Securing the future of pensions

Regulating defined benefit pension schemes: a response by the National Association of Pension Funds

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Executive Summary

The NAPF welcomes the introduction of a new objective for The Pensions Regulator (TPR) to "minimise any adverse impact on the sustainable growth of an employer" and the changing emphasis from TPR in the consultation documents, recognising the importance of the employer's long term support of the schemes.

However, whether the new objective, and TPR's approach to defined benefit (DB) funding generally, is effective will be determined largely by whether trustees still perceive there is pressure from TPR to secure the maximum possible contributions from the employer, in spite of the change in emphasis in the Regulatory Strategy, Code of Practice and Funding Policy. S**uccess will depend on the consistent and accurate implementation by TPR caseworkers in their discussions with schemes and sponsors.**

Feedback we gathered from trustees, actuaries, consultants and sponsors involved in the triennial scheme valuation process suggested that they believed TPR's position was to eliminate as much risk as possible from schemes despite current flexibilities in the system. **We therefore urge TPR to follow through on its undertaking to ensure that scheme risk is managed rather than eliminated and that they ensure this intention is clearly understood by trustees, actuaries, consultants and sponsors alike.**

TPR's interpretation of 'sustainable growth' will need to be carefully handled. Growth can mean something different to different types of sponsoring employer**. It is essential that TPR follows through on its promise to apply a broad interpretation of growth, depending on scheme specific circumstances, and works closely with trustees to ascertain what employer growth means to them.**

It is also vital that the essence of TPR's approach to DB funding is accurately communicated. It is important that trustees are not overloaded with unnecessary information and the Regulatory Strategy, Code of Practice and Funding Policy run to over 130 pages. It is very likely that the important messages could be lost in this volume of text and it is possible that many trustees will just not have the time to fully absorb the entire content. **We would therefore urge TPR to ensure the documentation is as concise and clear as possible**. **In particular we recommend the documents contain a summary of the key messages and best practice principles to help trustees prioritise their time. This will ensure that trustees take on board the essence of the new funding regime and crucial points are not inadvertently overlooked.**

About the NAPF

The National Association of Pension Funds (NAPF) is the leading voice of workplace pension provision in the UK. We represent some 1,300 pension schemes from all parts of the economy and 400 businesses providing essential services to the pensions industry. Ten million working people currently belong to NAPF member schemes, while around 5 million pensioners are receiving valuable retirement income from those schemes. NAPF member schemes hold assets of some £900 bn. Our main objective is to ensure the security and sustainability of UK pensions.

Introduction

Economic conditions in recent years and increasing longevity have put DB schemes under severe funding pressure. The NAPF is committed to working with the Government and regulators to ensure a sensible regulatory environment for DB schemes in the UK.

The Chancellor's Autumn Statement on 5 December 2012 announced that the Government "is determined to ensure that the defined-benefit pensions regulation does not act as a brake on investment and growth." This led to the proposal of a new statutory objective for TPR that is currently progressing through Parliament as part of the Pensions Bill 2013-2014.

The new objective requires TPR to "minimise any adverse impact on the sustainable growth of an employer"[1]. We have long argued for TPR to utilise the full flexibilities available to it in the regulation of DB schemes and believe that the consideration of the long term growth of the employer is crucial to establishing viable, long-term funding plans for DB schemes and to maximise the chances of delivering member benefits.

We welcome the opportunity to formally respond to TPR's consultation on the new Regulatory Strategy, Code of Practice and Funding Policy for DB pensions, incorporating this new objective. NAPF is working to ensure that the new objective, Regulatory Strategy, Code of Practice and Funding Policy promote sustainable DB pension schemes.

The new TPR objective

NAPF welcomes the introduction of a new objective for TPR. In our report 'DB Funding – a call for action'[2] we proposed that TPR's objectives should be reviewed and amended to more fully take into account consideration of the long term economic prospects of employers and the sustainability of the pension scheme.

This request followed feedback from NAPF members that TPR was placing a very heavy emphasis on affordability at the expense of other considerations, and the suggestion that the full flexibilities in legislation should only be used where the employer cannot afford to increase its deficit recovery contributions into the pension scheme. This placed an onus on trustees to pursue higher contributions into the scheme where the employer was judged to have the resources, placing added pressure on the employer and potentially the ongoing affordability of the pension scheme.

