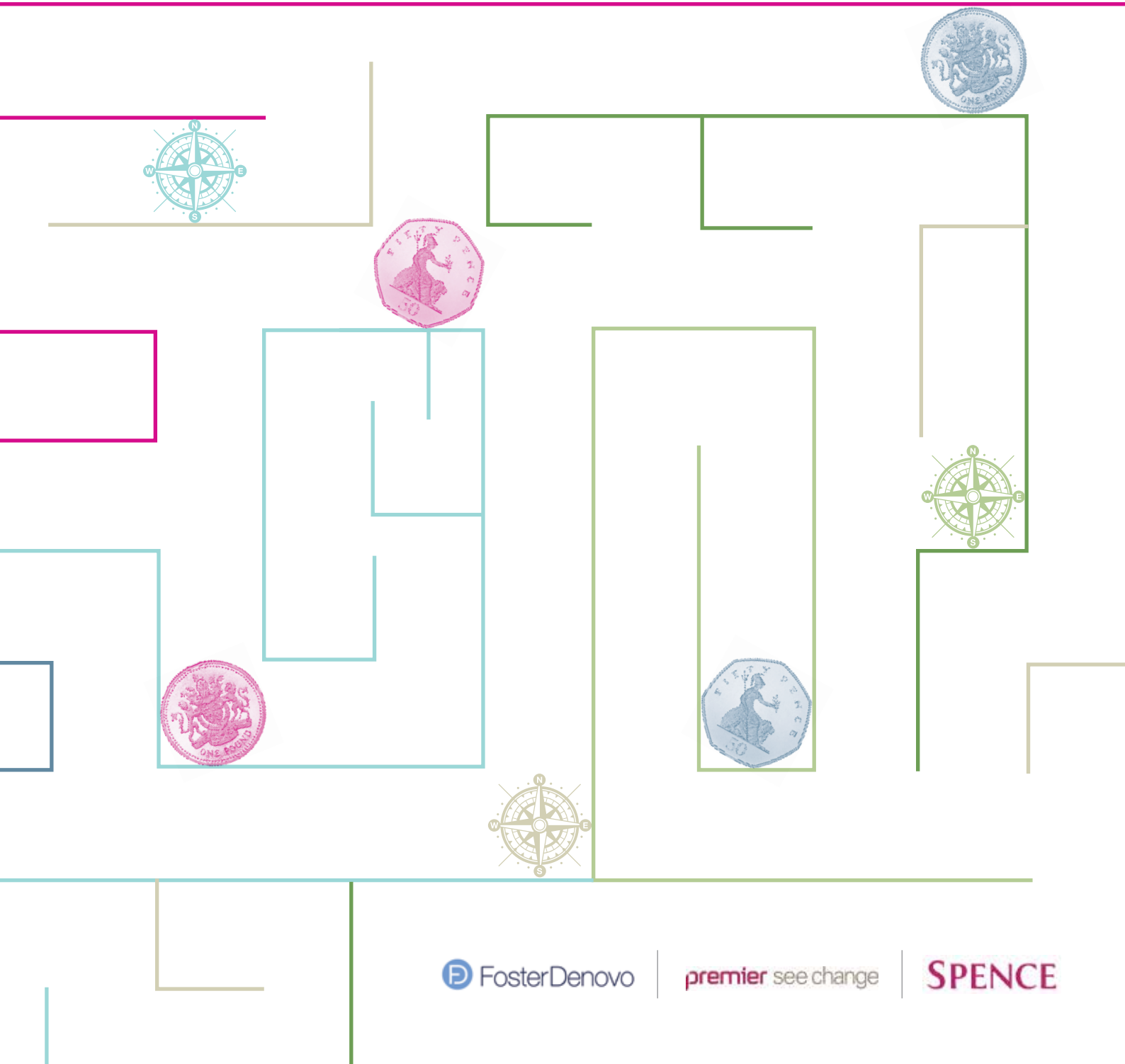




INSPIRING
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Navigating the Charity Pension Maze

2014





CFG

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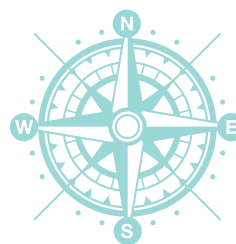
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Foreword



Charity Finance Group's vision is to inspire the development of a financially confident, dynamic and trustworthy charity sector.

CFG works with finance managers to enable them to give the essential leadership on finance strategy and management that their charities need; promoting best practice in charity finance, driving up standards, campaigning for a better operating environment and ensuring every pound given to charity works harder. CFG has more than 2,200 members, and collectively our members are responsible for the management of over £19bn in charitable funds.



Charities play a crucial role in bringing about social change; on a local, national or international level. Their actions and activities are the life blood of many communities, helping to give voice to the vulnerable, support to the disenfranchised and relief to needy. It is however sometimes overlooked that charities also play a huge part in society as employers in their own right.

It's critical that charities are able to attract and retain the right skills in their workforce. An important part of this is understanding the pension environment to ensure that beneficiary and donor support is maintained and equitable and fair support is given to charity staff.

The last pensions maze report was published six years ago in 2008 when the world was a very different place. Since then the economy has suffered the deepest and longest recession since the depression and we've experienced historically low interest rates and falling wages. These circumstances have presented a major challenge to charities.

The pensions landscape itself has also transformed. Back in 2008 auto-enrolment was the planned position, now we are starting to see the regime embedded across the country's employers. This year's budget and Queen's speech announced perhaps the most profound changes to pension provision ever.

Getting pensions right for charities is crucial. CFG is committed to see charities taking their place at the heart of civil society as effective and responsible employers.

The provision of this comprehensive report, which aids charities in their navigation of a number of complex issues and exposes some real challenges for the sector, I am sure, will be welcomed by our members and I would like to thank the charities, corporate partners, experts and CFG staff team for making it happen.

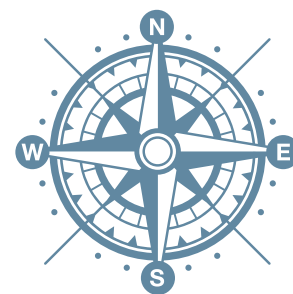
Ian Theodoreson,
Chair CFG



Charity Finance Group's 2014 Pension Maze provides a comprehensive tool to help charities navigate some of the most significant reforms to the private pensions landscape in decades, and I recommend it to all charities.

While we recognise there are pressures on charities and we are looking to help them we need to do this without undermining member protection.

Steve Webb MP,
Minister of State for Pensions



The map – how to find your way around the pension maze

Defined Benefit Schemes

Type of scheme	Managing your legacy	Ensuring good governance	
Own DB	Your scheme may be in deficit, you'll need to negotiate a recovery plan with your pension trustees. Key issues are your covenant and the assumptions used for the valuation. (Section 4.4-4.7)	The charity and its pension scheme are reliant on each other's success. Key to ensuring they both achieve their objectives is the creation of strong relationships, with proactive conflict management. (Section 3.1-3.5)	
	Are you considering a range of options for managing future DB risk? Options such as alternative asset investment strategies, delegated investment and pro-active management of the 'flight path' have different advantages. (Section 4.9)		
	Your scheme pays a levy to the Pension Protection Fund (PPF). How this is calculated is being re-assessed and may alter your annual fee. (Section 4.11)		
	The Budget 2014 and the Queen's Speech 2014 unveiled a series of changes to DC provision. The flexibility of this new approach may have a knock on effect for DB schemes. (Section 4.10)		
Multi-employer	Do you think you may be involved in a multi-employer scheme? Double check! Many charities are not aware of all of the risks involved with these schemes. (Section 5.1)	Multi-employer schemes are challenging for individual charities as there are generally a large number in each. Get involved as much as you can with the employer working group for your scheme to improve scheme governance. (Section 5.6)	
	The Pension Trust's various 'Growth Plan' arrangements cover many charities and have specific challenges. (Section 5.5)		

Defined Contribution

Charity specific	How will your current DC scheme work with auto-enrolment? If you want to use it for auto-enrolment, is it compliant? How will you plan ahead for maximum affordability of scheme provision? (Section 6.5)	Ensuring the design of your scheme is the best for your charity, including whether to set your own trust based scheme or use a contracted scheme (Section 6.2)	
		If your DC/Auto-enrolment provision does not have a Board of Trustees you will need to consider setting up a committee to oversee employee pension provision made up of key stakeholders, to ensure good governance of the pension scheme arrangements. (Section 6.7)	
Auto-enrolment			



Meeting current challenges	Stakeholder engagement
<p>You may consider closing your DB scheme to future accrual in order to manage future risks posed by increasing liabilities. Managing the process and messaging to staff is key to success. (Section 4.8)</p>	<p>Public interest in DB scheme deficits is becoming more intense; charities coming under increasing pressure to explain how their income is spent. Reporting your pension liabilities is key to managing stakeholder's understanding. (Section 9)</p>
<p>Are you considering a merger with another charity, a significant contract acquisition or strategic realignment? Any of these changes can have implications for your covenant. Working with your pension trustees and keeping them informed is crucial to long-term success. (Section 8)</p>	
<p>Pricing of work is always tricky and you will need to ensure that your charity not only achieves full cost recovery for the direct costs but also ensures sufficient income to cope with any volatility of costs that are required to fund the pension deficit. (Section 2)</p>	
<p>You may be considering a merger with another charity. If either of you have pension schemes the implications will need careful consideration. A restructure of this nature may trigger an unaffordable section 75 cessation debt. (Section 5.2-5.3)</p>	<p>The introduction of FRS102 to the charities SORP will mean that many charities will need to record a liability on their balance sheets for future payments to a multi-employer scheme. Beware of the impact this will have on your reported net asset position and carefully manage expectations in your annual report. (Section 9)</p>
<p>Are you considering tendering for contracts from the public sector? Beware the pitfalls of not pro-actively managing TUPE obligations. Take advice on any pension obligations you may have to undertake. (Local Government Pension Schemes pose particular challenges) (Section 3.7 and 8.3)</p>	<p>If you have any loans or overdrafts, now is the time to check the small print of those agreements when implementing FRS102. (Section 9)</p>
<p>How does your DC provision support your people strategy? Does it have the best structure? Are your communications with your employees transparent and consultative where necessary? (Section 6.64)</p>	
<p>The Budget 2014 and the Queen's speech 2014 unveiled a series of changes to DC provision. As an employer you need to be aware what new DC options are available to you, and how your employees will be impacted by these changes on retirement. (Section 6.8)</p>	<p>If your DC scheme is 'contract based' i.e. governed by a contract between the member and a provider, have you established a Governance Committee to ensure good value and staff engagement in line with the Pension Regulators Code of Practice? (Section 6.7)</p>
<p>Auto-enrolment shifts the onus of pension provision squarely upon the employer for the first time. You need to know when your staging date is and what steps need to be taken to get there. Do you have the systems in place to manage the rapid transition to auto-enrolment? (Section 7.3)</p>	
<p>There are a multitude of DC providers available to choose from, including trust based, contract based and master trusts. Your current provider may not be able to provide you qualifying auto-enrolment provision at good value; a number of new options have entered the market. (Section 7.3)</p>	<p>For many charities, auto-enrolment will mean they are paying contributions to pension provision for the first time. Are the implications of the additional costs understood by trustees and factored into full cost recovery calculation? (Section 7.1, 7.4 & 7.5)</p>

Section 1

The Maze: Changes and trends 2008-2014



1.1 Introduction

Pensions pose challenges for many employers, and charities are no different. The current auto-enrolment requirements and growing Defined Benefit (DB) schemes liabilities mean that pensions are rarely off a finance professional's agenda. Knowing how to navigate the pension landscape has become a crucial skill. It's not just the sector that is concerned; the Pensions Minister Steve Webb MP said at CFG's 2013 Annual Conference that charity pension issues were beginning to keep him awake at night too.

CFG has long been central in the sector's pension deliberations. The CFG Pension Maze series has mapped the pension's landscape for charities since 2003. The world in 2008, when Pensions Maze (2nd Edition) was published was a very different place. The Bank of England was forecasting¹ a recession but saw a return to growth no later than the end of 2010. Inflation was thought to have reached its peak at 5% and was expected to fall to the long term target of around 2%. Whilst their predictions were largely accurate, the economy fell back into recession as the impact of the Eurozone crisis became apparent in 2011/12.

The economy has presented major challenges for beneficiaries, charities and charity pension funds. CFG's annual report *'Managing in a Downturn'* launched in 2008 has tracked the impact of the changing economy. The latest in the series, *'Managing in the New Normal'*, documents charities facing continuing challenges.

Whilst the last few years have been tough, the timescale for DB schemes, including those which are closed to future accrual is measured in decades. There will be other economic cycles to face before all current scheme liabilities are settled.

DB schemes account for approximately £1 trillion of assets and 12.7 million members. Work-based Defined Contribution (DC) pensions add a further more than 5 million members. By 2018 it is estimated that there will be between 6 and 9

million people newly saving into pension schemes as a result of auto-enrolment. Most new savers will be in DC schemes and the Pension Regulator expects the assets to more than double (from around £400 billion) over the next 15 years².

Charities are managing not only challenging income streams but also volatility on their balance sheets. As employers, charities want to fulfil their pension promises and recognise that their staff are often lower paid than their private and public sector counterparts.

Despite this desire it is no surprise that our pension's survey highlights a continuing closure of DB schemes to new members and future accrual.

Six years on from CFG's last Pensions Maze what has changed and what shapes the current pensions landscape for charities?

1.2 Pensions reform 2012

'Workplace pensions' (or 'auto-enrolment' as it's more commonly known) with which all employers have to comply by 2018, is a flagship policy to tackle the rapid decline in pension savings. CFG published a guide in late 2013, 'Auto-enrolment for charities: a how-to guide' along with the findings of a survey of its members readiness for auto-enrolment. Overall, auto-enrolment is a huge undertaking for charities particularly those with low pension take up already where the additional cost of the scheme and administration complexity will be major challenges.

1.3 Deficits have grown and funding remains a challenge

Deficits continue to be a problem for those with DB schemes. Many charity balance sheets are under severe pressure. Many have seen their position deteriorate in recent valuations as historically low gilt yields, stagnant market returns and lengthening life expectancy have combined to drive up pension deficits.

Analysis on the top 41 charities in the UK in 2014 by Charity Finance showed that they hold almost £5.7bn in pension liabilities on their balance sheets and increase of 14% since 2012. These are backed by around £4.8bn in assets – leading to an overall deficit of £900m. In contrast, the buy-out deficit of these charities now stands at £5.2bn, up 18% in the last two years, while the unrestricted funds of these charities has reduced by 13% from 33.8bn to £3.3bn.

Based on the annual reports of 10,000 voluntary organisations, the sector is estimated to have net pension liabilities of £1.5bn. £1.2bn of this liability is concentrated in the largest 533 charities, those with an annual income of over £10m. However, smaller charities are not immune from pension liability exposure and problems. Smaller charities will often participate in multi-employer schemes which appeared to allow charities to share risk and minimise organisational administration and overheads.

In the face of these difficulties CFG welcomed proposals to put employer affordability at the heart of the Pensions Regulator's regulatory strategy. Protecting the long term affordability of deficit Recovery Plans for sponsoring employers could help ease the burden.

1.4 Multi-employer dilemmas continue

Charities with non-associated multi-employer schemes arguably face a greater predicament than DB deficits. Many are trapped in schemes with rising contributions and increasing orphan debt that they cannot afford; they cannot afford to leave either as they will 'crystallise' often enormous cessation (section 75) debts. As other employers in such schemes fail, the burden on those remaining increases. Recently examples such as the insolvency of 'People Can' and 'Spirit of Enniskillen Trust' or the failed NAVCA merger highlighted how potentially damaging these schemes can be.

For charities in the Pensions Trust's Growth Plan 3 reclassification as a DB scheme was significant; giving rise to liabilities previously not anticipated.

Sponsoring employers of multi-employer schemes have not been required to show on the balance sheet any liability for an underfunded scheme. From January 2015 the new SORP (implementing FRS102) will require charities with income over £500,000 a year (and charities with incomes over £250,000 and assets of more than £3.26 million) to account for the net present value of their agreed contributions to cover past service deficits. This is set to increase the booked unfunded liabilities of charities.

1.5 Governance has become ever more important

As employers increasingly use DC schemes, pensions governance becomes more important. Indeed DWP and the Pensions Regulator have placed greater focus on it. Ensuring pension savings are invested in well designed and appropriately governed DC schemes are important matters. It's concerning therefore that CFG's DC survey this year showed charities infrequently review their pension investment strategies. Equally concerning is that 40% of charities did not understand management charges; a key aspect of stewardship and governance. To assist with all these issues, the role of governance committees for DC schemes in particular will become essential.

Concurrently managing the legacy of DB deficits over the long-term requires pension and charity trustees to build a strong partnership approach. This requires both to develop a way of working which acknowledges respective roles and duties and effectively manages the conflicts that arise from different objectives and legislative frameworks.

1.6 Transparency, accountability and the reputation of the charity sector

During 2013 the charity sector experienced a noticeable increase of public and media scrutiny on charity expenditure. This scrutiny included interest in pension liabilities. Charities must transparently account for and strategically manage their pension provision. CFG's DB survey reports around 65% of respondents are concerned about the implications their pension provision has on stakeholder perception of their charity. These levels of concern increase for charities with high proportions of restricted income³.



