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Current issues

May 2025

Articles this month:

DB annual funding statement

On 29 April 2025, the Pensions Regulator issued its Annual Funding Statement for 2025, concerning private-sector defined benefit (DB) schemes. Its main themes are endgame planning, use of surplus, and market volatility; and it provides helpful guidance on questions arising from the new funding rules on matters such as the assessment of employer covenants and supportable risk, and what 'proportionality' might mean in practice.

The Statement is most relevant to schemes producing valuations at dates in the period from 22 September 2024 to 21 September 2025, which will be the first to be conducted under the *Pension Schemes Act 2021* reforms and the new Funding Code of Practice.[1] However, many of the themes will be of interest more widely.

The state of play

Most trustees are likely to be approaching valuations from a relatively healthy funding position. Continuing the improvement trend seen in recent years, as at 31 December 2024, the Regulator believes that 54% of schemes were fully funded on a buy-out basis; 76% on a low-dependency funding basis; and 85% on the basis of their technical provisions. It anticipates that the overall funding position continued to hold broadly true on 31 March 2025. Consequently, it expects that the trustees of most schemes will shift their focus away from deficit concerns and towards endgame planning. It intends to publish guidance on endgames '*in the coming weeks*'. It

[1] The Regulator would previously have described this collection of cyclical valuations as belonging to 'Tranche 20', but has made a slight change in its nomenclature. It refers to it instead as 'Tranche 24/25', making it easier to locate a particular tranche in time than was the case under the historical sequential-numbering system.

also encourages trustees to draw up policies on use of surplus, and to consider how they might respond to a sponsor's request for a refund.

As a counterpoint to this generally rosy assessment of the current state of affairs, the Regulator cautions trustees about the potential effects of an extended period of geopolitical and macroeconomic instability. It expects them to understand the possible implications of continued volatility for their sponsor covenant and investment strategy. They should also consider the potential impacts of the adoption of artificial intelligence technology and transition to more-sustainable energy sources.

Submitting valuations

The online (spreadsheet-based) '*Submit a scheme valuation*' service, for valuations at dates on or after 22 September 2024, should be available shortly (in '*Spring 2025*' or '*In coming weeks*'). The Regulator intends to publish a response to its statement-of-strategy consultation exercise at the same time. Until the new service is operational, trustees should not attempt to submit Tranche 24/25 valuation documentation, and will not be penalized for late compliance; however, the Regulator says that they should not delay completion of their valuations on that basis.

The Regulator will be '*risk-based and outcome focused*' when deciding which schemes require further interaction. The Regulator estimates that 80% of schemes could take the lighter-touch 'Fast Track' route to valuation compliance at minimal or no additional cost to their sponsors. If a scheme adopts the 'Fast Track' parameters, it is less likely that the Regulator will engage (though it's careful to say that the Bespoke route is '*equally valid*'). It has decided against making any changes to the parameters released in November 2024.

Diff'rent strokes for diff'rent folks

The Regulator continues its practice of grouping schemes by funding when providing guidance on expectations:

Funding position	Expected area(s) of focus
Fully funded on low-dependency basis	• Endgame planning • Risks/benefits of running on • Monitoring and management strategies
Fully funded on TPs but below LDFB	• Achieving low-dependency funding by relevant date
Below TPs	• Deficit recovery as quickly as reasonably affordable • TPs consistent with journey-plan position • Risks commensurate with covenant and maturity

Supplementary guidance

Appendices to the Statement provide clarification of the new funding rules. One answers questions about the Regulator's covenant-assessment guidance, and the other explains its position on consideration of supportable risk. It's clear that a proportionate approach can be taken to covenant assessment where future reliance on the employer is low.

Detail on how the Regulator will assess the first submitted valuations is still relatively sparse. Until a clearer picture emerges, the appropriate balance to be struck between rigour and proportionality will remain somewhat fuzzy. However, although there is little in this year's statement by way of new technical guidance, there are some helpful clarifications to help put theory into practice. The Statement says that trustees should set aside sufficient time to consider the new requirements, working collaboratively with their sponsors and advisers during the valuation process, and plan upfront to focus on what's important.

More generally, trustees and sponsors should, as encouraged by the Regulator, take the opportunity to pause, take stock, and review their plans. The exercise will be most effective and rewarding if they work together. They should also look ahead to the government's anticipated easing of surplus-refund rules to inform this long-term planning.

Decluttering DC pots

The Department for Work and Pensions (DWP) has confirmed plans to establish a mechanism for the automatic consolidation of small, deferred defined-contribution (DC) pension pots, and revealed some of the policy decisions that will shape the new system.

The Labour Government announced its intention to legislate for automatic transfers in July 2024, via the medium of the King's Speech, delivered at the State Opening of the current parliamentary session. At that time, information about the likely features of the nascent system was sparse. Previously, under the auspices of the Conservative Party, the DWP had indicated its intention to pursue a 'multiple consolidator' model for the system, under which a few authorized schemes would act as automatic destinations for small, inactive DC pots, using a central clearing house. It established a Small Pots Delivery Group ('the Group'), in February 2024, to provide recommendations on how to proceed.