This pressure was exacerbated by the asset purchase programme undertaken by the Bank of England, which increased the price of gilts and, by depressing interest rates, reduced the return on pension scheme investments. To secure the same investment return, employers therefore had to put more money into their DB pension schemes, making the provision of pensions more expensive.

[1] As it relates to part 3 of the statutory funding regime detailed under Part 3 of the Pensions Act 2004.
[2] DB Funding – a call for action, NAPF, October 2012

In October 2012 Michael O'Higgins, Chairman of TPR, advised against trustees being 'recklessly prudent' in their approach to scheme funding and acknowledged that there would be occasions on which "the right thing to do for the employer and the scheme will be to invest in the sponsoring company rather than requiring them to make higher pension contributions". [3]

There is a changing emphasis from TPR in the consultation documents, recognising the importance of the employer's long term support of the scheme. This is a welcome change but trustees will have to make a relatively subjective judgement on how to balance the need for the employer to invest in the business against the 'reasonable affordability' of contributions to ensure appropriate scheme funding. The Code still requires them 'to aim for any shortfall to be eliminated as quickly as the employer can reasonably afford'. The Code only provides detail of 'some relevant factors' that should be considered when determining reasonable affordability. So, whether the new objective is effective will be determined largely by whether trustees still perceive there is any pressure from TPR to minimise risk in the portfolio, and chase the maximum possible contributions, in spite of the change in emphasis in the Code. Its success will rely on the consistent and accurate implementation of the Code by TPR caseworkers in their discussions with schemes and sponsors.

There are also issues to be resolved around what 'sustainable growth' means to different types of sponsoring employer and it will be important for TPR to work closely with trustees to ascertain what employer growth means for them specifically. For instance, in multi-employer schemes, different employers may have very different growth objectives and there is no detail in the Code as to how trustees should calculate a 'combined' employer growth objective. Some large multi-employer schemes may have in excess of 100 employers so this is a significant challenge. Other sponsors, such as those in the not-for-profit sector, may have no aim of financial growth but be looking to maintain a steady income in the longer term. This may involve investing in 'soft' areas such as branding and reputational promotions. This is in no way a literal interpretation of growth but may well be in the best interest of scheme members in the long term. It is therefore important for TPR to follow through on its promise to apply a broad interpretation of what growth means to the employer depending on scheme specific circumstances.

Further details of our view on the new objective are provided in our response to questions 1 and 2.

TPRs approach to regulating scheme risk

In a survey of NAPF members in 2013, 47% of schemes[4] responding reported that they felt under pressure from TPR to take a more cautious approach to their scheme funding valuation than they otherwise would.

Feedback we have gathered from trustees, actuaries, consultants and sponsors involved in the triennial scheme valuation process suggested that they all understood TPR's position was to eliminate as much risk as possible from schemes.

[3] Michael O'Higgins speech to Professional Pension Show, October 2012
[4] NAPF response to the DWP Call for Evidence - Pensions and Growth. March 2013

Consequently, this meant that in spite of theoretical flexibility within the legislative framework schemes were tending to follow a 'path of least resistance' to avoid TPR scrutiny and ensure that they were as close to risk free as possible.

The tone of the proposed Code is much improved. However, it remains to be seen whether the shift in emphasis, and the focus in the principles of the Code on managing rather than eliminating risk, is substantial enough to really change market practice. This will depend in large part on whether trustees perceive that the approach of TPR has actually changed and they now feel better able to make appropriate use of the flexibilities in the regulatory framework based on their scheme specific circumstances.

If the perception among trustees does not change, the pressure on scheme sponsors is likely to remain. This is a concern where sponsors could otherwise be channelling investment elsewhere to the longer term benefit of employees, scheme members and the wider economy. It could mean that the unintended adverse impact of the Bank of England's asset purchase programme, diverting cash away from investment and jobs and locking it away the pension schemes, is preserved.

We therefore urge TPR to follow through on its undertaking to ensure that scheme risk is managed rather than eliminated and that they ensure this intention is clearly understood by trustees, actuaries, consultants and sponsors alike.

