

Pension Trustee Liability

Defined contribution schemes

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What are the risks?

With the risks associated with defined benefit schemes well documented, it may only be a matter of time before defined contribution schemes become the focus of litigation as they follow the trend of pension arrangements moving from defined benefit (DB) to defined contribution (DC).

For those employers and/or trustees who thought they were shifting the risk from themselves to members when moving from DB to DC, the claims of the future may just prove this assumption to be inaccurate.

The Pensions Regulator (TPR) has recently changed its focus, largely prompted by the implementation of auto-enrolment. Millions of people over the next few years will be contributing towards their retirement and the arrangement provided will undoubtedly be of a DC nature. Improving outcomes for DC scheme members is therefore an area of increasing focus for the regulator. TPR laid out its six principles for good defined contribution schemes in 2011 and they formed the foundation for a set of 31 quality features for DC schemes included in the TPR's draft code of practice, which it consulted on earlier in 2013.

In its latest scheme governance survey the TPR found 76% of schemes were aware of the principles, but only 31% said their scheme currently complied with them all - 18 months after the principles were published.

DC code at a glance

- The code contains detail and examples of:
- The scope of trustees' powers under the rules
- Key issues to be considered at trustee meetings
- Expected levels of trustee knowledge
- Internal risk management controls
- Setting investment strategies and default funds
- Security and liquidity of scheme assets
- Acting in members' best interests
- Appointing advisers
- Employer and member-nominated trustee engagement
- Administration and record-keeping
- Maintaining and monitoring contributions

The Pensions Regulator's defined contribution code of conduct has created a "paradigm shift" in trustee knowledge requirements and leaves trustees far more open to criticism, industry experts claim.

Subject to Parliamentary approval, the code will come into force in November 2013. At that time TPR will also publish further guidance containing practical examples of how trustees should use the code.

The TPR's recent scheme governance survey also highlighted further areas of concern.

Most notably only 54% of schemes said they had reviewed their Statement of Investment Principles (SIP) in the last three years. This is despite the fact that it is a legal requirement for them to do so at least once every three years or after any significant change to the scheme's investment portfolio.

Even more worrying is the fact that 8% of those who took part in the survey said they had never reviewed their SIP, while 12% said they didn't know when they last reviewed it, and 14% didn't even know if their scheme had one.

This is worrying because if trustees are not checking these things then who is? Are many DC members being offered investment strategies that just aren't up to scratch? Are these schemes leaking money in terms of cost and poor investment performance that could be prevented?

DC schemes along with DB also need to ensure they are compliant with TPR data accuracy requirements.

In 2010, The Pensions Regulator set specific targets for schemes to achieve by December 2012 regarding 'common data' - such as name, address and date of birth:

- 100% to be in place for member data created from the beginning of June 2010
- 95% for member data created before June 2010

By now, the regulator expects schemes to have taken significant steps to meet these targets including measuring their scheme data and, where data is poor, having plans in place to correct it. Failure to take steps to ensure the completeness and accuracy of data held by a scheme may lead to a breach of internal control requirements. Such breach may result in enforcement action being taken as well as the imposition of fines.

With DC now taking centre stage, it is important that trustees of Trust-based defined contribution schemes ensure they have the right Pension Trustee Liability Insurance in place. To discuss further please contact your local Chubb Financial Lines underwriter.

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