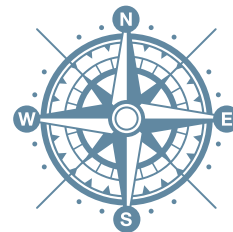
¹ Statistics from Bank of England Inflation reports: www.bankofengland.co.uk/publications/Pages/inflationreport/default.aspx

² The Pensions Regulator Corporate Plan 2014-2017: www.thepensionsregulator.gov.uk/about-us/corporate-plans.aspx#s8355

³ See CFG Pension Survey 2014

Section 2

Pension Provision and Charity Strategy



Many charities establish quality pensions to help them compete for staff as part of an overall benefit package. However, the environment charities faced at the time many schemes were originally established is very different from now. Pensions are now more expensive to provide. Multi-employer schemes charities face significant funding issues they had not anticipated. All at a time income when is uncertain. As a result, charity trustees are looking very closely at pension provision to ensure that the strategy being adopted fully reflects their charitable objectives.

Charities should start by asking some probing questions:

- Does current pension provision attract and retain staff?
- What is the take-up rate and do you understand why?
- Are employee contribution levels proving a barrier to entry for staff (e.g. specific ages or grades)?
- If you still have a DB scheme, why? (does maintaining it have a positive impact, such as reducing staff turnover)
- As part of any recruitment or leaving interview process do you ask about the effectiveness of the remuneration package offered?
- Would alternative strategies be more attractive?

The answers to these questions may result in consideration of alternatives to current pension arrangements. Be aware of the full implications of any change. Change in pension provision can be complex and emotive for the staff involved. Communicate clearly the rationale for any proposals and look to minimise any employment issues and the potential impact on productivity or quality of services.

Take legal advice regarding formal process and any statutory timescales but the following questions for those considering change might include:

- Are changes of contractual terms and conditions required?
- What period and type of consultation/ communication would be required and with whom?
- Is there a recognised trade union? Would there be any impact on scheme costs? For example closing a DB scheme to new entrants is likely to result in an increase in the employer funding rate which will increase short term contribution cost. However, will this be satisfactorily offset by reducing the risk of an ever increasing liability?

The sections on DB, DC and Auto-enrolment, will pick up specific employer related issues.



Section 3

Trustee Relationship Management and Advisor Selection

CFG's DB survey exhibited low levels of trust and confidence in the governance of DB schemes amongst respondents. This supports the need for proactive strengthening of governance processes as outlined below⁴.

3.1 Introduction: Recognising the human element

Don't forget that pension schemes and charities are run by people. Given this human element, effective working is less about rules and regulations and more about how the individuals concerned interact. Getting this right is fundamental.

In 2007 in 'the governance of work-based pension schemes', the Pensions Regulator quote the National Council for Voluntary Organisations (NCVO) definition of governance; "the systems and processes concerned with ensuring the overall direction, effectiveness, supervision and accountability of an organisation."

One of the crucial elements of good governance is the appropriate management of conflicts of interest between an individual and the organisation. A conflict of interest may arise when a trustee is required to take a decision where:

- 1) They are obliged to act in the best interests of the scheme's beneficiaries and;
- 2) Concurrently they have, or may have:
 - a) a separate personal interest, or
 - b) another fiduciary duty to a different beneficiary⁵.

Conflicts of interest arise in particular if a senior officer, or a trustee of the sponsoring charity, is also a member of the pension scheme's board of trustees. Benefits from this set up can include an increased understanding and better communication between the charity and the pension scheme. But it is difficult for an individual to negotiate with themselves and hold themselves accountable, without bias. Charity and pension trustees should agree a protocol for managing situations where conflicts or perceived conflicts are likely to arise. Further guidance is available from the Pensions Regulator⁶.

Conflicts can also arise between advisers. It has become more common for pension trustees and charity employers to get advice from different individuals. A single advisor would find it very difficult to provide unfettered advice to both sides where the interests of the two parties differ. The Actuarial profession has now issued professional guidance which actuaries need to follow in this area⁷.

⁴ See CFG Pension Survey 2014

⁵ The Pensions Regulator's guidance on conflicts of interest: www.thepensionregulator.gov.uk/guidance/guidance-conflicts-of-interest.aspx

⁶ The Pensions Regulator has issued guidance aimed at giving practical help to pension trustees to manage these conflicts: www.thepensionsregulator.gov.uk/guidance/guidance-conflicts-of-interest.aspx The Charity Commission also provides guidance around managing conflicts of interest in general: www.charitycommission.gov.uk/trustees-staff-and-volunteers/trustee-board/conflicts-of-interest/

⁷ The Institute of Faculties and Actuaries: www.actuaries.org.uk/regulation/pages/conflicts_of_interest

Case study 1: The importance of Engagement

Melanie Cusack, Client Director at PTL, tells us about the importance of engagement from the Pension scheme Trustee perspective, using the example of supporting a top 50 charity to manage the risk of c£70m deficit.

Background

- A top-50 charity – well governed by an active trustee board.
- A pension scheme – 5 trustees (including 2 member-nominated trustees and independent chair).
- The project – introducing a contingent asset to address a c£70m pension scheme deficit.

Various options were explored by the sponsor to mitigate this deficit, including Special Purpose Vehicles, escrow accounts and contingent assets. The pension trustees were advised of this work and fully supported it. The decision to promise some of the charity's assets to the pension scheme should the charity find itself in financial distress was deemed the best fit.

Engagement with the Finance Director

The Finance Director (FD) already enjoyed a good working relationship with the pension trustees, and it was agreed that regular liaison would be with the Chair of pension trustees, with the rest of the pension trustees consulted before making decisions. The frequency and frankness of discussions between the FD and Chair increased over the course of the project but, rather than taking opposing sides, these were approached in a spirit of collaboration. This meant that despite some challenging negotiations, all parties were mindful that they were working towards a common goal for mutual benefit.

Engagement with the charity trustees

Two of the charity's trustees also served as pension trustees. Potential conflicts had been carefully managed to that point but given the significance of the project, it was agreed that

a new approach was required. Consequently, an independent Pensions Working Group with clear terms of reference was created. The individuals involved were free of conflicts, and timely decision making – always challenging given the limited availability of the charity trustees – was expedited. The pension trustees did not deal directly with the Pensions Working Group, but the individuals were well known to them, giving comfort that where decisions were challenged, this was for sound reasons. The arrangement was so successful and efficient that it was retained after the contingent asset was put in place.

Engagement with the advisors

There are many hurdles to overcome when introducing contingent assets and consequently, a vast number of advisers are involved: pension lawyers on both sides, charity lawyers, property lawyers, property evaluators and the scheme actuary. Working with so many advisers proved to be one of the biggest, and most costly challenges. The FD and Chair of Pension Trustees endeavoured to control fees by working through many issues on a one-to-one basis and then reverting to their respective advisers for comment. This resulted in a better working relationship amongst all the parties.

Post-project relationships

Relationships between the pension trustees, the FD and charity trustees are stronger. The same is not necessarily the case with all the advisers.

Lessons learned

Multilateral engagement at the start of the project appeared to be high and effective. However, in hindsight, it became clear that this was really only adequate for day-to-day, non-controversial issues. In a joint review of the project, it was concluded that all parties should have spent much more time addressing the feasibility of the project and when and how decisions would be made.

Appointing a sole corporate (professional) trustee to the pension scheme can significantly reduce the potential for conflicts of interest; this is recognised and commented on in the Regulator's advice as being something scheme sponsors may wish to consider.

Below are some practical tips for trust based schemes, in particular DB schemes.

3.2 Two bodies, divided by a common purpose

Commonly the groups which take responsibility for DB pension matters are a charity's finance committee and a pension fund trustee board.

3.21 Step 1: Generate mutual understanding

Both the pension scheme and the charity have their own individual set of outcomes that they are trying to achieve, supported by strategic and operational plans which set out how they intend to achieve them. In addition, they are identifying, monitoring and mitigating key risks.

Both organisations should establish understanding of:

- each other's responsibilities to their respective stakeholders and beneficiaries;
- the regulatory frameworks and operational environment in which they work to achieve their outcomes.

This requires significant investment of time and resource. The charity needs to ensure that their trustees and senior officers are fully engaged in this process. The involvement of advisers can be helpful, allowing them to gain the same understanding; but the process should not be advisor led.

Charities, unlike profit driven organisations, do not have a simple goal of increasing shareholder value. Charities are highly sensitive to factors which could detract from their reputation and none would willingly walk away from the pension promises made historically to their staff. Understanding the respective objectives, strategies and risks generates appreciation of the needs and the drivers of behaviour. Mutual understanding reassures the parties that the discussions are reasonable, balanced and orientated towards a constructive outcome.

3.22 Step 2: Aligning interests and building shared objectives

Shared understanding allows the parties to identify where interests are naturally aligned or which may be a source of conflict. From this the trustees should establish shared objectives and outcomes that will ensure the long-term sustainability and viability of both organisations.

The lack of a profit motive, the mix of restricted and unrestricted reserves and the role that voluntary giving plays make charities different to 'normal' businesses. This means that 'normal' pension solutions often aren't appropriate. Pension scheme finances require a long-term perspective. Broadening pension considerations beyond immediate deficit contributions to considering the role of reserves, application of charity surpluses and/or windfall gains can be helpful in finding ways to achieve mutually agreeable outcomes.

Enabling the charity to maintain a level of investments and liquidity on its balance sheet as a part of its mitigation of financial risk may be more beneficial to the pension scheme in the long-term than the immediate transfer of those assets to the scheme. A sound reserves policy will underpin the long term success and covenant of the organisation to the benefit of the scheme. The counterpoint for pension scheme trustees will be to seek undertakings that assets won't be sold down or mortgaged and that creditors who rank higher than the pension scheme won't be introduced.

Once established, these shared objectives need to be documented and set out in clear terms.

3.23 Step 3: Sustaining the relationship to deliver against shared objectives

Set out shared objectives clearly. It is important to develop processes which build on this foundation through:

- a structure for meetings between the charity and the pension scheme, which go beyond the formal requirements, and foster strong collaborative relationships; and
- a mechanism for transparent flow of essential information between the two parties, which provides ongoing insights and assurance.

It is worthwhile bearing in mind that these processes are only effective if the people conducting them have the right skills. There is more to appointing appropriate pension trustees, than ensuring technical expertise; it is possible to have too many experts. Recognising the value in and seeking a blend of skills in a group, including wider commercial skills (such as chairmanship, mediation, consensus building and stakeholder management), usually improves effectiveness. Leadership is vitally important and having a Chair that can steer the direction and bring the best out of the team is invaluable. It is of as much importance as technical knowledge.

3.3 Structure of meetings

Formal meetings are required as a part of the pension trustees and charity trustees fulfilling their respective regulatory roles. To ensure these operate in an atmosphere of trust and openness, other interactions can help. A key relationship is that between the two chairs of the boards. Private conversations between Chairs can provide a forum to share the kinds of pressures, thinking and tone of discussions which really help when a problem needs unlocking.

The day to day link between pension fund trustees and the charity is usually between charity officers or executives. Whilst these officers may have strong influence, they seldom have full decision making powers. This runs the risk that officers attending each group can be put on the spot to explain why the other side won't see reason. Widening the points of contact between the two groups invariably brings both sides closer together. Boards with individuals in common can help build bridges and take pressure off officers/executives. Issues around conflicts of interest can usually be overcome with pragmatism as discussed above.

Additional meetings, at least once or twice a year, at relevant points during the planning cycle of each organisation, to talk about how the charity and pension scheme are developing is imperative. This ensures an ongoing dialogue, so that when significant issues arise, individuals are unlikely to be surprised and discussions can therefore be constructive and non-adversarial manner.

3.4 Flow of information

Both the charity and pension scheme trustees will monitor the performance of their organisation in achieving their strategic objectives. They are likely to have developed a robust set of metrics, scorecards, forecasts and allied information to provide them with assurance that they are on track. Sharing this information under agreed protocols can facilitate dialogue and help develop trust.

3.5 Restarting relationships which aren't working effectively

Financial pressures and a regulatory environment which can promote adversarial relationships despite the best of intentions, have led some organisations to the point where the pension fund trustees and charity trustees are at loggerheads. This puts both charity and pension scheme at risk.

It is understandable that these situations arise but failing to recognise and act to resolve the situation is a failure of leadership by both parties. Reflect on the implications of the situation and take time to consider how best to move forward. It may entail a change in trustee membership or responsibilities, or a fresh advisory team.

Case study 2: Covenant Monitoring Process

Keith Hickey, Group Director Resources at the Royal National Institute for Blind People (RNIB) describes the processes they have in place for sharing and reviewing information between charity and pension trustees.

RNIB's cycle for covenant monitoring is:

- A Triennial review – this involves a detailed covenant assessment of the employer
- An Annual review – this is an update report on the employer. Discuss any concerns and changes from the last detailed review
- A Quarterly review – the employer's covenant is a standing item on the agenda so that trustees can check for any important news and watch out for any sudden deterioration in the employer's financial position.

Trustees also reserve the right to review the covenant outside of this cycle if they have urgent concerns.

The quarterly review includes:

- The most recent Management Accounts as received by SMT
- Details of any notifiable events to The Pensions Regulator if they occur
- Details of any material corporate activity e.g. changes in group structure, mergers, and new associates
- Details of any material asset sales or changes in cash flow
- Details of any new bank, or intercompany loans, or the repayment thereof if greater than £0.5m
- Details of current position on banking covenants
- Details of any new material creditor or debtor (over £0.5m)
- Details of cash flow explaining variances greater than £1m from budget

- Capital or Revenue projects entered into if greater than £1m
- Details of key KPI's – Reserves against Reserves Policy, Net Fundraising Income, Quick Ratio, Level of Investments and Cash relating to General Funds

The annual review consists of the same information as in the quarterly review along with the Annual Business Plan for the Employer.

The contents of the triennial review are agreed prior to its production and it is undertaken by the Group Director of Resources. The methodology used in the assessment is to consider the four key aspects that affect RNIB's financial capacity and make an assessment of each one; namely:

- the external environment;
- the UK charity sector and its framework;
- RNIB's business profile – group structure, performance against strategy, risk management, reserve levels, analysis of major income streams, key trends, regulation and SWOT analysis;
- RNIB's financial profile – review of last three years financials, business plan and budget, review of pension scheme financials for last three years and most recent management accounts.

This is then brought together in a conclusion and opinion on the strength of the covenant.

The Trustees also receive a copy of the RNIB Strategy when agreed by the RNIB Board of Trustees and a copy of the annual accounts when published.

There is a confidentiality agreement in place between the RNIB and the Pension Fund Trustees since a lot of this information is confidential to the Employer.

3.6 The Pensions Regulator's new code of practice on funding

In June 2014 the Pensions Regulator published a new DB code of practice and annual funding statement. At its core is a theme to balance success of the pension scheme with success of the business supporting it, by the introduction of a new statutory objective focused on minimising any adverse impact on the 'sustainable growth' of the sponsoring employer. Ideally it will bring a helpful focus on collaboration, shared risk taking and taking a long-term approach. The Pension Regulator has committed to exploring the option of a developing guidance for applying the code to charities specifically.

3.7 Local Government Pension Scheme

The Local Government Pension Scheme (LGPS), and the many funds which make it up, are undergoing significant changes, ranging from the format of benefits, restructuring of the committees which run them, to the prospect of consolidation into superfunds. This is resulting in some governance issues for charities who participate in LGPSs.

Pensions continue to be material issue for new contracts with councils. The importance of arranging tendering processes that will identify pension issues early on using the right expertise (either in house or using specialist advisers) is covered in section 8. The responsibility for defining what is acceptable in terms of risk appetite is increasingly being reserved as a matter for the trustees of the charity, rather than left as a local management decision. A charity's strategy in regard to contracting and managing the inherent risks will be one of the areas of interest for the trustees of the charity's own DB scheme. In terms of the relationship with the LGPS itself, supplying information to and getting information from LGPSs should be fairly routine. However, some LGPS administering authorities are able to provide information more easily than others. As with all business partnerships, making sure the charity knows who to contact and who in the team will take responsibility for the relationship is critical, together with developing a forward plan for the necessary exchanges of information.

3.8 Adviser Selection

Trustees should regularly review their panel of advisers to ensure best quality and value for money. A new adviser can refresh a relationship and bring in new ways of thinking around existing issues. Appointing a new adviser can lead to operational costs. Trustees should undertake an objective appraisal of the relationship prior to undertaking a formal selection process. Giving direct feedback to the current adviser may encourage fresh thinking and lead to the scheme securing much of the benefit of a change; without the cost, inconvenience and risks of starting afresh.

Trustees should prepare a clear statement of the services they require and how success will be measured. Criteria for selection might include:

-
- **Relevant expertise in the charity sector**
 - **Cost and their attitude to cost.** Advisers do need to understand the low cost base and the lack of VAT recovery that charities have to operate in and fee proposals should reflect these constraints.
 - **References**
 - **'Fit'.** Pension trustees may wish to consider involving the charity in the selection process, especially where the organisations are dealing with challenging pension issues. Finding advisers who are credible to both the pension fund trustees and the charity is important if they are to build consensus.
-

Case Study 3: Adviser Selection

Mira Mohideen, Head of Pensions at Royal Mencap Society sets out the steps taken by the Trustees of the Mencap Pension Plan to change advisers.

