans.
- The risk profile is clearly relevant as trustees should consider the risks associated with a given plan.
- Liquidity requirements may be relevant for severely underfunded schemes – to ensure the scheme has sufficient funds to pay benefits as they fall due under the recovery plan.
- The age profile of members could be relevant for very mature schemes – to ensure the scheme has sufficient funds to pay pensions

In addition, employer affordability and, in the case of shared cost arrangements like the RPS, member affordability, are key considerations that should be included.

Question 21: Do you consider that the new affordability principle at draft regulation 20(8) should have primacy over the existing matters, if they do remain relevant?

No – although the affordability of recovery plan contributions is a key factor to consider, the regulations should retain the flexibility for recovery plans to be appropriately tailored to both scheme and employer circumstances. Recovery plans should also be able to continue to take into account the impact on an employer's plans for sustainable growth and therefore employer covenant strength, and any knock-on implications this might be expected to have on overall member security.

This might be the intended interpretation of the phrasing "reasonably afford" in draft Regulation 20(8), but this needs to be made clearer if this is the case, or covered sufficiently in TPR's DB CoP. In our view, what is reasonably affordable should take into consideration competing cash flow demands such as capital expenditure (both maintenance capex and growth capex in the context of forecast and targeted growth) as well as other underfunded DB schemes of the sponsoring employer.

Furthermore, although employer affordability may be the primary factor for many schemes to consider when setting a recovery plan, this may not be the case for all schemes. For example, the draft regulations, consultation and impact assessment are silent as regards shared cost schemes (like many sections of the RPS), where any funding deficits are shared between the employer and the active members. Member affordability can be more constrained than employer affordability. We consider it important that the circumstances of shared cost schemes are acknowledged within the regulations and / or the revised DB CoP, with

recognition that member affordability may need to be taken into account and may be a contributory factor to longer than average recovery plan durations.

The nature of non-associated multi-employer schemes is also not covered within the consultation. Often a key consideration for trustees of these schemes is around managing cross-subsidy and the amount that stronger sponsors might be perceived to subsidise the pension costs of weaker sponsors. Longer than average recovery plan periods may be appropriate in such circumstances and we consider it important that this is acknowledged within the regulations and / or revised DB CoP.

Lastly, for schemes with a very strong employer covenant it could be implied that "as soon as the employer can reasonably afford" means immediate payment into the scheme upon signing of the Recovery Plan, which is contrary to current practice where many strong employers would seek to spread contributions over a reasonably short period for which there remains a very high confidence of receipt. We believe that requiring immediacy of contributions in this scenario would result in a very significant short-term deviation of funds from capital investment programmes, thereby having a potentially material impact on the longer-term sustainability of the sponsor and more widely UK economic growth. Where the covenant can underwrite the risk of spreading these contributions it is not immediately clear that there is any significant value to a scheme of requiring this immediacy of repayment, whereas the broader economic consequences could be significant. Furthermore, the requirement could prove a disincentive to employers from agreeing to a more prudent funding target, if it meant that they were then compelled to pay contributions over a short time period.

It is also worth noting that TPR's 2021 Annual Funding Statement states that the "best support for a pension scheme is a strong employer" and we believe there is a risk that the proposed wording regarding affordability may undermine this principle.

Once again, we note that the financial consequences of what could be a significant change in the funding regime are not considered in the impact assessment.

Question 22: Will the requirements in draft regulation 20(9) work in practice for all multi-employer pension schemes?

We agree that it is appropriate for sections of a sectionalised arrangement to be treated as individual schemes for the purposes of the Regulations, as they are for the purposes of the Scheme Funding Regulations and Part 3 of the Pensions Act 2004.

However, please note our comments regarding the practicalities of meeting these requirements within the proposed 15 month timeframe, as set out in our response to Q16.

Question 23: Do you agree with the information presented in the impact assessment for the funding and investment strategy?

No.

We do not consider the extent of the impact assessment is fit for purpose in the context of the fundamental changes being proposed to the scheme funding regime, and the potentially material impacts on schemes, employers and members.

It is our understanding that the DWP has decided not to carry out an impact assessment of implementing a funding and investment strategy under the requirements of the draft regulations at this time. We understand that the DWP intends to update its impact assessment once further detail of the requirements is known following publication of TPR's second consultation on its revised DB CoP.

Whilst we appreciate that various details of the new funding regime still need to be determined, the draft regulations aim to introduce some significant shifts in policy. It is vital that the true impact of these policy shifts is fully understood before they enter into law.

For example:

- What will be the high level impact on the funding position of open schemes if all schemes are required to set a relevant date?
- What will be the high level impact on the funding position of mature schemes that are already past their relevant date and not yet at low dependency?
- What impact will the above have on employer contributions (and member contributions in the case of shared cost arrangements like the RPS), and what knock-on impact will this have on the employer covenant and overall security of member benefits?