Now, in response to a report from the Group, the DWP has decided that—

- the foundations for a system of automatic transfers for small DC pots[2], adopting the multiple-default-consolidators model, should indeed be included in the forthcoming Pension Schemes Bill;
- a feasibility study will explore the requirements for a Small Pots Data Platform (the auto-consolidation infrastructure) with the hope that some aspects of the design of the pensions dashboards system can be replicated and adapted for the purpose;
- it will explore the Group's preference for the Data Platform to operate on a not-for-profit basis, and generally funded via the general levy on pension schemes;

[2] Initially, those up to £1,000.

- development of the automatic-transfer system should not be allowed to hinder the establishment of the dashboards;
- initial communications with members about auto-consolidation should be the responsibility of the ceding scheme—the DWP will consider imposing information-sharing obligations upon employers;
- unless the member has expressed a choice (or opted out), the allocation will go to the consolidator holding the member's largest pot, with a 'carousel' system in place for those who don't have a pot with one of the authorized consolidators;
- it will be a single-tier, whole-of-market consolidator system (some Group members favoured a two-tier system, involving some consolidators that only take on pots from their existing members, and those willing to accept anyone), under a legislative framework that's capable of including GPPs as well as master trusts;
- the industry should work on improving efficiency so that it can process the likely level of transfers, at low cost, when the obligation becomes active; and
- implementation should be staged and phased (with details to be confirmed).

It's anticipated that the feasibility review, led by the Pensions and Lifetime Savings Association, will report back to the DWP in June, so that its conclusions can be taken into account in the drafting of the Pension Schemes Bill. Implementing regulations will be drafted in 2026, in consultation with the industry. Although aspects of the legislation will come into force during 2027 or 2028, the duty to consolidate will probably not become effective until 2030.

The DWP's plans are a step in the right direction. There are several hurdles that will need to be cleared, but the Government's willingness to work with the pensions industry to find the best approach should help to build trust in the system. It will be a great achievement if it's up and running in 2030.

Parliamentary proceedings

The denizens of Westminster touched on pensions issues several times during the month of April. Here's a highly condensed selection of highlights.

Statutory indexation (or absence thereof)

Responding to a Written Question in Parliament asking whether the Government '*plans to require profitable companies to increase pre-1997 occupational pensions in line with inflation*', Torsten Bell, the Pensions Minister, said that its forthcoming defined benefit (DB) surplus reforms '*will make it easier for individual schemes to make decisions that improve outcomes for both sponsoring employers and members, which could include discretionary benefit increases.*'

Fiduciary duty

Answering a small flurry of environmental, social and governance (ESG)-related questions from Mary Glindon MP, Bell said (amongst other things) the Government is '*not currently considering any change to the law*' on trustees' fiduciary duties.[3]

[3] <https://questions-statements.parliament.uk/written-questions/detail/2025-04-08/44970>,<https://questions-statements.parliament.uk/written-questions/detail/2025-04-08/44971>, <https://questions-statements.parliament.uk/written-questions/detail/2025-04-08/44972>, <https://questions-statements.parliament.uk/written-questions/detail/2025-04-08/44974>.

State-scheme integration (AKA clawback)

At a recent adjournment debate, Bell said (again, amongst other things) that the Government '*cannot retrospectively change the benefits schemes offered their members.*' The comment was made in response to calls to outlaw 'clawback' arrangements, under which occupation pension calculations take account of members' State pensions in order to provide them with (more or less nearly) level incomes throughout their retirements.

Responses to W&PC recommendations

The Government has responded to the Work and Pensions Committee's March 2024 report on *Defined Benefit Pension Schemes*. Perhaps reflecting the sizable lacuna since the report's publication (in fairness, there was an intervening change of government), the answers seem to mainly rehash known developments and policy announcements. In the 'more-newsworthy' column, the Government plans to consult on professional trustee accreditation and scheme governance measures '*later this year*'; talks about the possibility of establishing a '*small, focused*' PPF-run public consolidation vehicle for DB schemes; and seems rather lukewarm on the idea of improving the Pension Protection Fund's indexation terms.

Multi-employer CDC

It didn't happen in Parliament, but the Pensions Minister confirmed that the regulations allowing collective defined contribution (CDC) schemes to cover unconnected employers will be laid this autumn, with the intention that they will come into force (along with an updated Code of Practice from the Pensions Regulator) shortly thereafter. Bell also expressed interest in pursuing 'decumulation-only' CDC schemes, as a potential new retirement-income option, but the indication there was just that the Government would continue to work with the pensions industry to develop the proposition.

PPF plugs priorities

The Pension Protection Fund (PPF) has published its strategy for 2025 – 28. Its priorities for this period include; working with the Government on levy-legislation amendments, reviewing its indexation levels and preparing to make data available to the pensions dashboards.

The envisaged legislative changes would enable the PPF to set the levy at zero, but also allow it to be quickly reintroduced if necessary. Some of that can be achieved by secondary legislation, but other aspects will need to be included in an Act of Parliament. The PPF is also considering the changes necessary to remove the administration levy, which recoups the Department for Work and Pensions' outlay on the establishment and expenses of the PPF now that its funding has reached the point at which it's self-supporting.