Background

A formal review had not been undertaken for some time and the issues relating to a protracted actuarial valuation exercise in 2011 and escalating costs, prompted the Trustees to undertake a review. The impending valuation in 2014 meant that the exercise had to be completed within a six month time frame.

Steps taken, in a nutshell

- In early 2013, a benchmark exercise was undertaken. A total of 10 providers across the market were included in this exercise.
- Over a period, all of the work relating to the management of the Plan had been outsourced. As part of this exercise, we agreed to bring a number of these in-house which helped to clearly set out the scope for work being outsourced.
- A Third Party Evaluator (TPE) was appointed to support with the exercise. The TPE appointed had a good understanding of the market and provider capabilities.
- Clear criteria for the appointment were established. These were:
 - Cost effective provider (discounted rates recognising the finances of a charity)
 - Understanding of how charities operate and experience of working with them
 - Truly joined up service delivery model (needed to be seamless)
 - Creative advice to help mitigate the deficit and keep it from deteriorating further
- Ability to engage with the employer (the Trustees of the Charity) positively

- A sub-committee consisting of 3 Trustees, the Head of Pensions and the TPE was set up to take the exercise forward
- Based on the outcome of the benchmark exercise, a shortlist of five providers, including the incumbent, were sent the formal Invitation to Tender (ITT)
- From the responses, using the criteria above, a final shortlist was drawn up
- Arrangements were made to site visit the finalists. This is a very important aspect of the selection process as most organisations have the broad skill set required. However, the team put forward and the culture of the organisation is what makes the difference and meeting the people and visiting their offices helps to nail this down
- The last stage was a presentation to the full Trustee Board and the employer by two finalists after which an appointment was made in July 2013.

Key Lesson

The final decision is never easy, so keeping focussed on the criteria and being objective every step of the way is a necessity. To help us ensure objectivity we used a form of scoring at each stage of the process. Our TPE was very helpful in this regard.

Outcome

The combination of bringing work in-house and changing advisers dropped our costs significantly. We used the transition to clean our data. During the implementation historic issues were uncovered which, once resolved, will lead to further cost reductions. The valuation exercise has commenced and the fresh and creative approach brought to us by our new adviser is already making a significant difference to the experience and hopefully to the potential outcome.

Section 4

Defined Benefit



4.1 Introduction

A traditional DB scheme aims to pay a pension based on the number of years an employee works for an organisation and their salary (usually at the time of retirement). These schemes are therefore often referred to as ‘final salary schemes’. The reasons why these schemes are now rarely open to new members are as follows:

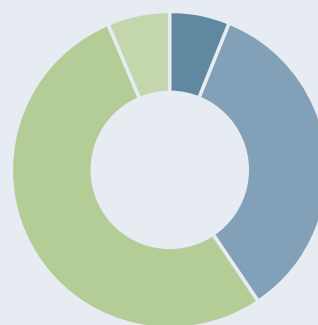
- the original funding assumptions on which these promises were made were not valid in practice leading to higher costs for the employer than anticipated because people are living longer (longevity) and inflation, expected return and trustee tolerance to risk are lower;
- tax changes, particularly around Advance Corporation Tax have reduced returns and resulted in higher contributions from the employer;
- lower real rates of return on investments over the last few years have led to increased demand for higher contributions from the employer;
- pension liabilities are much more visible as more and more charities disclose deficit on the financial statements.

Cost increases have highlighted the inherent risk in DB schemes as a result of which employers have sought mitigate risks by closing schemes to new members and to future accrual and switching to lower risk (to the charity) DC schemes for all employees, or made other changes to reduce risks.

DB pension deficits continue to pose significant challenges to many charities. In many cases the pension scheme – and its associated risks – can be expected to grow relative to the size of the charity, even when the scheme is closed to future accrual.

CFG’s DB survey indicated that the profile of those with single DB schemes is as follows:

Please indicate the status of your main DB scheme



- | | |
|--|--|
| Open to new members | Closed to new members and closed to future accrual |
| Closed to new members but open to future accrual | In wind up |

Of those who intend to close their scheme to future accrual, all stated they will move to DC provision.

Charities who have not taken these steps will be under increased scrutiny in future and will need to have clear strategic reasons for keeping their scheme open. They will also need to have transparent and robust risk management processes in place in order to maintain the confidence of stakeholders, as highlighted in a recent report by the Charity Commission⁸.

It is increasingly common for charities to focus on a long-term target to wind up their DB scheme, and to put in place a plan to reach that target considering both cash payments and investment strategy together, whilst reducing risk along the way. Recent developments in technology make a dynamic plan of this type, based on day to day financial market movements, a realistic possibility for all schemes. Where charities have assets on their balance sheets these can help support extended deficit Recovery Plans, which balance

⁸ Charity Commission report: www.charity-commission.gov.uk/media/606120/amr_pension_scheme_deficits.pdf

the interests of the charity, the pension scheme members and scheme trustees.

Charities can make proposals to scheme members to modify their benefits in a way that reduces long-term risk to the charity. Scheme members may find these options more favourable. The implications of the 2014 Budget on the modification of benefits are currently uncertain: it may increase or reduce the scope for such exercises in the future, or make transferring out of a DB scheme more attractive. In any case the 2014 Budget has introduced short-term flexibilities which many employers will wish to make available.

4.2 Background

A number of risks are posed by DB schemes to the charities that sponsor them. The costs of this type of pension are uncertain. These challenges can be illustrated in this stylised diagram which follows the valuation of a DB scheme from one valuation to the next.

If all things worked out the way the valuation had assumed they would in 2012, the pension scheme deficit should have fallen by 2015 because of the contributions to the deficit Recovery Plan. In the case of this scheme, asset returns may have been lower than expected, payments to pensioners may have been higher and the new assumptions that the Pension Trustees feel are appropriate in 2015 may also have added to the deficit valuation. Few aspects of these variables can be controlled directly, if at all, by the charity.

This section sets out a range of issues for charities with DB schemes. We look at current funding and

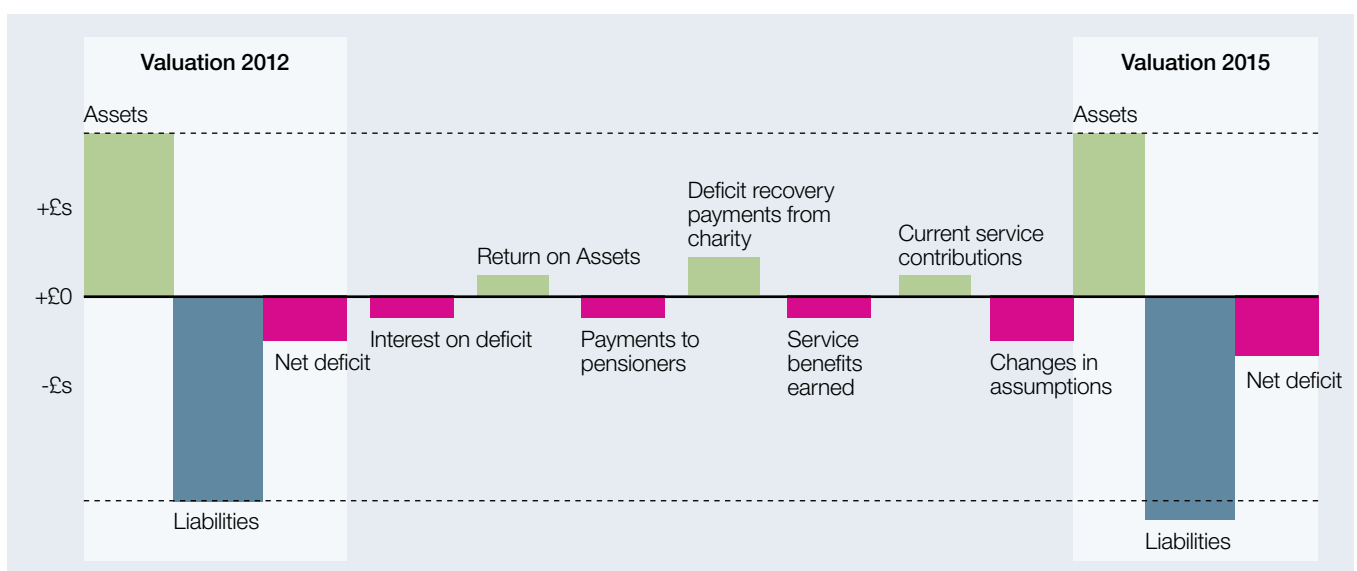
investment issues, including the implications of the current pension funding regime, and the latest input from the Pensions Regulator.

4.3 Pension Scheme funding for charities

The current funding regime has been in place for almost ten years. During that period many charities have faced demands for increased contributions from their pension trustees.

The Pensions Regulator's (TPR) 2014 guidance encourages pension trustees to seek contributions that are 'appropriate' (balancing the need to achieve full funding of the pension scheme as soon as possible against what is affordable for the employer, without affecting the sustainable growth of the employer's business).

Charity trustees will seek a balance between what they spend on, or invest in, charitable activities, and what they will spend on deficit Recovery Plans when considering how they spend their unrestricted income. A charity which reduces its charitable expenditure to fund a quicker Recovery Plan will need to consider the perception of funders and stakeholders. Diverting cash towards a quicker Recovery Plan bears the risk of alienating a supporter base. The charity's 'brand' needs to be protected in order to ensure the financial sustainability of both the charity and the pension scheme. The pension scheme and charity trustees both have a role to play. This requires a sophisticated and mature relationship between the two boards. It becomes more crucial when we consider the complexity of the legal and regulatory



frameworks on financial management of charitable income and assets. Building a strong, dynamic and trusting relationship between the two sets of boards is discussed further in Section 3.

There is an increased emphasis on managing risks holistically. For example considering what could go wrong with an investment strategy and the extent to which the employer would be able to fund any additional deficit which might arise.

The general trend over the last ten years has been increasing employer contributions. Charity employers have had to react to these increasing cash requirements, for example by taking another look at the pension benefits they can afford to offer or by increasing member contributions, where that is possible. Charities have also had to tackle pension deficits at the very time pension costs are increasing as a result of auto-enrolment (see Section 7 for more auto-enrolment details).

The sections below explore some specific aspects of the funding regime and solutions that charities can use, reflecting their particular circumstances. In summary, there are three key places where it is important for a charity to negotiate with pension trustees to reach the best outcome for their charity:

- the assumptions behind technical provisions;
- the covenant assessment; and
- options for Recovery Plans, including options for investment strategies.

4.4 Employer Covenant

The Pensions Regulator has emphasised that the strength of a sponsoring employer's covenant should inform all the decisions of the pension trustees in relation to a scheme funding valuation. Their guidance states 'In terms of cash-flow, the employer covenant represents the ability of the employer to provide the necessary cash flows envisaged to support ongoing accrual, the deficit repair agreed in a Recovery Plan and to account for any adverse performance compare to that assumed in the plans'.

The employer covenant is therefore a judgement of the charity employer's financial position, which can take account of its financial prospects and its capacity to fund the scheme. It is both backwards and forwards looking. It is important for the charity trustees to recognise that the pension trustees are required to ask appropriate questions to analyse the covenant. It also helps to consider

the information that the pension trustees will focus on, so that appropriate information on the charity's finances can be presented helpfully.

The Pensions Regulator has made it clear that pension trustees have a duty to keep the employer covenant under review and not simply address this at each triennial valuation. That means pension trustees must ask for regular information about the charity and make sure that they understand it. If charities want pension trustees to form an accurate appreciation of the covenant it is essential they provide information which is relevant and simple. This should not be seen as a burden. Strong relationships are necessary for delivering shared objectives for the charity and pension scheme.

4.5 Assessing the size of the liability: 'Technical Provisions'

The Technical Provisions are a prudent estimate of the amount of money needed now to provide the future benefits that members have earned in the pension scheme. Effectively this is the liability of the pension scheme. The difference between the liability and the assets of the scheme determines whether the scheme is in deficit or in surplus.

By how much the scheme is in deficit is a starting point in the negotiations that will determine the cash requirement under a deficit Recovery Plan. Given The technical provisions are driven by assumptions that may appear abstract but it is important that charities understand the basis of measures as they play a key role in determining the amount of cash a charity needs to pay. For instance, reducing the assumed level of investment returns by a seemingly insignificant 0.1% a year could add more than 2% to the Technical Provisions.

The pension trustees must consult with the employer on the selection of the assumptions used to calculate the Technical Provisions (and generally will want to reach agreement). One of the key challenges for pension trustees and the charity employer therefore is to understand the assumptions, and their implications sufficiently to reach agreement. Charities increasingly ask for advice to help them review the assumptions proposed by the pension trustees.

4.6 Recovery Plan and Recovery Periods

A Recovery Plan is the plan agreed between pension trustees and the employer to tackle any funding deficit. A Recovery Plan sets out the time period over which the deficit should be repaid and what the payment profile should be. The payments to repay the deficit are calculated so that if repayment is not immediate, an implied rate of interest is charged on the outstanding balance in the same way that a loan would operate.

4.7 Extending the Recovery Plan

There is a general expectation that Recovery Plans ought to be ten years or less. However a charity may agree an extended period over which to fund the deficit. The longer the Recovery Period, the more assurance the pension trustees will need on the future plans of the charity and how they drive financial viability in the longer term. It should be noted that charities differ markedly from enterprises. There is no pressure to pay a dividend to shareholders and they are subject to oversight through boards of trustees and sector regulators. As such, there are different mechanisms in place to protect their long-term viability. In addition, any charity that walks away from its pension commitments is likely to suffer considerable reputational damage. Charities are therefore walking a fine line when it comes to protecting their reputation whether by paying too much into a pension scheme, or conversely, too little.

Charities with significant pressure on cash-flow may be able to extend the period of their Recovery Plan by giving additional assurances. Pension trustees will need to ensure that any extended period will repay both the implied rate of interest as well as the underlying deficit balance. Potential options might include the following (NB: circumstances are likely to be highly specific to individual charities):

- Where a charity has significant assets on its balance sheet (such as heritage assets, property, or investments,) and relatively few other creditors, assets could be pledged to support the pension scheme in the long-term, subject to the regulatory and legal constraints of their specific charitable status. On this basis, the pension trustees may agree an extended Recovery Plan, which will lower the immediate annual cash contribution towards the pension deficit.
- A charity may have a predictable income stream, for example from the royalties of intellectual property or the income from property leases which could be ring fenced.
- An employer could formally pledge 'contingent assets'; these would be passed to the pension scheme if, for example, the charity were to become insolvent. The charity might also emphasise to the pension trustees assets which are free from restrictions or liabilities. If a contingent asset arrangement meets certain requirements, it can also help to reduce a scheme's Pension Protection Fund levy (see below).

4.71 Modifying the Recovery Plan assumptions

While it is clear that the Technical Provisions must be set prudently, the Pension Regulator's guidance explicitly allows more realistic assumptions to be used for the Recovery Plan. An allowance for higher returns on equities held by a pension scheme during the Recovery Period, for example, could be used to justify lower contributions.

4.72 Focusing on affordability

A repayment plan does not need to consist of regular, equal instalments. The profile of the plan can be adapted to suit the particular circumstances. For example, it would be possible to agree a structure where contributions are linked to income; so if more income is received, more contributions are paid (or vice versa).

4.8 Closing Schemes to new entrants and, or, Future Accrual

In the short to medium term, many DB schemes, and the risks associated with them, can be expected to grow. This is compounded when employees continue to build up further benefits (future accrual). Charities that continue to have employees earning further benefits should consider their alternatives and ensure they are comfortable that the additional risk being taken on is manageable.

Before a charity employer decides to close to new entrants or future accrual, it will need to think carefully about what kind of pensions to offer employees in the future. Employees are normally offered membership of a lower risk DC scheme where the costs are known in advance. A number of charities have already taken this route. Depending on the circumstances, there may also be a requirement that the scheme trustees have some input into the decision to close to new entrants or to future accrual. In this case, the charity employer would need to persuade them of the reasons to make a change and they may seek mitigation for the removal of a future benefit promise.

The charity needs to be aware that pension trustees may amend their assumptions once the scheme is closed to future accrual, if they perceive that the charity is less committed to funding the scheme in the long-term.

The transition from an open scheme to one that is closed to new members and future accrual is not a quick exercise; there are stringent employee and member consultation processes that need to be followed before amending the structure of their benefits. The transition can take upwards of nine months to complete. Maintaining goodwill of the employees requires good communication and consultation and scheme rules may need to be updated. This can't be hurried.

4.9 Strategies for managing future risks

4.91 Managing a closed pension scheme

Once a scheme is closed to new members or to future accrual the conclusion of the pension scheme may still be some way off. Charity trustees, concerned with the long-term financial sustainability of their charity must grapple with their pension deficit in the medium term so that it is not a continuing legacy issue for their successors in decades to come. This leads to them to consider what strategies are available to reduce risk.

Risk can be reduced by changing to a lower risk investment strategy or, to a certain extent, managing the liabilities of the pension scheme. We cover ways to reduce risk and manage pension liabilities in the next few sections. In this connection, the changes in the 2014 Budget may prove to offer some valuable additional flexibility opportunities (see section below on the implications of the 2014 budget).

4.92 Investment options

Over the last few years, a wide range of 'alternative assets'; hedge funds, 'Liability Driven Investment' and derivatives, have become available to smaller pension schemes through pooled investment vehicles. These are all valuable building blocks for pension scheme trustees wishing to improve the trade-off between risk and expected return.