The practical considerations for trustees

In general, and in theory, the Code contains adequate flexibility for trustees to efficiently manage their schemes. The emphasis throughout the Code on the collaborative approach that should be taken with employers and the change in emphasis from minimising risk to managing risk is welcome[5]. However, the Code may cause practical difficulties for the trustees of some schemes. For example it may lead to increased administration costs in some schemes, particularly smaller schemes who are unlikely to have in-house expertise and more likely to have to turn to external advisers to facilitate the transition to the new approach and to assist them with ongoing monitoring.

There are also a number of matters on which the Code is perhaps overly prescriptive:

- The practical difficulties some schemes (particularly smaller schemes) might have employing the risk management tools TPR recommends in the implementation of integrated funding solutions; and

- Onerous demands on schemes in the area of contingency planning where recognition is needed that trustees cannot always foresee, and plan for, every eventuality, nor will employers sign up to a range of contingency plans which may no longer be appropriate if a particular contingency arises.

[5] Subject to our later comments about some ambiguity in the wording with regard to risk taking.

The Code does not provide practical guidance to all types of schemes. The primary example being non-associated multi-employer schemes, many of whom will find it practically impossible to comply with the Code. We understand from TPR that they recognise there are number of anomalous scheme types for whom the Code will pose practical difficulties, and they intend to communicate individually with each of these schemes to discuss how best to interpret it in their scheme specific circumstances. However, there is no mention of this in any of the consultation documents. It would be helpful for TPR to officially acknowledge this anomaly so that scheme trustees and sponsors do not embark on unnecessary bureaucracy, trying to fit into a Code that does not work for them.

Further details of our view on the Code of practice are provided in our response to questions 3-6.

Getting the message across

Trustees are facing increasing challenges. The DB pension landscape is becoming more complex, with changes to the state pension system, difficult economic and investment conditions and increasing focus on the quality of scheme governance.

It is important that trustees are not overloaded with unnecessary information and the Regulatory Strategy, Code of Practice and Funding Policy run to over 130 pages. It is very likely that the important messages could be lost in this volume of text and it is possible that many trustees will just not have the time to fully absorb the entire content.

We would therefore urge TPR to ensure the documentation is as concise and clear as possible. In particular we recommend the documents contain a summary of the key messages and best practice principles to help trustees prioritise their time. This will help ensure that trustees take on board the essence of the new funding regime and vital points are not inadvertently overlooked.

TPR is consulting separately on 'Regulating public service pension schemes'. For the avoidance of doubt we recommend that TPR makes it clear that the new Regulatory Strategy, Code of Practice and Funding Policy will only apply to **private sector** schemes.

Further details are provided in our response to questions 5 and 18.

Conclusion

There is a real opportunity in the introduction of the new Regulatory Strategy, Code of Practice and Funding Policy to improve the working relationship between trustees and the employer, and enable them to collaborate to establish long term, viable, funding plans and improve the outcome of scheme members.

There is also an opportunity for TPR to improve its relationship with schemes and to shed the reputation it has acquired among some that it is intent on eliminating all risk within schemes. This has left those schemes feeling pressurised to de-risk to the maximum affordable to the employer and consequently caused frustration among trustees and sponsors alike.

However, the success of the new approach will depend upon TPR allowing trustees and employers to truly reach a collaborative agreement without placing any undue pressure on them or behaving in way that could lead schemes to believe there are prescribed 'targets' they need to meet to avoid Regulator intervention. Perhaps as importantly, TPR caseworkers must apply the Regulatory Strategy, Code and Funding Policy consistently and fairly across all schemes, which has not always been the experience of schemes in the past.

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Annex A: Consultation questions

In response to the specific questions in the consultation

NEW OBJECTIVE

Question 1: Is our new objective on sustainable growth adequately reflected in the approach outlined in the draft consultation documents? If not, what more could we do to reflect the new objective?

Subject to our concerns about the definition of growth in the new objective to different employers, the new objective is broadly adequately reflected in the consultation documents.

The emphasis on the importance of the employer's ability to provide long term support to the scheme is welcomed. However, there is still a strong emphasis on securing the maximum contributions that are 'reasonably affordable' but the interpretation of reasonable affordability is a relatively subjective measure, with the Code only suggesting a handful of factors that should be taken into account.

How trustees and TPR interpret 'reasonable affordability' and balance the need for an appropriately funded scheme against the need for employer growth in practice will be the true test of whether the reflection in the documents is sufficient.

The success of the new objective will depend on the practical and consistent implementation of the approach with schemes, their sponsors and TPR caseworkers.

