Spotlight on Pensions
PRESENTS
Le Grand View

DECEMBER 2019

The future of pensions regulation – cost vs benefit

A watershed in the regulation of workplace pensions is approaching. A number of developments on aspects of the regulatory system have been progressing largely in isolation, each considered in the context of the present system.

These are now coming to a head and for perhaps the first time we are able to see the whole picture of the future and the implications for those involved in all aspects of pensions provision. Those implications are potentially very significant, emphasising the need to couch responses to each proposal in the context of its place in, and effect upon, the wider system.

The Pensions Regulator

In response to criticism, particularly from the Work and Pensions Select Committee, TPR has embarked on a major upgrading of its involvement in the running of schemes. This is turning it from a risk-based regulator to one that exercises active control at increasingly more micro levels. In addition, new legislation is proposed to create additional offences and to give TPR new powers to pursue and punish transgressors.

New legislation was set out in sections 103 to 117 of the Pension Schemes Bill. It has fallen as a result of the General Election, but since it apparently enjoyed all-party support it is very likely to reappear in the next parliament. If enacted these provisions, in the context of TPR's new closer monitoring approach, would represent a significant increase in regulatory involvement in a broad range of daily activities both directly in respect of the operation of schemes themselves, and in regular supporting business operations. The latter would potentially bring into scope a wide range of people involved in business activities with an employer, but who may not have any direct involvement with the scheme.

At the same time, TPR is stepping up its monitoring of schemes of all sizes. It has instituted a programme of close involvement with a number of large schemes and is intending to roll out the programme to more. In response to evidence that smaller schemes are less likely to be wholly compliant with the minutiae of current regulatory requirements, they are also increasing focus on how those schemes are run, against the background of an institutional policy of driving consolidation of smaller schemes into larger arrangements.

Direct Government involvement

The Government has recently involved itself directly in regulatory affairs, potentially widening – and muddying – the regulatory environment. The Pensions Minister has written to 50 of the largest schemes requiring them to outline their ESG and stewardship investment principles and report in line with the Task Force on Climate-related Financial Disclosures framework.

Such intervention is not a welcome development. If direct involvement in regulatory matters by the Executive is to become a feature of the ongoing regulatory system, then it needs to be properly integrated, including being subject to appropriate scrutiny and review. Planned integration will be necessary to avoid duplication and the risk of contradictory requirements being placed upon schemes, and a consequent increase in their workload.

In response to criticism, particularly from the Work and Pensions Select Committee, TPR has embarked on a major upgrading of its involvement in the running of schemes.

Costs – the elephant in the room

Consideration of any regulatory system must include a cost/benefit analysis. Costs must be proportionate and affordable, requiring compromises on all sides.

The issue has been brought into sharp focus in the DWP's consultation document: The Occupational and Personal Pension Schemes (General Levy) Review 2019. This gives the first clear picture of the cost of the new regulatory effort.

The picture is not a happy one. Although the levy also funds the work of bodies such as the Money & Pensions Service and The Pensions Ombudsman, the lion's share of the costs will be attributable to the direct regulatory effort of the new-look TPR.

The figures are skewed to some extent by the fact that the levy has remained unchanged since 2013 (apart from a reduction in 2018/19 for schemes with over 500,000 members), despite cost increases over that period. Nevertheless, the figures are significant by any standards. A surplus of £24m in 2013 has become a deficit of £16m in 2019, which if no action is taken, will become a deficit of £50m by 2020. This feeds through to the need for eye-watering increases to the levy going forward.

As the consultation document observes "… a natural consequence of increased activity is additional pressure on levy expenditure. Without an increase in the levy rates or a significant reduction in the activity of the levy-funded bodies … the "deficit" is likely to continue to grow significantly". Clearly the cost/benefit assessment is central to any review of future regulatory efforts.

Any assessment of costs should also include those arising from the additional work required to meet the new regulatory rules.

Multiple or single regulator?

TPR's approach is not the only change in financial services regulation. In a recent speech on wider financial regulation, FCA Executive Director for Strategy and Competition Christopher Woolard announced its own review: "We will be issuing an open invitation for [public] thoughts and ideas, as well as setting out some of our own. And we'll publish detailed papers, including an analysis of future market dynamics, a Discussion Paper about our Principles, and a Consultation Paper on the Duty of Care."

Given announcements of closer working relationships between the FCA and TPR, it is likely that thought will once again turn towards whether it is appropriate to continue to have two separate regulators involved in pensions. From a cost perspective, there may well be savings to be made from bringing them together, although the opposite might be the case if the resultant organisation itself becomes too large for effective oversight.

Given announcements of closer working relationships between the FCA and TPR, it is likely that thought will once again turn towards whether it is appropriate to continue to have two separate regulators involved in pensions.

The issue also involves important considerations around the different approaches to their respective constituencies, although with the blurring of pensions with other financial arrangements, and TPR's closer regulatory involvement, those distinctions are diminishing.

Focus on the wider issue

So, all this adds up to a sea change in the regulation of late life financial provision. It will be important that forthcoming decisions are taken against the wider background, even though many of them will arise in consultations on narrower subjects, such as the General Levy.

Under that particular consultation, the Government's preferred option is for an interim increase in the levy, allowing time for a more detailed review of the levy. That is encouraging if it leads to a consideration of more fundamental questions around the future regulatory system as a whole. If the forthcoming FCA review then fed into this, it would provide an opportunity to craft an integrated approach for the future. Meanwhile a detailed analysis of the likely practical effects that would have resulted from the now defunct Pension Schemes Bill would add context as an example of how the proposed direction of travel would impact the sector in future. Whatever the final details, it seems that regulation is certain to change.

Pendragon
Wilmington Risk & Compliance