

PASA Consultation response

DWP Consultation: Extending CDC to
unconnected multiple employer pension
schemes

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PASA 



DWP Consultation: Extending CDC to unconnected multiple employer pension schemes

Section	Content	Page
1	Introduction	1
2	Consultation response	3

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About PASA

The Pensions Administration Standards Association (PASA) was created to provide an independent infrastructure to set, develop, guide, and assess administration standards.

PASA acts as a focal point and engages with industry and government to create protocols for understanding good administration - but also appreciates there's no one size fits all. PASA develops evidential Accreditation practices allowing benchmarking across and between the industry regardless of how the administration is being delivered.

As well as raising the profile of pension administration generally, PASA focuses on three core activities:

1. **Defining good standards of pensions administration relevant to all providers, whether in-house, third party or insurers**
2. **Publishing Guidance to support those standards**
3. **Being an independent Accreditation body, assessing the achievement of good standards by schemes**

There's no organisation providing such services across schemes, yet there's a demand for evidence of service quality from scheme trustees, sponsors, administrators, insurers, savers and regulators.

1 Summary

Earlier this year, PASA published a paper [Initial observations on CDC developments](#) which commented on recent policy and regulatory references to Collective Defined Contribution (CDC) arrangements.

CDC is currently seen as a potential means of addressing important questions about the nature of pension saving and how innovation can be combined with scale, choice, and support in decision-making to provide new opportunities for improving saver outcomes. If this consultation leads to legislation permitting unconnected multiple employer CDC arrangements (UME CDC), pension scheme administration products and services will need to develop and adapt to accommodate such arrangements.

There are risks to consider and some were set out in the previous PASA paper noted above. We agree it makes sense to operate an authorisation process and regulatory oversight to protect members of UME CDC schemes and build confidence in such pension arrangements for the future. We also support the proposed approach which should be similar to (but distinct from) the framework applying to single or connected employer CDC schemes. We've approached our review of the draft regulations on this basis.

2 Consultation response

Given our focus on pensions administration, we haven't answered each of the specific questions within the consultation. However, we have commented on the general approach and highlight areas the DWP should consider.

Use existing frameworks and terminology where possible

The DWP's proposals to use the existing CDC regime, where appropriate, and then draw on parallels with the DC Master Trust regime are sensible. As the industry is familiar with this regime, key concepts and legislation in relation to it should be used wherever possible rather than introducing new concepts or requirements. For example, the defined terms used to explain the difference between 'connected' and 'unconnected' employers borrow similar concepts and will be embedded within the existing CDC framework. This approach makes it easier for those applying the regulations to navigate their way through the legislative requirements.

The consultation doesn't address what will happen when there could be an overlap between the UME CDC regime and the DC Master Trust regime. For example, if a DC Master Trust sets up a new UME CDC section. It would be helpful to understand the DWPs thinking on this point.

Trustee duties

As UME CDC schemes will be occupational trust-based pension schemes, any proposed designs will need to be consistent with overriding trustee duties, including acting impartially between members and treating members fairly. There are elements of this within the consultation documents, such as creating new sections and planning member communications carefully. However, the Code of Practice adopted for UME CDC should explicitly reference the importance of meeting trustee duties. As when administering a pension scheme, day-to-day questions arise and it's not always possible to answer by means of checking what statute or regulation states. Trustees often need to apply trust law principles to the facts in front of them when making decisions, particularly where difficult questions could arise around fairness and intergenerational matters. These are even more likely to happen in UME CDC schemes.

Administration considerations

The following issues need to be carefully considered from an administrative perspective.

Record keeping – it's made clear in para 55 actuarial equivalence testing will require excellent DC record-keeping, or the process won't be effective. DC record-keeping sometimes goes wrong, and mistakes happen. It's unclear how such mistakes should be addressed and the consequences from a regulatory perspective if errors hinder the actuary's ability to conduct and approve the live running test. This could be a key risk factor in operating a UME CDC because of the trustees' reliance on third parties outside their control (i.e., payroll functions of individual employers as well as the administrator of the UME CDC). This may need extra scrutiny/safeguards as a result.

Communication requirements – Para 96 references the importance of IT systems' functionality, quality and maintenance for delivering scheme communications; this is an integral part of the authorisation process. We also

note there's an ongoing requirement for quality assurance systems and a feedback loop so members understanding of what the communications are telling them can be assessed. It would be helpful to understand more about how these are expected to operate and what responsibility the administration team will have to ensure these operate effectively.