Question 2: Is our interpretation of sustainable growth appropriate? (Paragraphs 4-9 of the funding policy)

The definition of sustainable growth will be different for different types of employer. This might be because of employer size or the sector in which the employer operates. For example the definition of growth for a not-for-profit entity will be very different to that of an employer that is part of a large multi-national group.

This is acknowledged to some extent in the paragraph 9 of the Funding Policy which states TPR will 'interpret our statutory objective on sustainable growth broadly to reflect this diverse range of circumstances.'

It will be important for TPR to work closely with trustees to understand what growth means to their sponsoring employer. For example a charity may wish to invest in ways that support their reputation, thus increasing the probability the charity will receive a continued flow of contributions and consequently the long term viability of the sponsor and the pension scheme. This is not an obvious, and certainly not a literal, interpretation of growth but it is likely to be in the long-term interest of scheme members.

Other employers may be restricted in their ability to make payments to their pension scheme by the requirements of other regulatory bodies. These employers may require particular flexibilities, such as a longer recovery period.

There is currently no mention in the consultation documentation of how non-associated multi-employer schemes should approach the matter of employer growth. These schemes can have hundreds of sponsoring employers, each of which will have a slightly different idea of what growth means to them. It would be helpful if TPR could be more explicit about how non-associated multi-employer schemes should balance the requirements of their multiple employers, for example whether they should focus their negotiations on the largest participating employers in the scheme. They should also acknowledge that the Code does not address the needs of non-associated multi-employer schemes and that they realise they will need to confer with these schemes on an individual basis to determine whether or not they meet the criteria for intervention.

CODE OF PRACTICE

Question 3. Does the practical guidance set out in the revised funding code reflect your experience of what good practice looks like? If not, why not?

In general the Code is a measured and common sense reflection of good practice in the DB pensions sector. The principles of working collaboratively, managing (but not eliminating) risk, proportionality, balance, fair treatment and good governance are all core facets of high quality pension schemes. The Code is not prescriptive and rightly allows significant flexibility to trustees - in theory.

Question 4: Is the approach to risk management set out in the code useful? If not, why not?

The integrated approach to risk management is welcome. The recognition that trustees should balance the risks which they consider to be appropriate for the scheme given employer circumstances, within flexible parameters, is encouraging.

The perception of schemes until now has been that TPR has wanted trustees to ensure that schemes are as close to risk free as possible. Consequently, they have not felt able to make use of the flexibility in the existing system. In a survey of NAPF members, 47 % of schemes[6] responding reported that they felt under pressure from TPR to take a more cautious approach to their scheme funding valuation than they otherwise would.

The tone of the proposed code is much improved but it remains to be seen whether the shift in emphasis is substantial enough to really change market practice. If it is not, the pressure on employers will remain. This could still be potentially damaging to UK growth and may mean that members do not get the best outcome from the scheme in the long term.

On a more specific note, the Code states that trustees must 'give good reasons if they do not take their actuaries' advice'. Almost all trustees will follow the recommendations of their actuary. It is therefore vital that the message that schemes are expected to manage, rather than minimise risks is

[6] **NAPF response to the DWP Call for Evidence - Pensions and Growth. March 2013**

also embedded in the action and advice of actuaries and scheme advisers. It will therefore be important to ensure that the Code feeds through via consistent implementation among caseworkers in their practical dealings with schemes. This theme of embedding consistency recurs throughout our consultation response.

There are some very detailed references in the Code to the tools trustees should make use of to understand risk. We will return to this matter when we come to consider potential costs but in practice it may not be feasible for all schemes, particularly smaller schemes, to undertake the detailed qualitative and quantitative stress testing recommended in the Code (para 50) without outsourcing that analysis to advisers at increased cost to the scheme or sponsor. We support the approach but TPR may have to offer some flexibility to the extent to which it is practicable for schemes to follow these elements of the Code.

On a similar note, the expectations on trustees with regard to contingency planning are also somewhat unrealistic. In practice it is not always possible for trustees to negotiate contingencies with employers to mitigate all potential scenarios. Schemes may experience a negative impact from factors that are unforeseen and are outside of trustee control, for example external market factors. Sponsors may also be unwilling to sign up in advance to contingency arrangements that may not even be appropriate at a future date.