Assets such as diversified growth funds can be used to diversify and reduce the risk without significantly reducing expected returns. Derivative contracts can be used to reduce the risk to the pension scheme from high inflation, or from changes in interest rates, by improving the 'match' between the value of the assets and the value of the liabilities; thus reducing the variability of the deficit.

Charities often wish to encourage the pension trustees to consider these options, with a view to stabilising future employer contributions. The detail of these types of assets is outside of the scope of this publication; charities should seek appropriate advice, particularly as the investment strategy has an impact on the funding assumptions and hence contribution requirements.

Case Study: Pension Increase Exchange

John Graham and Helen Downie from the Royal British Legion (TRBL), tell us about using a Pension Increase Exchange exercise to manage their DB scheme.

“Like many charities the Royal British Legion has a deficit on their DB Pension Scheme. The actuarial valuation at April 2008 showed a deficit of £5.4 million which rapidly escalated in 2009 to over £15 million. The last valuation in 2011 reduced the deficit to £2.4 million but these major fluctuations caused us at the Royal British Legion to look at what action we could take to improve the management of the deficit.

The fund had already been closed to new members in 2003 and in April 2010 the scheme was also closed to future accrual. These actions removed exposure to future liabilities but left the historic liabilities untouched. To tackle these we looked at two options, an ETV (Enhanced Transfer Value) exercise and a Pension Increase Exchange (PIE). ETV required more investment up front and historically the results of such an exercise have been mixed. PIE seemed to offer more certainty of a positive outcome and became our choice.

In PIE an offer is made to pensioners to give them a significant increase in their pension now in return for giving up (non-statutory) pension increases in the future. The increase is less than the full value of the inflation and longevity risk and so has the effect of reducing the deficit. In negotiations with the pension trustees we agreed that, of the actuarial valuation of the increases given up, 60% would be used to enhance the immediate pension leaving 40% to reduce the deficit. The business case, agreed with the Legion trustees, showed an upfront cost of around £200k with an expected take up of between 10% and 15% to yield a deficit reduction of up to £1 million.

The first stage of implementation involved an offer to eligible retired members; those with pensions earned before 1997 and in excess of the Guaranteed Minimum Pension (GMP). NAPF's, Code of Good Practice on incentive exercises published in 2012 recommends that full, independent financial advice (IFA) is made available to scheme members to help them decide whether or not to take up the offer. Through competitive tender the Legion appointed an IFA to advise scheme members. We worked with the IFA and our actuaries to ensure all member correspondence was clear, concise, unbiased and in line with the Code. The Pension Trustees have been kept fully informed at each stage.

We contacted eligible members with a 'warm up letter' which outlined the scheme and gave the member the opportunity to opt out; very few members did so. The warm up letter was followed up with a full offer letter and members were asked to contact the IFA for free, independent advice initially by telephone.

The response to our offer has been positive, with just over 20% of members accepting. Of those, 25% are called 'insistents' – those who the IFA have advised is not in their interest but who nevertheless have taken up the offer. The cost budget was achieved and liabilities have decreased by over £1 million. Following this success we have now extended the offer to future retirees. Delivery of this option will take time as our members mature and retire. However, we are optimistic that this option will be attractive. 90% of all members retiring from the scheme currently commute some of their pension. Embracing PIE, a retiree will be able to take the commutation and then enhance the reduced pension closer to the original value.”

Further considerations that pension scheme trustees might make when determining the investment portfolio of the schemes assets include whether the employer covenant calls for lower risk investment strategies. Charities ought to be mindful of this during covenant assessment discussions, Recovery Plan negotiations and investment reviews, since this has the potential to increase future contributions.

Pension law requires that the trustees of the pension fund should prioritise the best financial return for the membership; charity law regarding investments makes similar demands. However, charity trustees are also obliged to ensure that any investment choices they make do not detract from their charitable objectives. Circumstances can exist where a lower financial return is acceptable to avoid reputational damage, affect a social return or balance risks and secure capital.



Further considerations that pension scheme trustees might make when determining the investment portfolio of the schemes assets include whether the employer covenant calls for lower risk investment strategies. Charities ought to be mindful of this during covenant assessment discussions, Recovery Plan negotiations and investment reviews, since this has the potential to increase future contributions.



Pension law has developed to require trustees of most occupational pension funds to include in their Statement of Investment Principles the extent to which, if at all, social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investments and their policy in relation to their rights relating to those investments (e.g. voting rights attaching to shares). Such considerations remain subject to the overall principle that trustees have a fiduciary duty to act in the members' best financial interest.

As charity investment strategies have come under increased public scrutiny (for example the Panorama program in December 2013 'all in a good cause' scrutinising the investment choices made by a number of household names), it would not be surprising if the investment choices of charity pension schemes falls under the same spotlight in the near future.'

4.93 Insurance solutions, including buy-in and buy-out

A buy-out allows the charity to settle all of its remaining pension scheme liabilities. The buy-out passes the liabilities, assets, and associated risks to an insurance company, which charges a premium in return. The pension scheme can then be wound up.

Schemes can also purchase annuities for some, rather than all, of their members whilst the scheme continues. This could be a partial buy-out where the annuity policies are in the members' names.

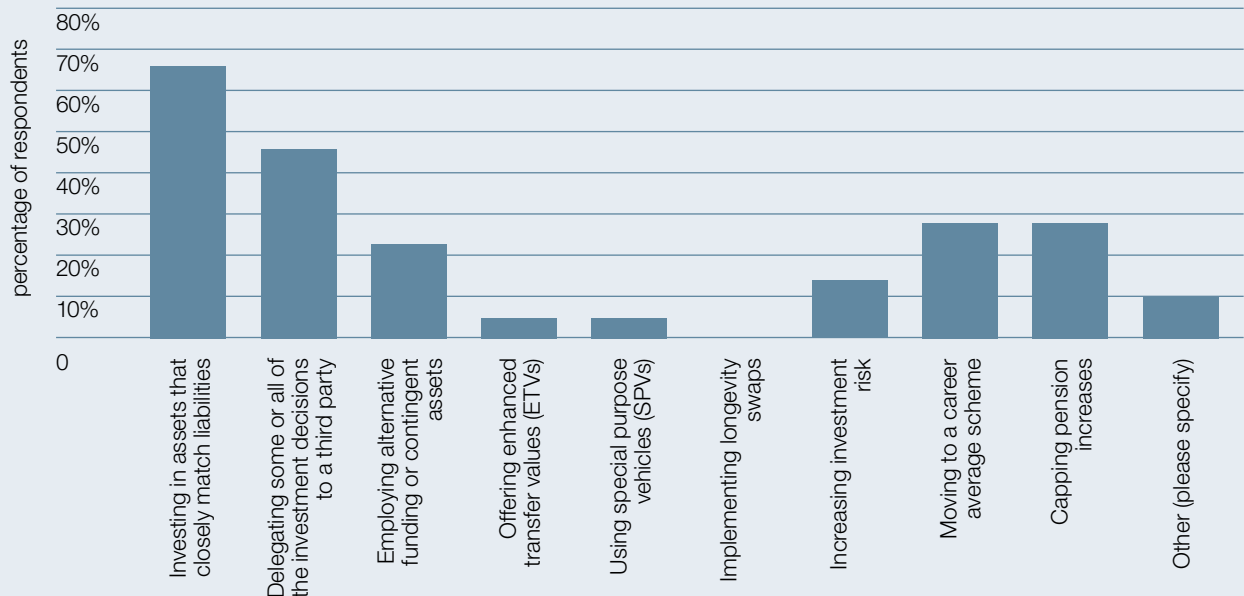
Alternatively, the annuity policies could be owned by the pension scheme, known as a 'buy-in', and normally covers members who are pensioners. In a buy-in the pension trustees own the buy-in policy, an insurer pays an aggregate amount to the scheme equal to the total pensions payable to the members covered by the policy; and the scheme uses that income to pay the pensioners. This has the advantage of exactly matching specific liabilities for the members included in the buy-in policy, but leaving the remainder of the scheme assets invested in higher yielding investments. The aim over a period of time is to reach the position where the remaining liabilities can be bought out with little extra cost.

Over the last five years, premiums for buy-in exercises in particular have compared well with the value of government bonds, which some pension schemes hold to support their liabilities for pensions in payment. This has made buy-ins attractive to charity and scheme trustees looking to reduce risk. For example, if a scheme is able to match some, if not all, of their liabilities with government bonds, they might look to purchase annuities instead. This would have the effect of not just matching the liability but moving the risk outside the scheme. Such a step would require careful planning and research.

4.94 Focusing on the 'end game' – Flight Paths

Pension scheme investments are made to meet long-term liabilities. This means traditionally, pension schemes, review their investment policy and mix of investments from periodically. This approach means that pension schemes are unable to take advantage of short term market changes to manage liabilities.

Have you used any of the following measures to manage DB risk?



It is increasingly common to put in place a plan to achieve self-sufficiency and, or aiming to buy-out and wind up the pension scheme in say 10-15 years. These plans are often called 'flight paths'. The target is to be fully invested in low risk assets at some time in the future with enough money to buy-out all the scheme benefits. In the meantime the funding of the scheme is projected to improve through contributions and returns from performance seeking investments, such as equities and property etc.

To effect this plan, the pension trustees and charity employer agree a target rate of investment return or target funding levels. Technology is now available to monitor actual returns or funding levels against this target on a daily basis. When returns or funding levels exceed the target, the investment manager is then instructed, in some cases, on a delegated basis to switch some of the performance seeking assets into lower risk assets to improve the match between assets and liabilities. This approach effectively crystallises any better than expected rates of return as they occur, can significantly reduce the risks for an employer and add real value by capturing the good

performance. Pension trustees need to agree up-front triggers for switching the assets and instruct the investment manager to do this automatically to reduce the risk of missing opportunities when markets are favourable.

4.95 Liability management exercises

Over the last few years, some employers have engaged in exercises aimed at reducing risk and managing their pension liabilities. These tend to involve:

- reminding pension scheme members that they can transfer their pension to another arrangement or that they can take a cash lump sum on retirement;
- offering an incentive for members to take a transfer;
- offering members the opportunity to exchange a pension which would increase in the future for a higher pension now (with lower or no future increases); or
- permitting early retirements.

⁹ The Charity Commission have guidance for trustees on charity investment matters: www.charitycommission.gov.uk/publications/cc14.aspx. CFG has produced a range of briefings and publications on this matter: www.cfg.org.uk/resources/Publications/cfg-publications.aspx

¹⁰ The NAPF has produced a code of practice for these matters: www.napf.co.uk/PolicyandResearch/DocumentLibrary/-/media/Policy/Documents/0257a_Incentive_exercises_for_pensions_a_code_of_good_practice_-_June_2012.ashx

Are you currently using any contingent assets to support the funding of your pension scheme?



From the charity employer's perspective, offering members options like this can mean settling their liability more efficiently. Some pension trustees and some employers, particularly in charities, feel uncomfortable undertaking exercises involving incentives, due to the potential reputational risks of offering employees excessive benefits. A code of practice¹⁰ has been developed which provides guidelines that industry expects to be met.

CFG's DB survey results indicated what options charities are exploring to manage the risks posed by their DB schemes.

4.10 March 2014 Budget

The March 2014 Budget changed the way in which members of DC Schemes will be able to take benefits. In essence, on retirement from the minimum pension age (which currently stands at 55) a member no longer has to buy an annuity. Instead, they are able to draw down their pension fund immediately or spread pensionable payments over time as they wish. Note that this is subject to income tax and governed by rules specific to the scheme.

While this does not apply directly to members of DB schemes, members of DB schemes could potentially transfer their DB benefit to a DC scheme and then take advantage of this new flexibility. At the time of writing (June 2014), there is a consultation on whether the government should ban transfers from DB to DC for non-public sector pension schemes (they are banned for unfunded public sector schemes). If no ban is imposed employers may consider whether to offer transfer value exercises to their employees; the new flexibility may make a transfer to a DC scheme

much more attractive. If this happens, there could be a significant demand for transfers from DB schemes, driving a substantial increase in the cash payments schemes need to make. This could influence investment strategies, at least to ensure that sufficient cash can be raised if needed.

Another 2014 Budget change that will affect virtually all schemes is the change in the definition of a small lump sum or trivial pension. A member can now take their entire pension pot in a pension scheme as a lump sum (subject to applicable income tax) provided that their pension pot in that pension scheme is worth less than £10,000. A member who has pension pots across a number of pension schemes can take what is known as a trivial commutation lump sum if the member has pension savings across these pension schemes which do not exceed £30,000. Members who take this option reduce the scheme's risks and the administrative cost of paying small pensions. Whilst many employers will want to encourage this, the specific circumstances of each scheme will need to be considered.

4.11 Pension Protection Fund

The PPF is currently consulting on a change to the way it calculates its levy which will have a big impact on the charity sector.

The Pension Protection Fund (or PPF) (www.pensionprotectionfund.org.uk) acts as a 'lifeboat' for Defined Benefit schemes when the employer is insolvent and the scheme hasn't enough assets to pay for benefits in full. In such circumstances, the scheme assets are passed to the PPF, and the PPF pays compensation, in the form of pension benefits, to the scheme members.

In summary, the compensation based on the member's circumstances at the time of entering the PPF is as follows:

- Any member who is over their normal retirement age or who retired early due to ill health will receive 100% of the pension they are currently receiving.
- Other members will receive the 90% level of compensation capped at a certain level. The cap at age 65 is, from 1 April 2014, £36,401.19 (this equates to £32,761.07 when the 90 per cent level is applied) per year.

The PPF also offers a dependent's pension (where this was payable under the rules of the former pension scheme) of half the member's entitlement. There is some inflation protection for benefits, but this indexing is very likely to be less generous than under the original scheme.

To fund the payment of benefits to members the PPF has the following sources of income; the assets which are transferred in from the original scheme (and those resulting from recovery arrangements); the return achieved on its investments; plus the levy they raise each year from ongoing solvent schemes and, therefore, indirectly their sponsoring employers. The size of the levy a scheme will be charged is broadly determined by three variables:

- The overall amount the PPF estimates is needed from all employers across all schemes.
- The size of the deficit of the individual scheme, as determined by a 's179' valuation (adjusted to reflect the specific investment strategy of the pension scheme).
- The perceived likelihood of the employer becoming insolvent and the insolvency risk.

In broad terms, the levy will be larger for charities with the biggest deficits and a higher probability of insolvency. The PPF relies on an external provider to determine the insolvency risk. The organisation measuring this risk is changing to Experian from Dun & Bradstreet and the change in methodology will have a big impact on charities as a whole. To date most charities have been assessed as a broad group and have generally been assessed as being in Band 1, representing the lowest risk. Whilst many will continue to receive this rating there is likely to be more differentiation in scores between the strong and the weak. This, and the

more limited data Experian holds on not for profit organisations makes it important to engage to ensure that the entity's score is appropriate. Whilst in common with other sectors, most schemes should see a lower levy, around a third of schemes are predicted to see an increase and some increases could be large. The cost per £1m of deficit of the levy can be illustrated as follows¹¹:

Band	D&B	Experian
1	1,300	1,200
2	2,000	1,700
3	3,200	2,200
4	5,000	2,900
5	8,000	3,900
6	11,700	5,500
7	14,700	8,100
8	19,000	11,800
9	22,300	17,600
10	29,200	28,300

Whilst it is important that this table is not used as a forecast of actual rates for 2015/16, as it is based on 2014/15 data, it shows that charities which move to higher risk bandings as a result of the Experian rating may see their levy increase substantially.

Charities should quickly establish the likely impact of this change on their levy and can do so through an online portal which trustees and their advisers can use to view the scores for their sponsoring employers – and the data that is held on them. Experian have emailed the trustees specified as contacts on The Pensions Regulator's Exchange system, with information on how to log on. Experian and the PPF are encouraging everyone to check their scores, and the data being used to generate them. The only grounds for appeal against a levy rate will be on the basis of the underlying data, so it is vitally important that charities ensure the data that Experian holds is correct. In particular, it will not be possible to be scored as a not for profit entity unless it falls within the definition in the Levy Rules – on which the PPF are consulting.

The PPF can reduce the levy where a charity can provide contingent assets. This approach needs careful consideration as the requirements to be successful are considerable. (www.pensionprotectionfund.org.uk/levy/riskreduction/Pages/ContingentAssets.aspx)

¹¹ This table is based on data from the PPF Combined annexes for Consultation Document, 29 May 2014

Section 5

Multi-Employer Schemes



A multi-employer scheme is a scheme where a number of employers participate under a single trust arrangement. Many charities chose to participate in schemes of this type as they presented an opportunity to share cost and pool risk. Each multi-employer scheme needs a single set of trustees, deed and rules, and one administrative set up. The costs therefore could be spread amongst the participating employers. Certain multi-employer schemes also enabled the pooling of risk, by ‘cross-guaranteeing’ one another’s liability. However, the extent to which the implications of this were fully understood by the charities involved at the time is debatable.



67% of CFG survey respondents are in a multi-employer scheme or a Local Government Pension Scheme



CFG’s DB survey indicated that the majority of charities would, or would consider closing their multi-employer scheme to future accrual if they could do so without triggering a section 75 debt. This high figure reflects the concern amongst charitable employers of the risks represented in keeping multi-employer DB schemes open.