It would be preferable for these questions to be answered using very high-level assumptions than not answered at all (for example that schemes at low dependency might expect an investment return of gilts+1% pa). If this impact assessment does need to wait for TPR to consult on some of the detail, then we suggest this must take place concurrently with the DWP's own consultation on these draft regulations.

We note that LCP have estimated that the potential impact on contributions and benefits of the proposed changes could be in excess of £30bn[6].

Question 24: Do you expect the level of detail required for the funding and investment strategy to increase administrative burdens significantly?

Yes – particularly in the case of sectionalised arrangements, like the RPS. The detail required is likely to add significant time, and therefore cost, when carried out across over 100 different sections with different designated employers. And, as noted in our response to Q16, meeting these requirements within a 15 month timeframe is likely to be very challenging.

However, whilst the additional costs of administering these changes is likely to be material, we would expect these to be small in comparison with the additional employer and member contributions which would be required as a result of the draft regulations being passed.

Question 25: Do you agree with information presented in the impact assessment for the statement of strategy, referenced in paragraph 6.1?

We agree that the cost of appointing a Chair is likely to be minimal given the large proportion of schemes that already operate with a Chair in place.

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[6] https://www.lcp.uk.com/media-centre/2022/10/new-pension-funding-rules-could-thwart-chancellor-s-pro-growth-agenda/

Regarding the impact assessment of the proposed requirement for schemes in surplus to submit a valuation to TPR, we would expect the cost of doing so to be materially in excess of the indicated £25.40 per scheme. This is on the basis that this is likely to be carried out by the scheme's actuarial adviser, whereby the standard process may be for a junior actuary to complete the submission, and a more experienced actuary to check the submission. Based on typical charge-out rates for actuarial consultancies, the true cost to schemes is likely to be in the range of £250-£500 per hour.

Once again, although assessing the impact of these changes is helpful, we would expect these to be insignificant when compared with an assessment of the additional employer and member contributions which would be required as a result of the draft regulations being passed, as set out in our response to Q23.

Appendix 2: Alternative approach to funding and investment strategy for all schemes, includes schemes that are not maturing

During our engagement with the DWP, we outlined an alternative approach to setting a funding and investment strategy which we believed would allow the DWP and TPR to regulate the wide range of schemes they are responsible for. Under this approach, trustees and employers would still set a low dependency target, but would only start moving towards this target at such time as the rate of new entrants slows materially or stops, such that significant maturity and the relevant date can be identified. In the meantime, a contingency plan is put in place, including an agreement on how the trustees and employer expect the low dependency target would be met by the relevant date if the scheme were to begin maturing, for example as a result of the employer closing the scheme to new entrants and / or future accrual. This may require additional contributions to be made by the employer in the event of the contingency plan needing to be triggered. This contingency plan would essentially require significant maturity to be calculated in three scenarios:

1. With an appropriate allowance for new entrants;
2. With no allowance for new entrants, but allowing for future accrual for current actives; and
3. With no allowance for new entrants or future accrual.

If the first calculation does not have an answer, because the rate of new entrants means the scheme is not expected to reach significant maturity for the foreseeable future, the trustees and employer would still be required to put in place a funding and investment strategy. This would set out a strategy for ensuring that pensions and other benefits can be provided over the long-term (as per the legislative requirement), but based on a realistic assumption about the flow of new entrants.

The second and third scenarios make no allowance for new entrants. They will therefore always give an answer, showing the date at which the section would be expected to reach significant maturity, if its circumstances were to change. The results of these scenarios could therefore inform the approach the trustees would expect to adopt if the employer took a decision which changed the future maturity of the scheme, such as closure to new entrants and / or future accrual. This could be considered to be a contingent journey plan for schemes that are open to new entrants, which would only be put into place if the employer chose to close the section (or otherwise materially reduce the flow of new entrants).

This would allow trustees to reach a conclusion on whether the contingent journey plan would be realistic and appropriate, taking into account the current funding position, the trustees' view of an appropriate level of risk to take over the journey plan, and the period over which low dependency would need to be achieved. If the trustees did not consider that the contingent journey plan was appropriate, for example low dependency could not be reached within the period to significant maturity with an acceptable level of risk, then refinements would be required. One possible approach could be to agree that the employer would make additional contributions after closure, if this would be needed to give an acceptable journey plan. This could involve the employer retaining some of the existing contributions being paid in respect of the accrual of benefits, with them instead accelerating the journey to low dependency after closure (rather than simply falling away).

Incorporating these issues into a funding and investment strategy would be a valuable component of integrated risk management, both for trustees and employers. The approach above would allow all parties to better understand the risk being taken in the scheme, and the extent to which these risks and contribution requirements would change if the scheme were to be closed to new members and / or accrual by the employer.