It would be helpful if the Code contained some recognition that the ability of trustees to adopt contingency planning arrangements is limited and that there may well be factors and influences outside of their control for which mitigating steps cannot be planned in advance. The important message is that trustees need to have the skills and processes in place to respond to changing circumstances, not be able to pre-empt and pre-plan for every eventuality.

Question 5: does the revised code provide practical guidance for trustees in relation to:

- **a. Working with employers and advisers?**
- **b. Assessing and monitoring the employer covenant?**
- **c. Assessing reasonable affordability, including understanding the impact on sustainable growth?**
- **d. Their investment strategy?**
- **e. Technical provisions and recovery plans?**
- **f. Any other issue not mentioned above?**

If not, what further guidance would you find useful?

The Code provides a sensible framework within which trustees can operate. The presentation of the Code is problematic. It is an extremely lengthy document, running to 73 pages. This is particularly onerous as it needs to be read in conjunction with the Regulatory Strategy (a further 13 pages) and the Defined Benefit Funding Policy (a further 49 pages). It will be a challenge for any trustee to fully absorb and understand the content of each of these documents. It seems very likely that many trustees will not have the capacity to do so. In an ideal world the Code and Funding Policy would be far more concise. In the event this is not possible for legal or other reasons, we would urge TPR, at a minimum, to draw out the key points for trustees to understand in each section in a summary of key messages.

The emphasis throughout the Code on the importance of collaboration between the employer and the trustees is helpful. However, the Code does not provide practical guidance to all types of schemes. For example it is completely silent on non-associated multi-employer schemes. Indeed, trustees of all types of scheme might find it helpful to have some practical case studies and examples, particularly in the short term as the Code beds in.

Some paragraphs within the Code appear to be aimed directly at the employer rather than the trustee (eg para 27). TPR states the Code is aimed primarily at trustees but employers will 'find it of interest'. Whilst most employers will wish to work collaboratively with the scheme it seems unlikely that awareness of the Code will be a priority for most. It may be of benefit to have a reference in the Code as to why it is in the interests of employers to work collaboratively and what trustees might do in the event their employer chooses not to engage in a collaborative manner.

In addressing employer covenant the Code is lacking in practical guidance for some types of scheme. In particular, the Code is once again problematic for non-associated multi-employer schemes. These schemes may have a mix of employers with strong and weak employer covenants. TPR has acknowledged this is an anomaly and we understand it is TPR's intention to liaise with non-associated multi-employer schemes individually to discuss their scheme specific circumstances. An acknowledgement of this within the Code would be helpful and give some comfort to multi-employer schemes that are simply unable to comply with the Code in relation to all of their participating employers.

There are several references in the Code to trustees not taking 'unneccesary' risks. This may be interpreted by some trustees as TPR expecting trustees to minimise risk. Whilst trustees may feel that taking some risk in the scheme is proportionate and in the best interest of members, that risk may not be absolutely necessary, particularly if the employer has a very strong covenant.

This language appears to be somewhat at odds with the over-arching message of the code to take a balanced and proportionate approach and to manage, not eliminate, scheme risk. As the perception in the past has been that TPR does want to see trustees minimise scheme risk we urge TPR to ensure that their message about trustees' approach to risk taking is consistent throughout the documentation.

Question 6: What, if any, significant additional administrative cost does the revised code impose on schemes and employers?

The impact of the Code on the cost of schemes' administration is likely to vary significantly depending on the type of scheme. Some schemes, eg. large schemes are likely to have the in-house expertise to be able to adapt to an integrated risk management approach with little impact. However, schemes without that expertise, likely to be predominantly the smaller schemes, may incur significant additional cost as they will need additional assistance from external advisers to facilitate their transition to the new approach and, most likely, with ongoing monitoring of risk.

REGULATORY STRATEGY

Question 7: Does our strategy, focused on 'protecting accrued rights to benefits through adequately funded and supported and well governed DB schemes', with risks identified and mitigated in a proportionate and balanced way, reflect the proper balance of all our objectives? (paragraphs 5-13)

The balance of the objectives appears to be appropriately reflected in the Regulatory Strategy subject to our comments about how the balance between employer investment and 'reasonable affordability' is interpreted by schemes and advisers. It is the consistent implementation of the strategy about which we have greatest concern.