There are two types of multi-employer scheme: segmented and non-sectioned.

Segmented multi-employer schemes operate in a very similar way to stand alone pension schemes where each participating organisation has a distinct ring fenced asset and liability share. In this instance, the main benefits of participating in a multi-employer scheme, is the sharing of costs.

A non-sectioned multi-employer scheme (also known as a last man standing multi-employer scheme) operates in a different way from standalone arrangements. The assets and liabilities for all the employees of the participating employers in the scheme are pooled (although allocated on a ‘notional’ basis). This provides some risk sharing advantages as the longevity, salary and investment experience are shared between multiple organisations and, from a member perspective; benefits are effectively protected by all the participating employers and not just their employer.

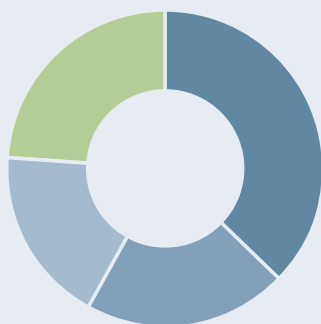
As the funding position of DB schemes has deteriorated over recent years, these schemes have exposed participating employers to additional risk.

5.1 Section 75 debts in multi-employer schemes

Many charities that have their own DB schemes have sought to minimise future risk by closing them to future accrual. In the case of multi-employer schemes, this entails the triggering of a ‘section 75 debt’ unless all employers in the scheme agree closure to future accrual at the same time. In reality, this is difficult to achieve, particularly where the employers are not related.

Since 2006, legislation under section 75 Pensions Act 1995 has required that a non-sectioned multi-employer scheme (an ‘active multi-employer scheme’) be treated differently from a non-sectioned multi-employer scheme in which no employers employ active members (a ‘frozen multi-employer scheme’).

Would you close the scheme to future accrual if you could do so without crystallising the section 75 (exit) debt?



Yes, definitely	Yes, we might consider it
Yes, we would strongly consider it	No

In an open multi-employer scheme, an employer who wishes to cease participation must depart the scheme after paying a debt based on:

- the cost of buying-out all pension accrued by employees attributable to that employer with an insurer;
- the employer's share of any liabilities that are not attributed to any employer remaining in the scheme ('orphan liabilities'), calculated on that same basis;
- the costs associated with calculating and collecting the debt.

This total liability is the employer's 'section 75 debt'.

The assumptions underlying the calculation of the section 75 debt are stronger than those used for the ongoing funding assessments, a fact which is often not appreciated. As a result of the stronger assumptions, the section 75 debt is greater than the funding value of the liabilities associated with the employer at time of calculation. It is also critical to understand that the debt payment is triggered as soon as the employer exits the scheme. Although there have been cases where employers have negotiated repayment plans for the debt, scheme trustees are under no obligation to facilitate this payment in this way, and in most cases demand immediate payment. Generally, therefore, it risks a considerable cash demand on the charity wishing to exit the scheme.

Although the debt is based on the cost of providing annuities at then-current rates, no annuities are required to be actually purchased for any scheme members. Instead, any payments made towards the debt are usually added to the scheme's assets and spread to cover the on-going future liabilities of the scheme, including the liabilities attributable to other employers.

There is also a mechanism under legislation which allows an employer to trigger the debt in a frozen multi-employer scheme by the giving of notice to the trustees.

This is in contrast to the treatment of a frozen multi-employer scheme. Although no further accruals are being made in respect of any employer in such schemes, participating employers may continue to participate, making deficit contributions on an on-going basis. A section 75 debt will only arise if an employer applies to the pension trustees to trigger their

debt, an employer winds up, becomes insolvent or decides to move its liabilities (and associated assets) to another pension scheme. A charity with their own pension scheme therefore has much more flexibility to manage and reduce its long-term risks arising from their pension obligations than one in a multi-employer scheme.

The fact that a much larger debt will be assessed on stopping future accrual than if an employer continues to accrue additional liabilities in an open multi-employer scheme presents a number of issues for individual participating employers, for the scheme and for remaining employers.

5.11 Problems arising from section 75 debt for individual employers

- Some employers otherwise capable of paying deficit reduction payments indefinitely into the future, cannot meet the cash demand of the section 75 debt and so must continue to accrue further debt by keeping active employees in the scheme.
- The fact that the section 75 debt increases as further liabilities accrue makes it more likely that, should the section 75 debt arise, it will lead to the insolvency of that employer.
- Even if the employer can manage to pay the section 75 debt, this does not secure the benefits for its employees, but rather to members of the scheme generally, making the employer more reluctant to incur the debt.
- There is little incentive for individual employers within these schemes to fund the scheme over and above the rate which is affordable for the weakest employer, since this does not derive any individual benefit. Disincentivising employers in this way increases the challenge for ensuring the scheme is appropriately funded, and ultimately, increases the overall risk for the scheme.
- Where a scheme has been closed to new members, employers run the risk of accidentally triggering the debt if the last active member leaves their employment. With only deferred members and pensioners remaining, the scheme will demand immediate payment of the debt in most cases.

5.12 Problems arising for the scheme itself

Whilst here we have concentrated on the 'catch-22' for employers, the schemes themselves are also placed in an increasingly painful vice due to increasing liabilities. The liability of the scheme continues to grow, while fewer employers are able to fund it.

In addition, the covenant of each employer needs to be considered when agreeing funding plans for meeting any deficit. The weaker the covenant, the shorter the Recovery Period leading to higher cost.

5.13 Problems arising for employers remaining in the scheme

As the number of employers reduces, remaining employers in the scheme will be obliged to pick up the liabilities of employee's employed by others. This risks a 'domino' effect – insolvency leaves behind more orphan debt leading to increased funding cost which can push further scheme employers into insolvency, and so on. On the other hand, employers that remains in the scheme while other employers leave, paying all or some of the section 75 debt, may see their liabilities fall.

DWP are currently considering a submission by CFG proposing to address these concerns, by making amendments to secondary legislation¹².

5.2 Restructures

Charities are increasingly looking to create partnership and mergers with other organisations in order to capitalise on their social impact and maximise effective use of resources.

Restructures through incorporation, mergers or take-overs are more problematic within multi-employer schemes. Should one employer cease to exist as a result of a change in organisation structure, a 'cessation debt' is triggered. Flexibility now exists through the use of apportionment and withdrawal arrangements, although these could be complex and costly to complete. There have been a number of instances in the last decade of merger or restructure negotiations coming to a standstill due to incompatibilities with pension arrangements. In particular, cases where charities

with heavily aligned missions that wanted to merge to form a new entity, were unable to take on the liabilities of the participating organisations and cases where the creation of a new entity, would have triggered a section 75 debt.

One trigger for the debt is known as an 'employment cessation event'. This occurs when a participating employer ceases to employ any active members within the scheme whilst at the time in question at least one other employer participates and employs active members¹³. This can happen in a variety of circumstances, such as a business transfer or share sale.

A change in the legal identity of the employer, such as the incorporation of charity trustees into a company with a limited guarantee, may be sufficient to trigger an employer debt (although see below). Similarly, a merger or amalgamation could trigger a debt, even though the previous employers are still part of the corporate structure. There does not even need to be a change of employment. The number of active members may simply reduce to zero through the passage of time for example where the last active member of the scheme retires or dies.

An employer wishing to end pension accrual in a multi-employer pension scheme will trigger an employment cessation event unless cessation could be coordinated to take place simultaneously with all other current employers¹⁴.

5.3 How to stop an 'accidental trigger'

Organisations need to be wary that they do not accidentally trigger an employer debt, especially where those employing the members do not change.

To stop employers facing large liabilities as a result of relatively simple restructuring, there are now two easements where an employment cessation event will not be deemed to have occurred. Both easements require a procedure to be strictly followed.

¹² Ref to on website.

¹³ An example of this in action would be the Growth Plan section of the Pensions Trust, if you cease to employ active members (assuming all the other current employers do not cease to employ active members at the same time) you trigger an employment cessation event.

¹⁴ The practicalities of this are difficult but not impossible. The author has done this in relation to a multi-employer pension scheme with around eight different (and non-associated) charity employers.

The first, the general easement, is designed for cases where a single employer is being replaced by another single employer (such as a legal identity change). The pension trustees need to follow a seven-stage decision making process. If, as a result, the trustees are satisfied that the receiving employer is at least as likely as the transferring employer to be able to meet the liabilities of the scheme, an employer cessation event will be deemed not to have occurred.

In situations where the liabilities involved are very small (the total annual amount of accrued benefits are less than £20,000/year), organisations may be able to rely on a de minimis easement. In both circumstances, Trustees will need to follow a strictly defined procedure and act without delay.

If employers discover that they have inadvertently triggered an employment cessation event, if they act quickly (within two months), they can apply for a 'period of grace'¹⁵ notice from the pension trustees, essentially freezing the trigger for a twelve month period. If the employer employs an active member within this time, no section 75 debt becomes due (the trigger is effectively undone).

5.4 Statutory employers (and dealing with section 75 liabilities)

Section 75 debts are the responsibility of 'statutory employers', i.e. those employers that meet the statutory definition and, as a result, are legally liable for debts arising. It can be more difficult than first appreciated to identify who the statutory employer is. For this reason, pension trustees are now required to identify the scheme's statutory employer in their Scheme Return to the Regulator.

A statutory employer for section 75 purposes is any entity which has employed an active member (or someone eligible to be so) since December 1996. This is subject to various exceptions. For example, an employer who has paid their section 75 debt upon leaving the scheme is no longer considered a statutory employer.

Another way for employers to be relieved of their status as statutory employer is through entering into a 'form of apportionment'. This is a legally enforceable agreement whereby another employer agrees to take over the old employer's scheme liabilities. In a similar way, an exiting employer could seek agreement to pay a lesser sum than the full exit debt in return for another entity guaranteeing the remainder.

Those who remain statutory employers will be left exposed to a scheme's hidden liabilities. For example, when it is not possible to match a liability for a member to a statutory employer, it is classified as an 'orphan liability'. The statutory employers in the scheme will assume responsibility for their own share of the overall deficit and a proportion of the orphan liabilities.

Employers need to ensure that when they 'leave' a pension scheme, they do so in a manner that results in their full discharge and they do not inadvertently retain residual liability towards the pension scheme.

¹⁵ Referred to by the Pensions Minister Steve Webb in his address to the CFG Conference, summer 2013.

¹⁶ A look on their website will show the range of different pension vehicles on offer and the myriad of different employers. A number of employers have their own 'white labelled' scheme that is ring fenced and operated by TPT for the charity in question. The author has been involved in advising charities that have transferred their external standalone scheme into a new bespoke section within the Pensions Trust, essentially a pensions outsourcing.

¹⁷ Liability is limited to the value of the promises as calculated under section 75. In addition, employers can take steps to limit their liability by crystallising their liability at a point in time. The point is that should an employer not satisfy its liabilities then those liabilities fall to be paid by the remainder - the last employer standing could face a very large bill.

5.5 The Pensions Trust Growth Plan

The Pensions Trust is an organisation that provides pension schemes of various types, particularly to charities and not-for profits. They are probably the largest provider of multi-employer schemes to the charitable sector with their 'growth plans'. Consequently the running of their schemes has a significant bearing on the landscape of charity pensions.

The Pensions Trust is a 'master trust' type of arrangement whereby, under one overarching trust, there are a number of separate sub trusts. From a legal perspective these sub trusts are treated as if they are separate pension schemes.

Two large schemes which many charities will be members are 'the Growth Plan' and the Social Housing Pension Scheme', which are non-sectionalised multi-employer pension schemes for non-associated employers. They are large schemes used by many different employers who have no legal connection with one another and where liability is shared amongst all employers and arguably unlimited from a practical perspective.

As multi-employer pension schemes, the risks of triggering exit liabilities include employers wishing to cease accrual, active members being extinguished through retirement, death or leaving service, and organisational change or restructure. Any event that could have a material impact on the covenant of the employer may be of concern to the Pension Trust.

Growth Plan (GP) has been running for decades and is made up of four series. The management of these four plans is related under the umbrella of the Growth Plan arrangements.

The four growth plan series are as follows:

- Growth Plan Series 1 (GP1) – The General Fund was established in April 1946 and closed to future benefits on 1 April 1997. Members purchased a defined amount of level pension at retirement with their contributions.
- Growth Plan Series 2 (GP2) – This was established as a replacement for GP1 on 1 April 1997 and closed to future accrual on 30 September 2001. Members purchased a defined amount of increasing pension at retirement with their contributions.
- Growth Plan Series 3 (GP3) – This was established on 1 October 2001, and was originally thought of as a self-contained DC scheme. Contributions are invested in a 'pot' for each individual; the pot is invested. The pension provided is not guaranteed but is based upon the contributions paid, the investment return achieved and the annuity rate available at retirement date. There is an underlying capital guarantee that the member's value will never be less than the value at the start of the year plus contributions. The Scheme trustees have invested the funds in low risk asset classes to limit their exposure to this guarantee.
- Growth Plan Series 4 (GP4) – This was established on 1 October 2008. This scheme is DC offering a choice of investment funds. There is no capital guarantee.

There has been significant legislative uncertainty over the last few years on the status of these schemes, sparked by the 2011 judgment in 'Houldsworth and another v Bridge Trustees and another and the Secretary of State for Work & Pensions' (the 'Bridge' case) was given. This case has caused considerable confusion about the extent of any liability which exists and to which organisations it applies; the DWP are in the process of clarifying the legal framework underpinning this case.

Whilst the outcome of these legislative changes are yet to be determined, as it stands GP 1 and 2 will continue to be treated as DB arrangements. Growth Plan 4 (GP4) will continue as a DC (money purchase) arrangement.

GP3 has been effectively re-classified as a DB scheme as a result of the underlying guarantee it contains. Prior to this reclassification, the assets and liabilities of Growth Plan 3 were broadly fully matched; however, because of the umbrella nature of the Growth Plan, the reclassification means that GP3 liabilities have been amalgamated with GP1 & GP2 liabilities. Consequently, many employers with only GP3 liabilities have been subject to a significant increase in their deficit. Those with only GP1 & GP2 liabilities have seen an equivalent reduction.

In an attempt to alleviate the impact of this, the Pensions Trust took the decision to close GP3 from the end of September 2013 and move future contributions to GP4 to prevent further accrual of GP3 liabilities. Whilst this was seen as a relatively simple solution for many of the employers participating, there are a number of potentially negative implications, for example, preventing the flexibility for employers to move to an alternative DC provider.

5.6 Advice for charities in multi-employer schemes

Given the challenges outlined above to managing liabilities accrued from multi-employer schemes, charity trustees would be forgiven for feeling the odds are stacked against them. Certainly, without legislative change, managing a charities exposure to these schemes will be demanding.

As a first step a board of trustees needs to ensure they fully understand the pension arrangements their charity has in place. This applies even when there are only a minority of staff and in some instances only one or two employees or ex-employees in a scheme. This is likely to involve pressing scheme trustees for a full understanding of future liabilities and valuations. You can find more on how to manage relationships with trustees to good effect in section 9.

Next, it is essential to monitor the membership of the schemes, to ensure that the section 75 debt either isn't triggered, or that sufficient contingency plans are in place if it is. In certain circumstances, the best course of action may be to withdraw from a multi-employer scheme. The case study below outlines how one charity went about doing so. It may be expensive and time-consuming, but the long-term benefits of being able to actively manage the charity's specific liability and assets could enable the charity to have a better long-term impact.

We are aware of cases where the long-term liability can outweigh a reasonable probability that the charity will be able to fulfil its obligations. In these circumstances, it is vital that trustees seriously consider taking advice on the long-term solvency of the organisation, and how the activities of the charity can be best maintained.

Case Study 4: Taking control of pension costs and risks

Having become increasingly concerned with the lack of control they had over their DB pension costs from participating in an industry wide multi-employer scheme, Caroline Hoare, the Director of People at the Girls' Day School Trust, explains how GDST worked with their advisors to bring this key business risk under control.

Our pensions challenges

Over the last few years we have been pursuing a strategy of taking more control over our own destiny and bringing a number of previously outsourced services in-house. Following careful analysis and thought, the Trust decided that it would be sensible to do the same with our pension provision for support staff.

Until 2012, we participated in a multi-employer DB scheme for independent schools (the ISPS). Whilst this kept running costs low, we were concerned about the lack of control we had over the risk levels in the scheme and the benefit flexibility we could offer our non-teaching staff. We felt we had little influence over the management of the scheme and were left exposed; because leaving ISPS would trigger a Section 75 debt (our share of the deficit in the scheme on a buy-out basis) of £50m, which simply wasn't affordable. A further consideration was the impact of auto-enrolment.

The solution

We worked closely with Hymans Robertson to implement a significant pension change programme that brought our costs and risks under control, and actually strengthened our employee engagement. Given today's environment of closing DB schemes, we took what might appear to be the unusual step of setting up a new stand-alone DB scheme. However, it made sense for us because:

1. it provided a vehicle to house a past service transfer of our share of the multi-employer scheme assets and liabilities, meaning we could exit without triggering the Section 75 debt (because we were not just walking away and instead funding it over time in our own scheme);

2. it gave us more control over the level of risk we wanted to run in the scheme and greater flexibility; and

3. whilst we were adamant that the change should not impact on benefit levels for staff already in the scheme, we were able to close the scheme to new joiners and set up a DC scheme, giving us a fit-for-purpose auto-enrolment solution.

