

Pensions Update - Special Edition

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BAKER & MCKENZIE

The New DC Code and "How to Guides"

A significantly revised Defined Contribution ("DC") Code of Practice came into force on 28th July (the "New Code"). To coincide with this, the Pensions Regulator ("tPR") has also published six "How to Guides" (the "Guides") which sit alongside the New Code. The New Code is relevant for trustees of occupational pension schemes providing money purchase benefits including those providing money purchase benefits solely through Additional Voluntary Contributions ("AVCs"). Further detail about precisely how the New Code will apply to different types of schemes in different scenarios is given below.

The New Code replaces the previous Code of Practice no.13: Governance and administration of occupational defined contribution trust-based schemes, dated November 2013 (the "Old Code").

This note provides a summary of some of the key aspects of the New Code and accompanying Guides and considers what steps trustees should now be taking.

Why is the Old Code being replaced?

There have been several drivers behind the introduction of the New Code, including:

- a desire by tPR to make the New Code and Guides clearer and easier to use;
- an increasing focus by tPR on schemes providing money purchase benefits with the advent of auto-enrolment;
- a need to reflect legislative developments since 2014 which have impacted schemes providing money purchase benefits; and
- a recognition that, at the time that the Old Code was drafted, much legislation was not designed for schemes offering money purchase benefits.

Who does the New Code apply to?

The New Code applies to occupational pension schemes with two or more members (whether active, deferred or pensioner), which offer money purchase benefits. It applies to DC schemes and DC sections within mixed benefit schemes. It also applies to money purchase AVCs within occupational defined benefit ("DB") schemes, money purchase benefits with a DB underpin and money purchase underpin benefits.

However, the New Code applies only *"insofar as the relevant legislation applies"*. One important example of where relevant legislation may not apply is the governance and charge control requirements, which do not apply to a DB scheme where the only money purchase benefits are AVCs.

Navigating the New Code and Guides

The New Code and Guides represent a consolidation of the Old Code and guidance, updated to take into account legislation and best practice since the Old Code was first introduced in November 2013.

The structure of both the New Code and Guides has been re-vamped. The New Code has been split into the following main sections, each of which will be supported by a separate Guide:

- The trustee board.
- Scheme management skills.
- Administration.
- Investment governance.
- Value for members.
- Communicating and reporting.

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If you wish to discuss any of these issues further, please contact your usual Baker & McKenzie lawyer.

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One of the criticisms of the Old Code was that it was too long and difficult to navigate. The New Code is significantly shorter. However, when read together with the accompanying Guides, there is still a lot of material: over 100 pages. TPR has said that it intends the New Code and Guides to be accessed digitally and for readers to have the facility, when reading the New Code, to be able to click through to the relevant part of the Guides.

The New Code is where tPR sets the standards that it expects trustees to meet in order to satisfy the legal requirements. It is designed to assist trustees in satisfying those requirements.

The Guides contain practical information and examples of approaches which trustees might use. The guides are not intended to be prescriptive, although the introduction to the Guides states that "*in some instances they state what we [tPR] consider to be best practice*".

There are statements in both the Code and Guides that make clear that proportionality can play a part in how the Code is interpreted by trustees where the only money purchase benefits are AVCs. The extent to which trustees can do this depends on an assessment of the value of the DC AVCs relative to the DB benefits.

The New Code and Guides will be a key reference point for trustees of DC schemes. They are not, however, a "one stop shop" and trustees of DC schemes (and other types of schemes containing money purchase benefits) will need to continue to refer to other relevant tPR Codes and guidance.

Legal status

The legal status of the New Code and Guides has not changed. A breach of the Code does not result in a direct automatic penalty, but a court or tribunal will take into account whether the Code has been followed when deciding whether or not trustees have breached a legal requirement or expected standard. There is no direct or indirect penalty for failure to follow the Guides, although trustees will no doubt wish to be consistent with the Guides, where possible, as a matter of good practice.

As part of its objective to make the Code and Guidance clearer, tPR has changed the way it uses language. The New Code and Guides use the word "expects" when referring to something the Regulator expects and "the law requires" when referring to a legal requirement, although one of the criticisms levelled at the New Code and Guides is that this has not been consistently applied.

What's new?

Much of the New Code and Guides will be familiar to trustees. However, some key points for trustees to note, including some key points of difference between the Old and New Code, are as follows:

The 31 quality features

The New Code and Guides are no longer structured around 31 quality features, although the spirit of these features has been preserved.

Higher level of knowledge assumed

TPR has assumed that readers of the New Code and Guides have a fairly detailed knowledge of the legal requirements underpinning the Code. This is reflected in the fact that express references to the legal requirements within the main body of the Code have, for the most part, been removed, although cross references continue to be footnoted.

References to new legal requirements

The New Code and Guides have been updated to reflect legal requirements which have been introduced since 2013 (up to and including April 2016), in particular the governance and restrictions on charges legislation and the requirements relating to new DC flexibilities.

Points to note in relation to the Guides

Much of the material which is new has been included in the Guides rather than the Code, including updated examples to take into account developing best practice. Some key points to note in relation to specific Guides include:

Trustee board: some of the guidance and best practice examples contained in this guide are fairly aspirational. It includes guidance on promoting diversity

in the trustee board, places an emphasis on appointing an independent professional trustee "where appropriate" and suggests that a mentoring system could be put in place for new trustees, together with a "fitness and propriety" policy to ensure consistency in approach for their appointment. This Guide also states that trustees should give "serious consideration" to appointing a scheme secretary, either from an external service provider or by using the sponsoring employer's company secretariat - tPR's clear view is that it is best practice to have a scheme secretary in place to assist the trustee board.

Scheme management: this Guide includes the suggestion that the Chair of the trustee board can support the process of trustees' evaluating their own performance by conducting annual appraisals. It also focusses on the importance of working well with advisers, providers and employers, including the suggestion that trustees consider setting up a joint trustee and employer sub-committee to facilitate discussions.

Administration: this Guide contains more detailed guidance than previously. Trustees should also note, in particular, the commentary in the Code and the relevant Guide in relation to the requirement on trustees to process core financial transactions promptly, which include specific timescales.

Value for members: this Guide includes a step by step process for assessing value for members. This is a potentially helpful tool for trustees who are required to assess and report on value for members as part of the annual governance statement, although it still remains unclear what, if any, distinction tPR draws between value for members (perhaps value in return for cost which the member has borne together with the broader member experience) and value for money (perhaps taking account of the employer's perspective).

Communication with members: Appendix 1 to this Guide includes some examples of generic risk warnings which trustees can use to comply with the requirement from April 2016 to provide risk warnings to members as part of the decumulation process (some exemptions and alternative ways of meeting the requirements apply).

Investment governance: this Guide notes the importance of reviewing and negotiating investment management agreements to ensure that what is agreed is appropriate and reminds trustees of the importance of obtaining professional advice to assist them in meeting their investment responsibilities

What do trustees need to do now?

Trustees should take steps to familiarise themselves with the New Code and Guides. There is a lot of material to get to grips with. The trustee board as a whole will wish to understand the key changes being introduced by the New Code and across the various Guides. One strategic approach to this might be to delegate a review of each Guide to a relevant sub-committee of the trustee board and for the sub-committee to consider, with its advisers where appropriate, the impact on the scheme and its operational and governance practices and report back to the full trustee board.

When familiarising themselves with the New Code and Guides, trustees should consider whether their particular scheme meets the relevant standards set out in the Code and to what extent the scheme is complying with best practice. Trustees may also require advice to confirm the extent to which the Code and Guides are relevant to their scheme.

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