Question 8. Where risk has already crystallised, should our focus be on managing the impact of that risk to achieve the fairest and best possible outcomes in the circumstances? (Paragraph 13)

The Code includes a definition of Fair Treatment as "Trustees should seek to ensure that the scheme is treated fairly among competing demand on the employer in a manner consistent with its equivalent creditor status.

In the context of the managing risk in a situation where the risk has crystallised and it is likely the scheme will enter the PPF it would seem appropriate for TPR to clarify that it will want to achieve the fairest and best possible outcome for the *scheme and member benefits.*

FUNDING POLICY

Question 9. Do you agree with our priorities for the regulation of DB scheme funding? (Paragraph 14)

The priorities for regulation seem reasonable. The key will be how these are implemented in practice.

Question 10. Is our risk assessment approach, focusing on key areas of covenant, funding, investment and governance risks, useful? If not, what other areas of risk should we focus on? (paragraphs 21-30)

The focus of risks is reasonable. Again we would stress the need for TPR to follow through on its approach to managing rather than minimising risk. For example the language 'Tending to weak covenant means that risk-taking should be appropriately limited' (P28) could lead trustees to interpret this as meaning risk in their scheme should be minimised. Trustees need to feel empowered to decide what they feel to be 'appropriate' for their own scheme when balanced with the ongoing impact on the employer. TPR will need to work with them to understand the reasons for their decision.

We have certain concerns about TPR's ability to assess these risks accurately which we expand upon below.

Question 11: Is our approach to segmenting the landscape by covenant in order to tailor our policy and operational approach appropriate? If not, what would be a useful way of segmenting the landscape?

The approach to segmentation is a pragmatic way for TPR to prioritise the limited resources available to it. However, we have concerns about the practical implication of using TPR's estimate of employer covenant as outlined in our response to questions 12 and 13.

Question 12: Is our proposed policy focus for the different covenant strengths appropriate? If not, why not? (Paragraphs 34-37 and Appendix A)

The split by employer covenant is a relatively blunt instrument. TPR's ability to accurately assess the covenant of each employer is limited in comparison with the ability of the trustees to accurately assess the covenant of their own sponsoring employer. We understand in practice that limitations on capabilities mean only a short time is spent estimating the covenant of each employer. TPR will also experience the same difficulties in relation to the segmentation of non-associated multi-employer schemes as trustees will do.

TPR must be very clear that this is a tool being used to prioritise resources and may not accurately reflect the true level of an individual (or multiple) employer covenant. It is very likely that some schemes may try to estimate the segment into which they will be placed by TPR and thus make an assessment of whether or not they are likely to come under TPR's 'intervention radar'. This may not matter if TPR's method of assessing covenant is sufficiently accurate, but if it is not it could lead to a reputational risk to TPR if resources are inaccurately allocated and schemes unexpectedly fail. TPR needs to keep the accuracy of its employer covenant assessment process under review and make improvement to it where practicable.

Question 13: We used a broad suite of risk indicators to assess scheme risks in the round. Is this the right approach? If not, why not? (Paragraphs 38-43 and 48-49, Appendix C and D)

In principle the move away from individual triggers to a broad suite of risk indicators assessing schemes in the round is to be welcomed. However, we have a number of concerns about the use of the Balanced Funding Outcome Indicator (BFO) as outlined below.

Question 14: Do you think that our proposed Balanced Funding Outcome Indicator is useful to:

a. **Measure risk in the system?**

b. **Inform our approach to prioritising schemes for further investigation?**

c. **Inform our approach to measuring our impact?**

(Paragraphs 38-43 and Annex C)

Whilst the Funding Policy states that the balanced funding outcome indicator "does not set a minimum level of funding or contributions" it is clear from the policy that the BFO is a primary factor on which TPR sets its risk bar for intervention. There is a risk that, despite this warning, the BFO is seen as a minimum 'target' schemes will need to meet to avoid TPR intervention.

It is natural that schemes and trustees will want to avoid the scrutiny of TPR and will try to ensure that their BFO indicator score lies within the safe area. As with the covenant assessment this may not matter if TPR's assessment of the schemes risk is accurate but the BFO is heavily reliant on TPR's assessment of the employer covenant, which is inaccurate in itself.

Trustees need to be empowered to make the decisions and assumptions appropriate to their scheme and feel confident that they can explain any apparent resulting adverse impact on the BFO indicator. However, in practice only a minority of trustees are likely to feel confident enough to do that.