It was difficult to know where to start on implementing all of this, our advisors actively and very effectively guided us through the whole process, negotiating the bulk transfer, and project managing the DB scheme set-up, the DC scheme set-up, the bulk transfer and auto-enrolment implementation.

The changes took place in the latter half of 2012 – we initially embarked on a comprehensive staff communication programme explaining the changes and consulting on the closure to new joiners. It was important to us that staff that had previously not joined the scheme were given the opportunity to join before the closure, and we experienced great engagement on this offer. Having set up the two new schemes, the changes took effect on 31 December 2012 and the bulk transfer followed in two payments during 2013.

Establishing our own pension scheme gave the Trust more influence over the scheme's assets. The GDST Scheme is now managed by a group of trustees nominated by the Trust and the scheme's members. Overall, we feel they will be better placed to ensure that the level of investment risk taken is proportionate to the size of the Trust's resources and ability to fund the scheme. We are delighted and relieved that we now have far more visibility, control and influence over our pension costs and risks, and look forward to the schemes settling down into business-as-usual.

Section 6

Defined Contribution



6.1 Setting the scene

A DC scheme is where an employee builds up a fund, by making regular contributions with the support of their employer, which can be converted on retirement to purchase an annuity in the member's name to provide income. An option is to take a proportion of the fund as cash on retirement. The rules surrounding these types of schemes are subject to radical reform as a result of the Chancellor's Budget in March 2014.

The pensions landscape as a whole is now dominated by these types of arrangement. The Pension Regulator's 'Purple Book'¹⁹ tell us that there are 6,150 DB pension plans. This number increases if we include smaller DB scheme managed by Insurance Companies. In contrast, DC schemes exceed 40,000. This will only increase further as auto-enrolment continues to gather momentum.

In response to this growth in the DC market there have been a number of regulatory and legislative changes made to ensure schemes are adequately monitored and that scheme members benefit from increased protection and flexibility in retirement.

DC schemes can be set up in two ways: trust based or contract based. From the employer's position, deciding which of these two approaches is the most appropriate requires careful consideration. Each option has its own merits in respect of costs, charges, regulatory requirements and governance, depending on the context of the employer. Employers need to consider their wider business objectives, as well as the needs of employees, when selecting the right type of scheme.

6.2 Contract-based v Trust-based

Ultimately both types of arrangement aim to achieve the same result – to build up a fund for scheme members which, can be used to provide retirement benefits. In the event of death before retirement, the funds can be used to provide a tax-free lump sum, subject to the limitations of the Lifetime Allowance.

Many factors can influence the structure of benefits at retirement, in particular: the level of contributions paid into the arrangement; investment fund performance; expenses deducted from the fund prior to retirement; general economic conditions at the point of retirement; and the rules of each plan.

Due to a combination of regulatory pressures (e.g. the recent introduction of a cap on Annual Management Charges, and a greater focus on governance), the growth of the Master Trust market and the similarity of services offered by providers for either option, means that the decision to go Contract-based or Trust-based is not clear cut.

Trust-based arrangements are where a board of trustees legally owns the pension funds on behalf of the members, and have a fiduciary duty to act in their interests. These can be split into:

- self-administered arrangements, using a 'third party administrator' or an 'in-house pension team';
- insured arrangements, usually using an Insurance Company;
- master Trusts, where multiple employers come together under one single trust and have all investment decisions and regulatory requirements taken on their behalf by the Master Trust.

¹⁹ The Purple Book is published annually by the Pension Protection Fund and the Pensions Regulator. It provides comprehensive data and analysis on the defined benefit pensions' landscape. The Purple Book 2013 was published on 5 November 2013: www.thepensionsregulator.gov.uk/docs/purple-book-2013.pdf

Contract-based arrangements are governed by a contract between members and the provider and can be split into:

- Stakeholder Pension Plans, introduced in 2001 by the government as a way of ensuring that all employees had the option to save for their pension over and above the state pension. These schemes were typically offered by an insurance company. These stakeholder arrangements have been superseded by auto-enrolment, but previous members may continue to contribute to these schemes. Stakeholder is a type of pension whereas Auto-enrolment is the process to get people into pensions. Employers can still add new members into stakeholder schemes. Stakeholders have a charge cap of 1.5% p.a. for the first 10 years, followed thereafter by 1% p.a. Due to the charging cap, these plans tend to have a lower range of available investment funds compared to a personal pension plan.
- Group Personal Pension Plans, which have been around prior to 1990. These tend to be the main contract based DC scheme for employers wishing to provide an attractive benefit package to their employees, using a third party provider. Market pressures have greatly reduced charges and these plans tend to offer a wide range of investment funds and member education features. Such schemes effectively outsource pension provision and the charity will therefore have little control over the running and governance of the scheme.
- Group Self-invested Personal Pensions (SIPPs) have increased in number in recent years. They give greater flexibility to members in determining how their funds are managed, but are not used as a matter of routine as corporately provided pension schemes. They tend to incur a higher level of charges due to the specialist nature of investment options available, which can include direct equity investment, commercial property and the ability to borrow money in order to make further investment.

6.3 Which scheme is right for my charity?

There is no specific formula to follow and it would be prudent for employer's to seek advice on which arrangement is best for them. Where the decision can be seen as a strategic decision for the organisation, charity trustees ought to be engaged in the process.

Generally, larger DC schemes have tended to favour trust-based arrangements. Lower fund management charges, when added to the additional fees incurred in running schemes tend to be lower than an alternative contract-based pension plan, such as a group personal pension.

For small & medium sized employers, contract-based schemes have been dominant in recent years. However, over the last few years, these trends have not been so conclusive. Some providers will offer exceptionally competitive terms for very large contract-based schemes, which can be as attractive as trust-based arrangements. Conversely, with contract-based schemes coming under increased scrutiny to increase the level of governance, we may see a swing back to trust-based schemes in the near future.

6.4 The Master Trust – a third way?

Over the last two to three years there has been a wave of enthusiasm in the pensions industry for 'Master Trust' products to satisfy employer's pension provision requirements.

The running of a trust-based pension, the burden of maintaining governance, providing various services to members and sourcing appropriate professional support for the scheme is costly. The 'unbundled' nature of these schemes means that separate costs are usually incurred for trusteeship, governance, administration, consulting services and investment management. There are additional costs to take into consideration for staff attending trustee or governance meetings and managing the risk to the charity in running its own pension scheme.

	Contract-based	Trust-based
Contractual relationship	A contract between the Provider (insurance company) and Employee. There is no relationship between the Employer & the Provider.	Established under Trust where the Employer and Trustees are party to the Trust. Scheme members are beneficiaries.
Trusteeship/ Governance	Not required. However, best practice means that establishing a Governance Committee is advisable. Formal meetings not required, but still advisable.	Trustees are required. At least one third of these should be member nominated, unless a specific exemption applies. Independent trustees can be appointed as an alternative option (but all of the trustees must be independent if there are to be no member-nominated trustees). Also required: <ul style="list-style-type: none"> • Formal minuted meetings • An internal dispute resolution procedure • A statement on investment principles • Trustee training
Scheme Accounts	Not required.	These are required to be prepared & audited annually. NB: A wholly insured scheme is exempt from this requirement.
Regulator	The Financial Conduct Authority & The Pensions Regulator.	The Pensions Regulator (to which members pay a levy).
Administration	Usually undertaken by an Insurance Company.	Undertaken by third-party or in-house team.
Tax relief eligibility	Employer contributions receive corporation tax relief. Employee contributions receive tax relief at source if paid conventionally (i.e. net of basic rate tax, with higher rate relief claimed back from HMRC). Salary sacrifice ensures tax relief on 'net pay' basis (i.e. at marginal rate).	Employer contributions receive corporation tax relief. Employee contributions receive tax relief at source where employer takes contributions from pay before deducting tax (or tax relief can be claimed back from HMRC). Salary sacrifice ensures tax relief on 'net pay' basis (i.e. at marginal rate).
Investment Funds	Usually all provider funds available – typically in excess of 60-200 funds.	These are chosen by the scheme trustees. Typically 15-20 funds are made available to members in the larger schemes.
Expenses	Fund management charges are deducted from the fund. Other services are met by employer fees.	Fund management charges are deducted from the fund. Other services met by employer fees.
Leavers	As the contract is between the Provider and an individual, there is no on-going employer responsibility.	Leaver benefits remain within the Scheme and continue to be the responsibility of Trustees.
Retirement Options	Tax free cash, annuity, flexible retirement, full encashment, small pot & trivial pension rules all available.	Tax free cash, annuity, flexible retirement, full encashment, small pot & trivial pension rules all available.

A master trust provides the trusteeship, governance, administration, consulting and investment management on a bundled-together basis. This is similar to the multi-employer schemes outlined above but in this case provides DC benefits only. With each employer having their own sub-trust within the overarching master trust, economies of scale are achieved as a 'shared' delivery of services to each of the various employers is provided. Part of the fund management charge is used to cover trusteeship, governance, administration, and consulting and investment management.

These benefits need to be considered against the potential challenges of such as scheme.

These types of arrangements are still relatively new, and charities need to consider a range of factors before entering into them, as follows:

The Pension Regulator has stated in its principles, that 'the features necessary in a scheme to deliver good outcomes for members, include features such as the provision of a suitable default fund, transparent costs and changes, protected assets and sufficient protection for members against loss of their savings'. Whether therefore, the default fund provided by a master trust is appropriate for all members, given that the membership will likely consist of employees from a number of organisations, will need to be carefully considered.

Master trusts may only be able to offer a limited potential for member engagement and consultation in running the fund; a Master trust tends to remove the employer from the burden of running the scheme. There is no requirement, therefore, for the employer to be actively involved in trusteeship or running governance committees. An employer needs to determine whether this low level of engagement is appropriate for their employees.

The employer of the charity will need to be satisfied that the potential conflict of interest between the providers providing the trust management alongside the provision of services to the scheme is adequately managed.

Generally, all types of schemes have their own merits and it is important that employers and trustees receive advice that covers all options, so that they can understand the pros and cons of each and make a very informed decision as to the right strategy going forward.

6.5 Scheme Design

6.51 Contribution levels

Contribution levels can be influenced by a number of factors and will also need to meet auto-enrolment requirements (laid out in the next section). These factors can include:

- a need to meet existing employee contractual requirements;
- to reflect contributions paid to a previous arrangement e.g. where a DB scheme has been closed to future accrual;
- employer and employee affordability;
- competing against other organisations; and
- the need to attract and retain employees.

6.52 Salary Sacrifice

The use of salary sacrifice is increasingly the norm for many employers. For those employers operating a contract-based pension, it ensures employees are able to secure tax relief at their marginal rate (in addition to national insurance tax relief). This puts contract-based pensions on a par with trust-based pension plans and generates valuable national insurance savings for employer and employee. For some employees, salary sacrifice is not appropriate (for example, if their staff are already paid a below market rate). However, salary sacrifice is so commonplace that employers who have not thought about salary sacrifice are now in the minority. Successful implementation is usually down to good communications. There are strict rules laid down by HMRC on this which charities need to be alert to. Staff presentations and clearly worded communications are essential.

6.53 Investment funds

Investment funds within trust-based and contract-based pensions usually have a default option where member contributions will be invested, unless the members select alternatives from the available funds. Usually these default funds have a 'lifestyle' approach (i.e. where investments are switched automatically and without cost, into less volatile funds as the member approaches retirement).

In recent years we have seen an increase in more specialist default funds, including blended options, target date funds and 'multi' default funds (i.e. giving the member an increased choice linked to their risk profile or appetite for socially responsible investment). This trend towards increased choice for the employee has knock on effects for the level of complexity that the employer needs to manage.

For those members wishing to invest outside of the default investment fund, a group personal pension plan tends to have a greater selection of funds to choose from. A trust-based pension may offer 10 to 20 alternative funds, all selected by the trustees. However a group personal pension can offer anything from 60 to 200+ funds, offered by a number of different investment managers, all selected by the insurance company's own internal governance team. While the move to increased choice in investments may on the face of it sound appealing, some employee groups may prefer simplicity and welcome straight-forward, accessible, investment guidance.

One forthcoming development will be the imposition of a fund management cap of 0.75% p.a. on default funds for qualifying pension schemes (i.e. those being used for auto-enrolment qualifying purposes). This is due to come in to effect in April 2015. The effect that this cap will have on the availability of choice pension plans for employers will be discussed in more detail in the next section.

6.64 Communication

Communication is becoming increasingly more important. As an increased range of retirement options become available communication becomes key. However this emphasis is not high amongst the charity sector according to CFG's DC survey. Almost 60% of respondents provided no support for members to source the best deal at retirement.

During the 2014 Budget announcement the Chancellor stated the requirement for providing guidance to all retirees at retirement. There is an expectation that employers and trustees will have to provide increased levels of information to members in order for them to make fully informed decisions at retirement. There is a range of ways of communicating the scheme to members on joining and during their on-going membership.

Having clear paper-based communications (in plain English) must be a standard. Increasingly, staff presentations and generic 1-1 advice is offered. In some cases, the use of technology, including internet-based services, SMS text messaging and emails have proven to be valuable channels for conducting this communication and for easily providing a two-way feedback loop.

6.7 Governance of DC schemes

Trust-based pension plans benefit from having trustees monitoring the scheme and there is substantial guidance and regulation in place. However, contract-based pension plans are not supervised by trustees. Instead some employers have established a Governance Committee to monitor the pension plan. To assist these employers, the Pension Regulator published a paper in July 2013 designed to provide guidance on how to effectively monitor a contract-based pension plan. The paper helps governance committees understand issues including:

- early identification of administration problems;
- better value for money;
- improved employee engagement and awareness of employer contributions;
- improved member understanding of their retirement savings; and
- fewer member complaints.

For the committee to be successful, it needs clear responsibilities, objectives, and authorities and to be measured against those.

In November 2013, The Pension Regulator published their Code of Practice: Governance and administration of occupational Defined Contribution trust-based pension schemes²⁰.

This code of practice sets out the legal requirements and standards of governance and administration that trustees of occupational DC trust-based schemes need to attain. The Code introduced 6 'principles' and 31 'quality measures', which trustees have to demonstrate they are meeting.

²⁰ The Pension Regulator: Code of Practice: Governance and administration of occupational Defined Contribution trust-based pension schemes. www.thepensionsregulator.gov.uk/codes/code-governance-administration-occupational-dc-trust-based-schemes.aspx

Any organisation running a DC scheme should be familiar with The Pensions Regulator's papers of July and November 2013. Advisers are expected to have commented on both items and made sure appropriate advice is provided accordingly.

Good governance of DC schemes needs to move beyond short-term tactical issues, such as changes in legislation. Charities need to develop a strategy for DC schemes founded on clear objectives that support the overarching strategy of the organisation. It is therefore important for governance committees to be given absolute clarity on the purpose of providing a pension package and how this fits within the overall reward strategy. On an operational level, the committee needs to ensure that the people and processes support high quality service delivery to the employee and day-to-day risks are being proactively managed.

Worryingly CFG's DC survey indicated the governance of DC schemes is not high on the agenda for charities. 21% of respondents reported that they review their investment strategies and aims of the default investment option annually. 20% said they review this every two to three years. Almost 50% of respondents confirmed that they do not review this at all. Charities should have a better understanding of the governance and running structures of their DC pension schemes.

6.8 Other Pension reforms

The Queen's Speech in June 2014 introduced the Private Pensions Bill (following on from Budget announcements), which set out new ways of saving for a pension using the so called 'Dutch style pension schemes', 'Collective Defined Contribution schemes' or 'Defined Ambition Schemes'.

Previously, members decided on whether to draw their 'pension commencement lump sum' (tax free cash) and then consider whether they wished to use the balance of the fund to purchase an annuity or move into flexible retirement (drawdown or phased retirement).

Under 'capped drawdown', members must withdraw a regular taxable income from their pension fund which must fall within a minimum and maximum limit imposed by the Government Actuarial Department. An alternative to capped drawdown was 'flexible drawdown'; under this members could fully encash their pension fund, subject to income tax. This option was only available to those who could demonstrate they had £20,000 p.a. of secured income (e.g. through a combination of state and company pensions).

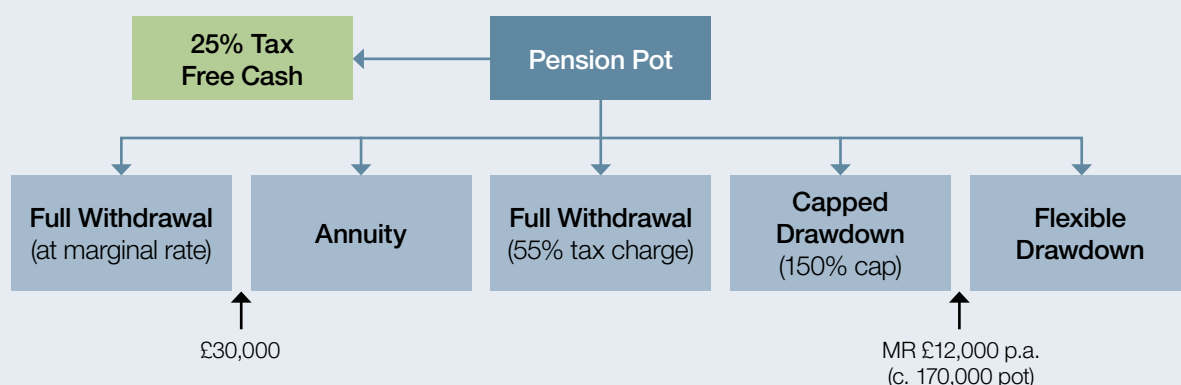
There were additional options related to 'small pots' of up to £2,000 or 'trivial pension' of up to £18,000 where members could fully encash their funds, subject to meeting certain rules and the payment of tax.