Systems and processes for administration– Paragraph 98 sets out this key requirement. IT systems must have the capacity and capability to reconcile employer contributions with member records. However, as noted above, this also requires employer systems to operate effectively, so understanding and communicating the responsibilities between the relative parties in advance will be important. Regarding compliance-related matters, we anticipate the Pensions Regulator will need to consider third-party involvement as a critical consideration.

Responses to specific questions

A. Sections of a Multi-employer CDC scheme

Question 1: Do you think draft regulation 25 delivers the policy intent for the opening of a new section for unconnected multiple employer CDC schemes?

New terminology is needed to cover what 'sections' mean in a UME CDC scheme. The paragraphs of the consultation (paras 13-17) explain what happens when a new section is needed because conditions have changed and the original scheme design is no longer viable. For example, a scheme can no longer present itself as providing a 1/80 target pension with CPI increases. A UME CDC scheme could have different 'targets' for other employers. Employer A may favour an accrual-based approach – e.g. the Royal Mail-type structure. Employer B may favour a more DC-oriented or points-based approach – where the target benefit is based on the projected outcomes of all member plus (uniform) employer contributions to the scheme. It's not clear whether both types of these sections would be permitted under the same UME CDC scheme.

B. Viability Report

Para 42 clarifies the scheme proprietor must approve a viability report – consistent with cooperation between them, the trustees and the scheme actuary. We support this approach, however it's unclear what will happen if there's a difference of opinion. If the proprietor doesn't want to trigger the change in the scheme benefits a revised viability report might indicate, could they use a power of veto over the production of the revised report to pressure the trustees (and scheme actuary) to change their minds? The trustees are the ultimate protectors of members' benefits, and the balance of power between the trustees and the scheme proprietor should be on the side of the trustees.

C. Actuarial Equivalence Test

Question 6. Do you have any comments on the drafting of the actuarial equivalence test?

Figure 1 in para 61 clearly states actuarial equivalence can be satisfied at a member level or employer level. This is consistent with different approaches to benefit accrual, as outlined above. If two employers are participating with 15% contributions, and Employer A is paying 15%, consistent with a 1/80th target benefit. In contrast, Employer B uses

the accumulated 15% contributions to provide a DC-style member target benefit. Could they both take place within the same UME CDC scheme and will they both work at the inception of each employer's participation and on a live-running basis?

D. Scheme Proprietor requirements

Para 76 states *“To avoid any potential conflicts of interest, section 14C would also require that the scheme proprietor only carries out activities that relate directly to unconnected multiple employer CDC schemes of which it is the scheme proprietor or prospective scheme proprietor.”*

This is similar to a requirement in the DC Master Trust regime relating to the role of scheme funders and it's intended to make the financial operation of the scheme proprietor transparent. However, this isn't always straightforward to manage from a commercial perspective and the best entity to be the scheme proprietor for a UME CDC scheme might well be the top company in a group. To require a new entrant to set up a new corporate subsidiary to act solely as proprietor to a UME CDC scheme may limit the attractiveness of setting up a scheme and make it unworkable if the intention is to permit DC Master Trusts to operate UME CDC. It may be necessary to consider offering an exemption from this requirement in certain circumstances, similar to the approach within the DC Master Trust regime.

E. Promotion or marketing activities

Question 8: Do you have any comments on the draft regulations on promotion or marketing?

Para 86 states: *“We propose that trustees of unconnected multiple employer CDC schemes cannot undertake promotion or marketing activities.”*

In practice, this may not be straightforward to operate. From a commercial perspective, when an employer is considering which UME CDC scheme to choose for its employees, part of its selection and due diligence may involve meeting the scheme's trustees to understand if they're appropriate custodians of their employee benefits arrangements. Trustees may 'accidentally' become involved in what may be construed as marketing activities unless it's very clear where the line is drawn between providing information to prospective new employers looking to join the UME CDC and actively promoting or marketing the scheme.