The PPF says it will work with the Government to move forward with a review of the rules governing indexation of compensation. This recognises the need to reconsider the non-indexation of compensation attributable to pre-6 April 1997 service, as recommended by the House of Commons Work and Pensions Committee in March 2024.

It also aims to finalise all known applications to the Fraud Compensation Fund (FCF) and work with the DWP and Pensions Regulator to determine whether any future claims on the FCF are likely.

Kapow! Exploding DB superfund myths

The Pensions Regulator has published a blog on the process of transferring members into a DB superfund. It aims to dispel some 'misconceptions' about the expectations that it has for trustees in such cases.

The blog reflects on experience from the first three superfund transfers and addresses some ‘friction points’ that were observed. In summary:

- an actuary’s estimate of the costs of buying out (for the purposes of Gateway Test 1) is acceptable (no need to obtain quotes from insurers);
- trustees aren’t expected to duplicate the Regulator’s assessment process for superfunds when performing due diligence on a candidate;
- an extensive rationale for the transfer needs to be established, especially when a transferring scheme has ongoing sponsor support;
- the requirement that the superfund transfer would improve the chances of members obtaining their full benefits (Gateway Test 3) may not always necessitate exploration of mathematical probabilities and detailed modelling; and
- the Regulator is prepared to accept ‘boundary conditions’ (clauses in transfer agreements that prompt revision of their financial terms in response to changes in market conditions) that cease to operate at the point when scheme members are informed about the impending transfer, as long as a rationale is provided.

HMRC newsletters

Pension Schemes Newsletter 169, from His Majesty’s Revenue and Customs, includes the following:

- confirmation that the online Managing Pension Schemes (MPS) service now allows for the submission of pension scheme tax returns for the year 2024/25 (and will be the only way to submit such returns for that and subsequent tax years, so there’s also a section about migration of existing schemes to the MPS);
- the deadlines for applying for the 2016 flavours of fixed and individual protection from the lifetime allowance, and international and pension credit enhancements, have passed; the look-up service that allows trustees and administrators to check whether members have valid protections should appear on the MPS '*in late 2025*' (meanwhile, the service allowing members to check their protections via their online tax account has been re-labelled '*Check your pension protections*' and is set to be 'enhanced' later this year);
- a statement that managers of EEA-based qualifying recognized overseas pension schemes (QROPS) have been warned that they will cease to qualify unless, by 7 May 2025, they confirm that they satisfy the conditions applicable to other overseas jurisdictions;
- updated statistics on use of the defined-contribution flexibilities and scheme registrations; and
- a call for volunteers to help test the aforementioned look-up service, the overseas transfer form, and the online pension scheme return.

Qis custodiet ipsos custodes?

The Pensions Regulator announced plans for a '*framework for oversight of professional trustees*'. It also published a market oversight report based on work with 11 of the largest trustee firms.

The Regulator says that it will begin establishing supervisory relationships with firms during the summer, and will cover them all by the end of the year. Areas of particular interest include business models, relationships with sponsors and advisers, and the trustees' decision-making and internal controls.

You're NIC'd

The legislation implementing the Budget-announced changes to employer National Insurance Contributions (NICs), received Royal Assent on 3 April and came into force from 6 April 2025. The *National Insurance Contributions (Secondary Class 1 Contributions) Act 2025* provides for a 1.2 percentage points increase in the rate of employer NICs (raising them to 15% of relevant earnings), and a lowering of the earnings threshold for liability (from £9,100 to £5,000 p.a.).

And Finally…

With a large number of 'deliverables' (the final report from Phase 1 of the Pensions Review, consultations on Unlocking the UK Pensions Market for Growth, the Local Government Pension Scheme (England and Wales): Fit for the Future, and Options for Defined Benefit Schemes…) promised for '*Spring*', AF feels it is opportune (nay, seasonal) to note that government departments have historically favoured the astronomical definitions of the seasons. By that we do not mean that they lean towards verbosity (like that opening sentence). Rather, the astronomical seasons are defined by the position of the Earth in its orbit around the Sun. Using that system, the seasons are demarcated by the vernal and autumnal equinoxes, and the summer and winter solstices.

Alternatives include the system commonly used by meteorologists, under which (in the northern hemisphere) spring is rather unimaginatively deemed to cover the months of March, April and May; summer is June, July, and August; autumn stretches from the beginning of September to the end of November, and winter covers December to February. Or one could just do what normal people do, and say, 'Nope, it's still Baltic in here—the heating's staying on', or 'Oh, bloody hell, I'm going to have to start cutting the grass again.'

The significance of the Government's bias towards the astronomical definitions is that this spring will not end until 21 June 2025. Coincidentally, that's the day before Parliament dusts off its flip-flops and inflatable bathing rings and trots off for the summer recess. AF is rather charmed by the notion of the Ministers phoning the Astronomer Royal to ask when the Sun will reach the highest point in the sky this year, because that's the latest they can put things off…

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