The perceived unfairness and complexity of retirement options led to the Chancellor proposing a new set of transitional rules for 2014/15 and then, subject to consultation, even wider changes for 2015/16, set out below.

The diagram below shows retirement options for DC scheme members, for the 2014/15 year only.

Trivial pension rules now have a limit of £30,000 and small pot provision has increased to £10,000. Those individuals reaching retirement with a lower value in their pension fund and who might have previously struggled to find an annuity provider are being given a possibly more attractive option to consider.

Retirement options for 2014/15 tax year



Case Study 5: DC Design

Kevin Barnes, Finance Director at Barnardo's tells us about their approach to designing a DC scheme in the wake of auto-enrolment.

Getting DC scheme design right can be a key factor in attracting, retaining and rewarding staff, particularly if you need to recruit workers from the public sector. Barnardo's has had two attempts at this, the first when first setting up a DC scheme and then during a regular review six years later. The latter coincided with needing to be prepared for an influx of members as we approached auto-enrolment.

We couldn't afford higher contributions so had to make sure contributions work as hard as possible for members. Key to our design was in securing:

- 1) a low Annual Management Charge for contributing and non-contributing members (there can often be a steep increase in fees when contributions cease);
- 2) a wide range of investment options to suit all types of investor;
- 3) clear communications and member tools from the provider; and
- 4) salary sacrifice to make contributions free from national insurance as well as tax; thereby reducing the cost of contributions for employees and Barnardo's.

Tender

When undertaking the review we went to tender, inviting eight potential providers to quote. Of these only three providers responded due to the average salaries and level of staff turnover being less attractive than many private sector employers. We considered and rejected the use of 'NEST' as we wanted to offer all staff the same pension scheme.

Contribution levels

We also wanted to avoid having to explain to auto-enrolled members that contributions will increase over the next few years. To avoid this, we took the decision to commence with employee contributions of four percent, matched by Barnardo's. There is an option to increase either to six per-cent or for the employee to pay more, with Barnardo's contribution limited to six percent. We would like to offer more but have to consider what is affordable now and in the future.

Communications

We know that many members find pensions confusing. Good design can ensure the pension scheme is right for most but it is difficult to ensure that one scheme is right for all employees. 'Lifestyling' can help as it reduces risk in the scheme gradually, increasingly over a very long glide path. Our scheme includes a 15 year reduction in risk taken, assuming members do retire when they tell us they will or we expect them to. Communication with and from members is key to get these decisions right for members, and the pension provider can take the lead here.

Governance

We have created a 'stakeholder committee' to ensure the scheme is well run, kept under review and holds Barnardo's and our pension provider to account including for the performance of the default funds, even for the tracker funds. The committee is also the place where we can consider member feedback, complaint handling and developments in pension legislation. Membership of the Committee includes representation from two members and our recognised trade union.

For those who wish to consider flexible drawdown, the minimum level of secured income was reduced from £20,000 p.a. to £12,000 (broadly equivalent to having a pension fund of £170,000).

The option to simply encash the whole pension fund, subject to a 55% tax charge, remains in place.

From April 2015, the changes are even more radical; they act to simplify the number of options available at retirement. These are detailed in the diagram at the bottom of this page.

Members can still draw 25% of their fund as a pension commencement lump sum. There are three options available for the remaining balance in the member's pension fund:

- 1) the fund can be used to buy an annuity; or
- 2) the fund can simply be fully encashed, subject to an income tax charge; or
- 3) the fund can be moved into flexible drawdown (this final option allows withdrawals of any amount, including full encashment).

The ease with which large sums can now be withdrawn at any one time, has caused some to express concern over members capability to be able to make informed financial decisions for their retirement. This has further enhanced attention on the importance of member education; with government committing, in principle, to accessible independent advice for all retirees. The details of this are still being consulted on; in particular with regards to where the burden of responsibility will fall for providing this resource. Ultimately, there is an expectation that employers will play some part in educating their employees. The Pensions Regulator refers to this in Principle 6 within their Code of Practice: Governance and administration of occupational Defined Contribution trust-based pension schemes.

6.9 Making education work

There are many options which can be considered by employers. Fundamentally, good member communications will ensure clear non-jargon related statements at retirement, detailing member options.

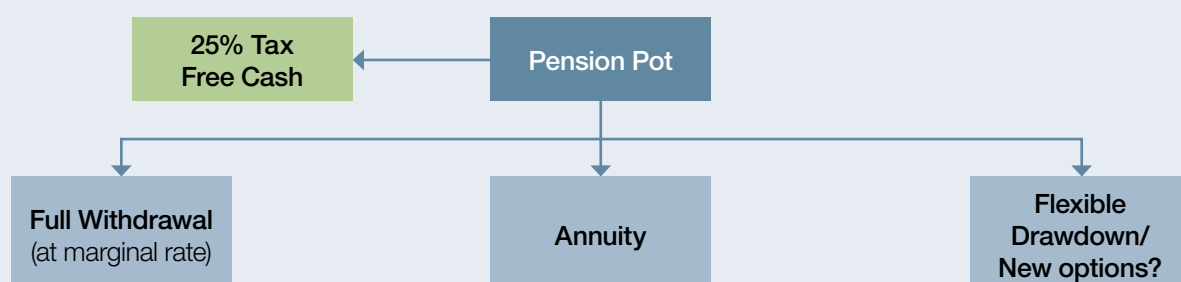
Options which should be considered include:

- financial awareness seminars in the lead up to retirement;
- member specific advice at retirement, provided by independent financial advisers;
- providing access to educational web-based material that clearly details the member options and provides assistance in connection with annuities, especially impaired life / enhanced annuities.

6.10 The Outlook

Regardless of legislative and regulatory pressures, the outlook for DC schemes remains very positive. The schemes provide certainty in terms of employer costs and are a long way from the dangers associated with DB schemes.

Retirement options for 2015/16



Section 7

Auto-enrolment



Arguably, auto-enrolment has been the biggest issue facing employers over the last few years. The biggest impact has been the costs associated with implementing auto-enrolment requirements and making contributions for previously non-pensioned employees.

In October 2012, the Government introduced 'work place pensions' which is now more commonly referred to as 'auto-enrolment'. This pension legislation obliges employers to automatically enrol 'eligible' employees into a workplace pension scheme. This will mean making contributions to the retirement savings for the majority of their workforce. All employers have been given a date by which they have to comply (known as their 'staging date'), starting with the largest employers first and ending with the smallest 'micro' employers in 2017. The staging of employers in this way was designed to ensure that the introduction of auto-enrolment can be managed by employers, the government and the pensions industry. There are a huge number of smaller organisations yet to complete the process. By the time this publication goes to print less than 1000 charities (~945) will have auto-enrolled. By early 2015 a further 3,238 charities will auto-enrol. But the vast majority of charities (approximately 22,000 of them) are only due to auto-enrol in 2016 and 2017. This means that we will not realise the full impact of auto-enrolment on the charity sector until two years' time.

Government introduced auto-enrolment, as the first of many steps intended to tackle the economic impact of impending demographic changes to the UK population. The result of this is claimed to both encourage a positive cultural shift in attitudes towards saving for retirement and ensure that there are provisions in place to pick up the future cost of retirees.

Auto-enrolment shifts the onus of pension provision squarely upon the employer for the first time. This poses a new set of challenges for charities, many of which are still struggling with the impact of a difficult economic environment.

In order to support charities with the challenges posed by auto-enrolment, CFG produced a best practice guide in November 2013 in collaboration with Foster Denovo, Premier Pensions and Stephenson Harwood.

The following sections will look at the impact that auto-enrolment will have on charities over the next few years, and a look at the impact of the auto-enrolment program thus far.

7.1 The story so far

Auto-enrolment had been successful in introducing an extra 3 million people to saving for their retirement. Initial findings show that opt-out rates amongst employers who have staged are considerably lower than many had anticipated they would be. Opt-out rates for the scheme stand at approximately 9%. Government had originally projected opt out rates of 30% for the lifetime of the scheme. Stronger than expected take-up figures for the phases covering the largest employers caused them to revise down this projection to 15% for the lifetime of the scheme. It is not clear whether this trend will continue. Some believe that the opt-out rate will increase as employees have to increase their pension contributions in 2017 and 2018 in order to meet the Government's minimum contribution levels by 1st October 2018.

²¹ CFG's best practice guide, auto-enrolment for charities, November 2013: www.cfg.org.uk/resources/Publications/-/media/Files/Resources/CFDG%20Publications/Auto_EnrolmentPublication.pdf

²² Large employer research into opt-out rates August 2013: www.gov.uk/government/uploads/system/uploads/attachment_data/file/227039/opt-out-research-large-employers-ad_hoc.pdf

7.2 Changes to pensions announced by DWP

In March 2014, the Department of Work and Pensions (DWP) announced a series of changes to pensions to ensure that charges provide scheme members value for money. The details are as follows:

- from April 2015 a 0.75% cap on charges will be introduced for the default funds of all qualifying pension schemes;
- the government has also set out equivalent caps for schemes with combination charge structures;
- three different categories of pension charge will be banned altogether: payments for sales commission which are deducted from members' pensions; increases to charges when people are no longer employed by a company but leave money in the company's pension scheme (also known as an 'Active Member Discounts'); 'consultancy charges' where members have to pay for advice given to their employer.

In addition there will be new rules to ensure that all 'transaction' costs in pension schemes are published transparently.

This will impact organisations that have already staged. They may find that their providers wish to review their existing pension arrangements, in light of the effect that the charging provisions will have on the affordability of these arrangements. When selecting or reviewing pension scheme arrangements for auto-enrolment, employers need to take the recent DWP announcements into account.

7.3 Pension scheme selection

The assumption by many charities that they will be able to use their current provider needs to be challenged. Our survey suggested that 70% anticipate that they will use their current DC scheme for auto-enrolment. The cap on annual management charges may result in pension providers being more selective over the schemes they offer. Some charities, for example those with high staff turnover, low paid staff or high numbers of casual and bank staff, may find that mainstream pension providers will no longer offer them terms. The advice here is to consider your pension arrangements early on in your auto-enrolment planning.

NEST (National Employer Savings Trust), a not-for-profit organisation that was set up to provide a guaranteed pension scheme for UK workers who had previously been 'effectively locked out' of retirement savings in alignment with the introduction of auto-enrolment. 1 million people have already started saving with NEST, with opt-out figures below the market average at 7%.

53% of schemes used by CFG survey respondents have an annual management charge of greater than .5% and a worrying 40% say they don't know what their management charges are. There is a risk therefore, that members will be auto-enrolled into poor value schemes if these figures aren't challenged.

Our auto-enrolment survey suggested that less than 7% intended to use NEST for auto-enrolling their employees. However, in practice, many charities have discovered on review that their current DC pension provider is either not suitable for mass enrolment, or is unwilling to provide it to existing clients for auto-enrolment. We expect that over the lifespan of auto-enrolment, more charities will be using NEST or other low cost providers.

All employers are entitled to use NEST, although this may not be the most appropriate solution for everyone. It may also be worth considering other low-cost options as there are several potential providers to choose from.

7.4 Awareness of auto-enrolment among charities, and confidence in capacity to implement it appears to be relatively high.

Overall 76% of respondents said they were confident or very confident in their capacity to implement it. Of those auto-enrolling in 2014, confidence was at 84%. For smaller charities auto-enrolling in 2015, 16 and 17 this was still high at 63%.

Based on the feedback CFG has received from those charities that have already auto-enrolled, we would question whether some charities have underestimated the scale of the task at hand.

7.5 Auto-enrolment in the long term?

Currently auto-enrolment rules will increase employer contributions from 1% to 3% by 2018.

Most people expect this to increase further. In Australia, auto-enrolment has existed for 20 years. Employers went from paying contributions of 3% to 9% p.a. within the first 10 years of auto-enrolment. Employers will be picking up a 12% p.a. contribution rate within the next 5 years. In the long term, we should not be surprised if we see 'auto-enrolment stage 2' where increased levels of contributions are required.

Section 8

Contracting, Outsourcing and Restructuring



This section deals with operational issues that arise when a charity seeks to take on contracts for any employees who already carry out service for another employer, and the challenges that can arise when charities seek to restructure in order to meet external challenges. This section outlines the highly complicated set of considerations that need to be taken into account when entering in contracting arrangements. The complexity of the various legislative frameworks and operational demands may leave those new to contracting somewhat perplexed. There is a need for careful due diligence in advance of entering such arrangements. Ensure adequate advice is sought.

8.1 Contracting and Outsourcing

Charities are said to be an integral part of service delivery for the public sector. As a result, charities are looking to tender for public contracts where they feel they can add value and fulfil their charitable objectives.

A charity undertaking a new stream of work and employing new staff has relatively straightforward pension obligations. The charity only needs to ensure that the new staff has access to appropriate pension provision, in line with the charity's people strategy. On the other hand, if the contract relates to public services already being delivered, and there is a transfer of staff to the charity as a part of the outsourcing arrangements, the pension challenges can be highly complex. Such arrangements can involve a transfer of risk over and above the obligation to provide the employees with a pension scheme for the period of the contract.

For example, the Local Government Pension Scheme (LGPS) does not recognise multiple employers relating to specific periods of service for an employee, so all past liabilities are transferred to the newest employer. If a charity takes on an employee who is a member of the LGPS with say, twenty years' service, if there is a deficit when their contract ends, the charity is not only liable for the deficit that is a result of the employee's time with the charity, but also the previous twenty years of service. Clearly this can lead to highly onerous and punitive payments at the end of a contract.

8.2 Employees

Under contracting arrangements, where staff are being transferred to a new employer that transfer is likely to be governed by the TUPE legislation. TUPE operates to preserve employees' rights when the organisation or service they work for transfers to a new employer. From an employment law perspective, a critical question is whether or not a particular outsourcing is within the scope of TUPE, it should not always be taken as granted, and will not always be transparent. Legal advice to transferor and transferee may legitimately differ. Whether you are an employer who is transferring staff or you are assuming the function and will be receiving an influx of new staff that currently carry out the function, there are various statutory obligations you need to manage and factor into any timetable and you will need to ensure that you have appropriate HR and legal advice.

²³ TUPE refers to the 'Transfer of Undertakings (Protection of Employment) Regulations 2006' as amended by the 'Collective Redundancies and Transfer of Undertakings (Protection of Employment) (Amendment) Regulations 2014'. The TUPE rules apply to organisations of all sizes and protect employees' rights when the organisation or service they work for transfers to a new employer. www.acas.org.uk/index.aspx?articleid=1655

²⁴ For example, you may have ended the provision of services to another entity or you may yourself have outsourced functions.

TUPE

Charities are more and more involved in taking on services, which have traditionally been managed in the public sector. It is important therefore, that charities understand the rules around TUPE and take advice where necessary.

The purpose of TUPE is to protect employees' employment when the business in which they work, or the services they are providing, are transferred from one entity to another. It can apply where there is a transfer of an undertaking, business, or part of an undertaking or business, or where there is a service provision change.

TUPE generally prohibits rights relating to an occupational pension scheme from transferring. However, where an employee has pension rights relating to their employment (e.g. those rights to early retirement, or enhancements, which are contingent on dismissal) do follow with the transfer of employment. These rights are known as Beckmann liabilities, after Beckmann and Martin case law.

The nuances around these rights are complex; a charity should seek protection when receiving staff under TUPE. Beckmann issues should be a particular concern in relation to public sector outsourcing. Many of public sector scheme arrangements provide for enhanced benefits paid on occasions that may fall within the context of TUPE .

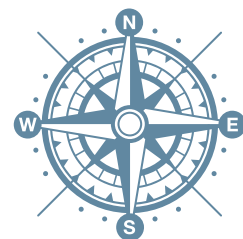
In addition, pensions legislation provides that certain minimum pension benefits have to be provided in the event of a TUPE transfer. There is no obligation to replicate an existing occupational pension scheme. Instead a receiving employer may, depending upon the pension benefit package previously enjoyed by the transferring individual, be required to put protection measures into place. There are various options available; this is what is known as the 'matching up to 6%' (of the employee's basic pay) obligation. It is common for a DC scheme to be utilised to satisfy this requirement, with contributions up to 6%.

In addition, there are now general obligations in relation to the need for an employer to auto-enrol its employees.

8.3 Extra provisions

Transfers from the public sector involve more onerous provisions dealing with historic public sector employees who will transfer along with the function. These provisions will generally apply regardless of whether from a strict legal perspective, TUPE would actually apply in the individual case in question. These additional obligations are generally imposed through contract law. The scope for negotiation on obligations not determined by TUPE will depend on the Contracting Authority's own policies. As these are not statutory standards, there may be some room for negotiation. In practice, this is rare and difficult to achieve since the contracting authority is generally following government policy.