Many may see the BFO as a target and focus on ensuring their scheme is comfortably in the 'safe' zone above it. This may not ultimately mean trustees are making the best decisions for members. Moreover, there is a risk that the trustees of schemes with balanced funding outcome indicator levels significantly above the level that would attract scrutiny by TPR may be put under pressure by their sponsoring employer to reduce demands on the employer.

There is no easy solution to this problem. We appreciate that TPR must prioritise its resources and we welcome the level of transparency being demonstrated. However, it could be made clearer that this is a measure TPR is making use of to inform its understanding of the entire universe of schemes and is just one of the measures taken into consideration to determine the schemes that might require intervention. It should be made even clearer in the Funding Policy that it is not a target and trustees should feel empowered to make the decisions they feel are appropriate for their scheme and that, provided they have valid reasons for doing so, this approach will be acceptable to TPR.

15. Our policy for targeting our resources where we can have the greatest impact takes account of the level of risk, including scheme size. A greater proportion of our interventions will, therefore, be in larger schemes, with smaller schemes generally being regulated through education and other targeted approaches such as portfolio reviews.

a. **Is it right that our risk bar for intervention takes account of the level of risk posed by schemes and their size?**

   In terms of prioritising TPR resource it seems reasonable to focus on the regulation of larger schemes, which will benefit the greatest number of members. However, there is a reputational risk to TPR in the event that a significant number of small schemes, or even one high profile scheme, slips through the regulatory net. TPR needs to be extremely careful not to give the impression that members of smaller schemes are less important that those of their larger counterparts. TPR's statutory objective is to protect the benefits of members of occupational pension schemes, not just to protect those members of the largest schemes.

b. **Is education the most effective and proportionate way of regulating across a diverse landscape? (Paragraphs 52-53)**

Paragraphs 52-53 relate specifically to small schemes. Education is certainly helpful for small schemes, but education is a tool for enabling trustees to perform their role to a high standard and to empower them to have meaningful dialogue with the employer to the benefit of the scheme. While it may reduce the likelihood of TPR needing to intervene, education should not be considered a regulatory tool. It is a form of support.

16. Is proactive engagement an effective way of engaging with schemes and targeting our resources in order to achieve balanced outcomes? (Paragraphs 58-60)

Proactive engagement can be helpful in some circumstances, but is also an additional burden on scheme resources. Proactive engagement should be used where it can have a net benefit by reducing the likelihood of TPR needing to intervene in the scheme at a later date. For example, where a scheme's employer covenant assessment varies significantly to that calculated by TPR because the trustees have access to information not available to TPR. It is also helpful for schemes whose circumstances are unique and do not fit into the Code of Practice, such as the non-associated multi-employer schemes already discussed as an anomaly.

17. Is our proposed approach to measuring the impact of our regulatory approach appropriate? If not, do you have any suggestions? We are particularly interested in your views on how we should be measuring success against our new objective on sustainable growth. (Paragraphs 82-85)

The use of surveys to assess the understanding of, and the perception of the effectiveness of TPR's implementation of, the new objective will be key. Engagement with stakeholders will also be essential. NAPF will be regularly engaging with members to assess their opinion of how the new objective is working in practice and how consistent the implementation is and we will feed our findings back to TPR. We will also be glad to facilitate meetings with NAPF members for TPR to get direct feedback.

There should also be some form of external monitoring of TPR's performance, for example by an industry-wide steering group, and TPR should report on its compliance with the objective in its Annual Report.

Any additional comments

18. Are the documents structured and drafted in a way that makes it easy for you to understand the key messages and issues? How could they be improved?

We reiterate the comment about the length and number of documents it is necessary for trustees to read. This is likely to make the documents relatively inaccessible to the average trustee. It also means that it is very easy for a reader to overlook the essential messages that trustees need to understand. This is particularly true for new trustees, or trustees that are still not completely confident in their level of knowledge.

In the extreme it is possible that a proliferation of lengthy documentation could deter potential trustees from even applying for the role.

We recommend that the length of the Code and Funding Policy are kept to a minimum and, in the very least, a summary of the key messages for trustees to take away is included at the beginning of each document.

19. Are there any other comments which you would like to make on the proposals contained in these consultation documents?

We have no further comments on the proposals.