F. Continuity Strategy

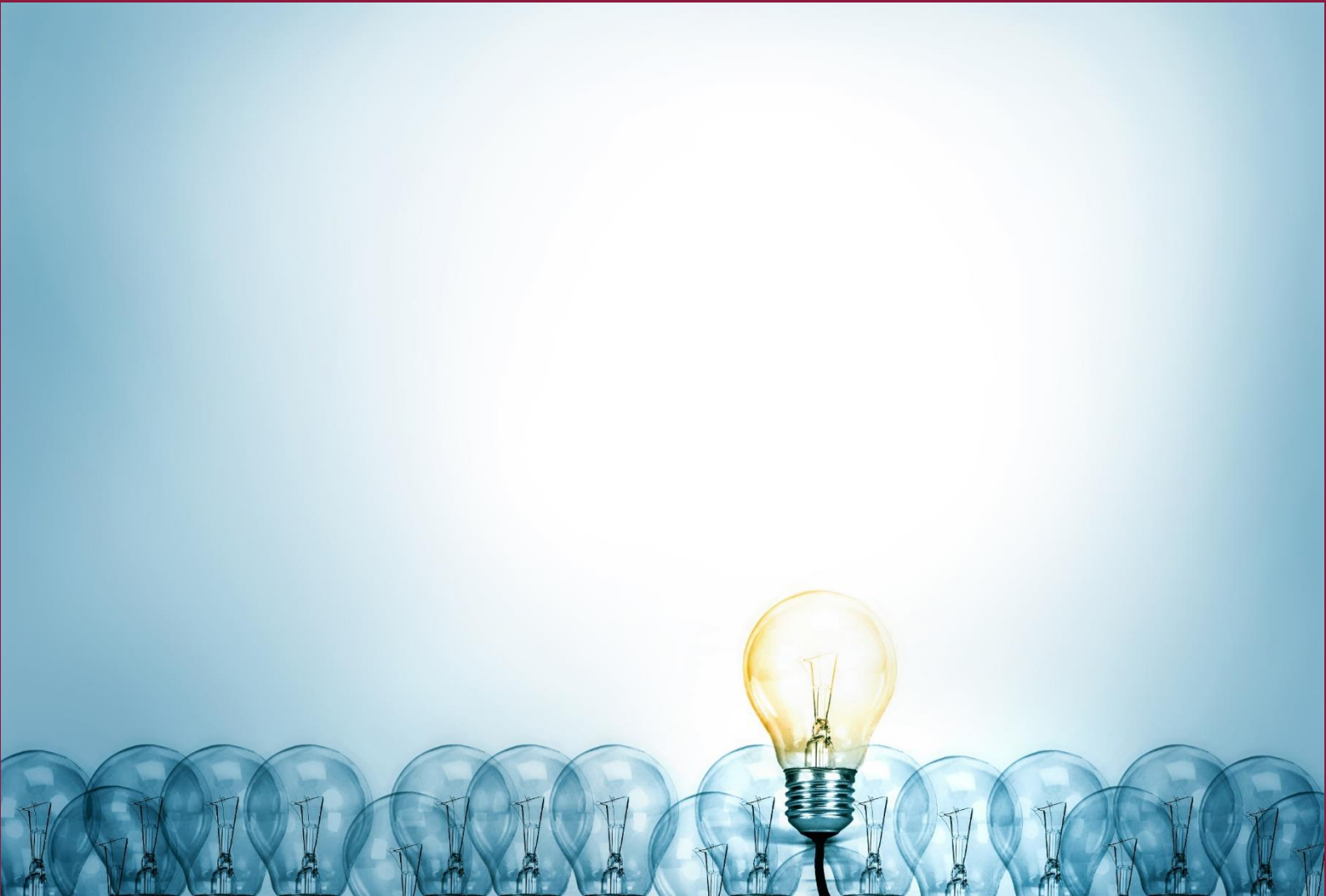
It would be helpful to understand if it's envisaged a different continuity strategy could be pursued for each separate employer participating in a UME CDC scheme. It may be if one employer section has been closed to new members for some time, then the trustees believe the section should be transferred elsewhere. The basis on which such a decision should be made, and considerations facing the trustees, could differ depending on the section and each employer within the section. This should be considered as part of the UME CDC framework so duties and options are clear before such a scheme is set up.

G. Valuation and Benefit adjustment

Question 10: Are the draft regulations clear on how valuation and benefit adjustments should happen?

Para 117 states, "*adjustments of the rate or amount of benefit provided under the scheme must be applied to all the members of the scheme without variation*", whereas Para 120 talks about "*Where scheme rules allow for members' benefits to target different annual increases based on their employer...*".

The intention seems to be that uniform adjustments should apply within each employer section, but the rates can vary across different employer sections. It would be helpful if this could be clarified.



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