For taking on contracts in the public sector, charities need a good understanding of the relevant regulatory frameworks, such as 'Fair Deal' and 'best value authorities', as well as specific tendering processes and conditions for bodies such as the NHS and DWP. There is a huge amount of detail that can trap the unwary and is beyond the scope of this publication.



8.4 Controlling Risks within your organisation

Control becomes particularly important for a charity that relies heavily upon 'winning' new sources of income and actively pursues outsourcing or partnering opportunities. Pension risk and liabilities can be long term and easy to discount or overlook in pursuit of getting the new contract although the pension liability itself could dwarf any gain and on worse case endanger the future viability of the organisation.

It is often the business development function of a charity that leads on the acquisition and negotiation of new contracts. It is vital, in managing pension risks that the teams involved have an appreciation of the potential risks posed by pension obligations under the contract. It is imperative that the charity appoints a single team or person who has the responsibility for the pensions aspect of the contract negotiations, and who has to be satisfied that the risk presented by the contract fall within the charities risk appetite. This avoids the danger of pension issues falling through the gaps between business development, finance and HR. However all teams must have an awareness of the risks from their own area of expertise.

Whatever agreement is reached it is important to retain the key documentation. This goes wider than the contract and should include specific correspondence dealing with pensions and risk sharing, original tender documentation and responses to queries, actuarial letters and the like. These may be needed some time in the future and retention policy should ensure these are kept centrally.

8.5 Organisational and Structural Change

Restructuring gives rise to a number of legal issues, particularly around employment. In addition organisations may find that as a result of restructure, they have accidentally crystallised substantial liabilities relating to their pension schemes. Wider discussions on multi-employer schemes and cessation events triggered by restructure can be found in Section 5.

It is important to remember that a debt may arise due to a direct legislative trigger such as an employment cessation event. It may also arise through the operation of the pension scheme's own trust powers which may in turn lead to a debt under legislation. Therefore, it is important to consider both the risks under statute directly and the risks under the pension scheme governing documentation.

The position also differs on whether or not the employer is part of a multi-employer pension scheme or whether it is the sole employer in a pension scheme. For example, employers in the Growth Plan or Social Housing Pension Scheme and parts of the Pensions Trust will be in a multi-employer scheme. Some employers may have their own bespoke pension scheme for which they are the only employer²⁵.

²⁵ But beware legacy employers who may have participated in the past, unless historic employers exited correctly they may still be technically liable to the pension scheme and deemed to be a 'statutory employer' (see below for more information).

8.6 Moral Hazard

The complex system of transfer of liabilities raises the possibility that an employer seeks to avoid liabilities by transferring pension liabilities to a new entity which is not financially able to meet its commitments, or by shifting assets between companies. In pension law, this is known as 'moral hazard' and is covered by anti-avoidance regulation.

If a pension scheme does not have the assets to meet its liabilities and the employer is 'insufficiently resourced' but there are others in the group that do have sufficient resources, although they are not technically legally liable, the Pensions Regulator has the powers to compel other entities to put support in place or even inject funding into the pension scheme.

The powers are aimed at the unscrupulous. However the exercise of these powers can also arise in other general circumstances such as strategic change. In addition to a corporate entity, directors can, but rarely, face personal liability.

The types of events where the Regulator may need to get involved are broad. The Regulator will be concerned if the assets available to support the scheme are reduced. This could include making a large donation or capital project, extending a loan to another group, or a sale of assets at an unvalued rate. The Pension Regulator will focus on whether there is a weakening in the employer covenant and on the obligations owed by the employer to the scheme. Some scenarios, such as the giving of priority to a creditor, are not directly related to the scheme, but could pose a threat to member's interests. Decision makers will need to assess their actions and the potential impact on their pension scheme.

There is a statutory defence to a claim if it can be shown that the recipient of a claim considered the potential effect on the scheme, took all reasonable steps to eliminate or minimise any potential detriment, and that it was reasonable to conclude that the act would not be materially detrimental to the pension scheme. It is important therefore that decision makers carefully document decisions and the reasons behind them, to show they have reached their conclusions in the correct manner. Section 3 on governance and trustee relationships is of relevance.

Employers seeking reassurance that an event in contemplation will not be caught by the Regulator's powers (or at least will not be subject to investigation) may apply for clearance from the Regulator. Under this process, employers provide the Regulator with the information relating to the proposed event. The Regulator will then be able to tell the employer whether, on the basis of the information given, the moral hazard powers will be used.

Section 9

Accounting for pensions

9.1 Introduction

Since the introduction of FRS 17 on 1st April 2005 many charities have learnt to live with including the valuation of a pension deficit as a liability on their balance sheet and the volatility of the valuation from year to year. Few finance professionals, however are able to confidently explain these movements from year to year. This lack of understanding of the numbers is exacerbated by the fact that pension scheme trustees use a different valuation methodology for arriving at the pension liability figure for scheme funding purposes.

The pension scheme valuation is of more commercial relevance since it sets the benchmark for the funding requirement of the scheme, which the charity will need to meet from its cash-flow. The FRS 17 valuation is largely an accounting estimate which only has commercial relevance for readers of the accounts who wish to assess the financial strength of the organisation; it does also have an impact on distributable reserves in companies limited by shares that wish to pay dividends.



The FRS 102 definitions of pension schemes are very similar to the ones previously used; schemes will continue to be classified as DC or DB. However, where charities have taken advantage of an exemption to account for any liability in respect of their membership of one or more multi-employer schemes, this will no longer be possible.

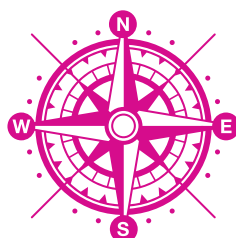


Some charities are learning to live with a liability that reduces their net assets to near zero or below. Recognising the challenges of adopting FRS 17, the Charity Commission produced guidance on pension scheme reporting and the impact of pension scheme deficits on charity reserves in their publication 'Charity reserves and Defined Benefit pension schemes'. This was helpful in focusing in on the issue as being one of liquidity (cash flow) when considering a charity's going concern status, rather than the absolute value of their net assets, or in some cases, net liabilities.

9.2 Charities SORP 2015

A new charities SORP (the SORP) comes into effect for accounting periods on or after January 1st 2015. The SORP will appear as two versions; one for smaller entities (based of the Financial Reporting Standard for Smaller Entities – FRSSE) and one based on FRS 102. These SORPs will include changes as a result of adopting FRS 102, 'The Financial Reporting Standard applicable in the UK and Republic of Ireland'. Whilst the FRSSE SORP may offer the benefit of limited disclosures in respect of pension liabilities it should be noted that the FRSSE is likely to be updated within 12 months of publication.

The FRS 102 SORP disclosures are largely comparable for a pension scheme under FRS 17. Charities will need to account for a liability equivalent to the net present value of future deficit recovery payments. This is discussed below.





9.3 Defined Contribution Schemes

DC schemes are relatively straightforward in accounting terms, as the employer's pension contributions are recognised as an expense using the accruals basis of accounting. The accounts of the charity will include the employer contributions payable in the period to DC schemes within the gross payroll costs within the total wages and salaries figure (included in the SOFA and disclosed separately in the notes to the accounts).

Disclosure requirements under current UK GAAP and FRS 102 include the requirement to provide information on:

- the nature of the scheme;
- the pension costs for the year;
- pre-paid and outstanding pension contributions at the balance sheet date.

The introduction of FRS 102 will have very little impact on the reporting of DC schemes in charity accounts. A minor change is that FRS 102 notes that a prepayment of contributions to a DC scheme can only be recognised in the financial statements if the prepayment will lead to a reduction in future payments or in a situation where a cash refund can be obtained. Similarly, where payments to a DC scheme have been lower than the contributions due for the year, under FRS 102 the outstanding liability must be discounted (assuming the effect of this is material) if it is not expected that the contributions will be paid over within 12 months.

9.4 Defined Benefit Schemes

There are many more extensive disclosures relating to DB pension schemes which are required in the financial statements. As with accounting for DC schemes, the accounts must reflect the costs of employing staff and providing retirement benefits. The costs include those expenses included within wages and salaries as current service costs of employment and also actuarial gains or losses on the DB pension scheme. These actuarial movements should be disclosed separately on the face of the SOFA after the net income/expenditure for the year and before the net movement in funds. The DB pension scheme asset or liability must be shown separately on the face of the balance sheet.

Under both FRS 17 and the FRSSE, the assets and liabilities of the pension scheme require a valuation to be prepared by a qualified actuary appointed by the sponsoring employer each year. The pension scheme assets are valued at fair value and pension scheme liabilities are measured using an actuarial basis for both the benefits promised by the scheme and the constructive obligations. There is scope to influence the valuation through the actuarial assumptions that are used. Even a small change in assumptions can significantly affect the reported scheme net asset or liability value.

The FRS 17 valuation is undertaken by a professionally qualified actuary appointed by the charity who should normally be independent of the pension scheme actuary using the relevant actuarial guidance notes. Whilst a full FRS 17 valuation need only be undertaken at intervals not exceeding three years, in practice, because most charities accounts are required to reflect changing conditions and asset values, the valuation is usually undertaken more frequently (on an annual basis). The FRS 17 valuation methodology has led to significant volatility in charities net asset values. Explaining this, and how the funding valuation used by the Pension Scheme trustees differs, has proven problematic for many finance professionals.

FRS 102 broadly follows the same principles as current FRS 17 when accounting for Defined Benefit schemes. However FRS 102 does not require the use of an independent actuary to calculate the Defined Benefit obligation and it does not specify the frequency against which a full valuation is required to be undertaken. It does however require a rigorous evaluation to be undertaken, therefore it is important for charity Trustees to undertake these at an early stage and determine if their charity is able to dispense with any professional actuarial valuations for accounting purposes. Given the size of the majority of charities, it is unlikely that many, if any, will have the necessary expertise to undertake this exercise in house.

There are changes to the valuation methodology that are beyond the scope of this publication. Charities need to ensure that they have adequate advice to understand how these may impact on their specific circumstances.

It should be noted for those charities with trading subsidiaries that incur tax, and have deferred tax, that under FRS 102, for Defined Benefit schemes, any resulting deferred tax is no longer set off against the pension scheme liability/asset. This 'netting off' was specifically required under FRS 17.

The conditions to recognise a pension scheme asset remains the same under FRS 102 valuations.

9.5 Accounting for Pension Scheme Deficits

Where the Defined Benefit pension scheme is in deficit, the full liability is reflected in the balance sheet as a pension scheme liability, unless the particular opt-outs applying to some multi-employer schemes apply. Details of the pension scheme deficit liability shown on the balance sheet and the deficit recovery plan must be disclosed in the Trustees' Annual Report.

The Charity Commission has issued guidance on pension scheme deficits and the impact on going concern²⁶. Where the pension scheme liability, calculated under current UK GAAP, exceeds the amount of the unrestricted funds of the charity, this is not to be automatically interpreted as creating a state of insolvency in the charity and highlighting going concern implications. While a shortfall will be a trigger for a detailed review of the charity's cash flow, it may not automatically signal major problems that could ultimately lead to the closure of the charity.

Many charities have adopted the practice of showing their reserves both before and after the pension liability as a way of demonstrating to readers of the accounts the short term asset position of the organisation.

²⁶ *Charity Reserves and Defined Benefit Pension Schemes: www.charitycommission.gov.uk/detailed-guidance/money-and-accounts/charity-reserves-and-defined-benefit-pension-schemes/*

9.6 Multi-employer Schemes

Prior to the latest charities SORP, where it was not possible to separately identify and to use Defined Benefit accounting for a multi-employer plan, the charity had to account for this as if it were a Defined Contribution plan, and make additional disclosures in the accounts, including information on how the liability has been determined. As a result contributions falling due in the accounting period were accounted for and disclosed (along with any comparatives for the previous year), with no balance sheet entry required to show an effective deficit position, should one exist.

Now in most cases where a charity participates in a multi-employer DB scheme, and the charity has entered into an agreement that sets out a schedule of contributions to fund any deficit, the charity shall recognise the net present value of the contributions payable and the resulting expense in the SOFA. This will have a significant impact on the balance sheets of many charities. Any deficit can only be excluded from the balance sheet if either an employer is unable to identify its share of the assets and liabilities or if the FRSSE continues to be applied. If the former applies the charity still needs to account for their recovery plan commitment.

Whilst the above outlines the generality of the requirements for appropriate accounting treatment the characteristics of individual pension schemes will need to be considered on a case-by-case basis.

9.7 Disclosure of pension costs of senior employees of the charity

The charity SORP requires disclosure in the notes to the financial statements of details of staff earning more than £60,000, being disclosed in bands of £10,000. Remuneration takes into account all emoluments. Pension contributions by the charity in respect of such individuals are not disclosed as a part of this figure of aggregate remuneration. The new SORP now requires this for all charities, not just those over an income threshold.

The disclosure of contributions to Defined Contribution schemes gives an indication of the benefit to the charity employee. The disclosure of the contributions to a Defined Benefit scheme does not provide an indication, as the level of funding is dependent on whether the scheme is in deficit or surplus. As a result, the pension details required to be disclosed for these higher paid staff participating in a Defined Benefit scheme are only the numbers to whom the benefits accrue and the nature of the scheme.

Acknowledgments

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We are proud of longstanding relationship with both ACEVO and CFG which have helped us to understand the unique challenges that charity employers face.

We recognise that auto-enrolment presents a number of challenges to Charity employers at a time when their budgets and resources are already stretched. Our unique auto-enrolment process is designed to help organisations fulfil their employer duties in a cost-effective and compliant way.



Premier is an award winning, nationwide provider of employee benefits and financial services. Our clients come from all backgrounds and industry sectors.

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Spence & Partners is a firm of actuaries that provide specialist pension support to third sector organisations. Director and company owner, David Davison, leads the Public Sector, Charities and Not for Profit pensions practice, heading an experienced team familiar with the issues charities face and with access to the modeling tools and communications skills necessary to guide Boards through a variety of solutions.

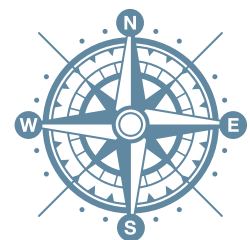
Spence can provide actuarial and administrative services for pension schemes and specialist services for the charity sector including advice for participants in multi-employer schemes such as Pension Trust & Local Government Schemes, local authority outsourcing, pension accounting, auto-enrolment and pension implications of organisational restructures.

Reviewers



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Peter Askins, Director of Independent Trustee Services Limited



Contributors



Pinsent Masons is an international law firm with the UK's largest pensions law team. We are passionate about advising pension schemes, and those who support them, in dealing with the challenges that arise and achieving exemplary governance standards. By putting our clients at the centre of our business and simplifying the way we guide them through an increasingly complex world, we are committed to becoming the pensions team of choice. To find out more about how our specialist charity sector team can help you, please contact: Nick Stones, nick.stones@pinsentmasons.com 0121 623 8600



MHA MacIntyre Hudson is a top 20 firm of Chartered Accountants, offering a wide range of services including assurance, advisory, consultancy and training. We were awarded National Firm of the Year at the 2013 Accountancy Age awards. Our dedicated not for Profit sector team acts for over 500 charities and has been ranked in the Top 5 of the Charity Finance audit survey for the last 6 years. This long term experience and specialist knowledge of the sector enables us to identify practical and pragmatic solutions for our Not for Profit clients, whilst also ensuring client service excellence.



LCP helps charity and not for profit organisations deliver their charitable objectives by giving them focused pensions and investment advice, supported by considerable sector experience. We help our clients to quickly understand the difficult pensions issues which they face, so that they can manage their defined benefit pension liabilities, reduce their risks and confidently plan ahead. We have particular experience in advising employers on their involvement with the Pensions Trust's arrangements. Our charity clients include Barnardo's, Cancer Research UK, Christian Aid and Scope.



Stephenson Harwood has provided specialist pensions legal advice to not-for-profit and corporate organisations and trustees for over 30 years and is acknowledged in Legal 500 and Chambers & Partners as a leading pensions law firm. It comprises 110 partners and over 600 staff and has specialists capable of dealing with virtually every commercial issue affecting any organisation. The Stephenson Harwood pensions team is one of the larger city based pension teams.



PTL (Pitmans Trustees Limited) is an award-winning provider of governance services to trusts across the UK.

Much of our work is in the pensions arena, where we represent more than 200 schemes ranging in size and type. Whether we act as trustee, secretary or adviser, we bring a professional, pragmatic and personable approach to deliver real value and practical solutions – in an increasingly challenging environment.

PTL was founded in 1994 and has offices in London, Reading, Birmingham and Leeds. Over the years we have helped numerous charities to enhance governance, reduce risk and manage their pension schemes more efficiently.



Hymans Robertson is an award-winning actuarial consultancy that delivers a full range of services including actuarial, enterprise risk management, third party administration, investment and communications consulting, founded in 1921. We're an independent UK firm and our client base includes FTSE 100, privately owned firms, not-for-profit organisations and public sector pensions. Charitable services are an important element of our work and we support organisations such as St Vincent's Hospice and Glasgow City Mission. Plus, some of our partners recently raised £125,000 for Hospice Association of Scotland, Maggie's Centres, Carers' Trust and Education for All when they cycled from London to Marrakech.

CFG wishes to give a special acknowledgment to Sarah Woodfield (CFG policy team) and John Tranter (Chair, steering group) for the significant work that has gone into producing this publication

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