Title: Requirements for Defined Benefit pension scheme trustee boards to appoint a Chair and to regularly prepare, review and submit a statement on their scheme funding and investment strategy to TPR with their actuarial valuation. **IA No**: **DWP-003-2019** **RPC Reference No: RPC-4339(1)-DWP** **Lead department or agency:** DWP **Other departments or agencies**: n/a	**Impact Assessment (IA)** **Date: 05/02/2019** **Stage:** Development/Options **Source of intervention:** Domestic **Type of measure:** Primary legislation **Contact for enquiries:** DWP eleanor.king1@dwp.gsi.gov.uk ivor.millen@dwp.gsi.gov.uk
Summary: Intervention and Options	**RPC Opinion: Green**

Cost of Preferred (or more likely) Option (in 2016 prices)			
Total Net Present Social Value	**Business Net Present Value**	**Net cost to business per year**	**Business Impact Target Status**
£ -148.9m	£-148.9m	£17.3m	Qualifying provision

What is the problem under consideration? Why is government intervention necessary?

The Green Paper consultation[1] and subsequent White Paper[2], on defined benefit pension schemes identified concerns about a lack of accountability and clarity on what is a good funding strategy. This can result in poor scheme funding and investment decision-making sometimes focused on the short term i.e. the next funding valuation due to be submitted to The Pensions Regulator (TPR).

The current legislative framework is supported by (non-statutory) guidance from TPR in the Defined Benefit Funding Code of Practice[3]. In TPR's research survey[4], 92% of trustees interviewed stated they had read the DB code of practice or a summary of it provided by the adviser. However, only 64% of trustees stated they had carried out all five of the activities named in the survey intended to assist in the management of funding, investment and covenant risks. This presents evidence to suggest that the non-legislative framework is not sufficient to encourage these behaviours from trustees. We want to encourage behavioural change across all schemes.

Government intervention is necessary to ensure the current quantitative process of assessing scheme funding through an actuarial valuation is complemented by a qualitative narrative from the trustee board that explains their approach to decision making and risk management. We want trustees to set out their scheme funding strategy clearly for themselves and to explain it to the Regulator. We expect this to lead to improved decision-making, and a more collaborative approach from trustees and their sponsor employers. We also expect this approach will encourage schemes to focus on key risks and mitigations. Our intention is to better protect members' pensions and give TPR the information it needs to assess whether they should take regulatory action.

What are the policy objectives and the intended effects?

These are to:

- support good governance; improve trustee decision-making in relation to scheme funding by requiring trustees to explain their approach or how they are complying with legislative requirements;
- support collaboration between the trustee board and the sponsor employer; and
- enable TPR to enforce a stronger "comply or explain" regime for all Defined Benefits schemes in relation to scheme funding.

Ultimately the intended effect is to enhance security of members' pensions.

[1] Defined benefit pension schemes: security and sustainability: Link
[2] Protecting defined benefit pensions: Link
[3] DB Funding Code of Practice- Link
[4] DB Trust-based pension schemes research: summary report 2018. Link

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Option 0: Do nothing. This would make no difference to trustee decision making and would not support TPR's regulatory enforcement action.

Option 1 (preferred option): To require all DB trustee boards to a) appoint a Chair and b) prepare and review annually a Statement strategy and to submit the Statement to TPR in accordance with requirements to be set out in secondary legislation. In addition c) we will require trustee boards to submit their valuation (with the new Statement) to TPR even when there is Statutory Funding Objective[5] surplus. As part of the work on this option, we also considered alternative implementation options with TPR and through informal engagement with stakeholders e.g. considering whether all or some DB schemes should submit a Statement, or how often the Statement should be submitted. These were not pursued, as they would not raise standards across all DB schemes.

Option 2: (alternative to legislation) Whether the existing legislative framework could be used to deliver our objectives. As discussed above, there is currently a non-statutory DB funding code. While, it would be possible to encourage some behavioural change from trustees using the DB Funding Code- as evidenced above- this approach has not worked currently and would not support TPR's regulatory enforcement (as the code has no statutory force). As such, we concluded that this would not support our broader objective of improving the scheme funding system.

A chair was deemed necessary to lead the trustees and give focus to the trustee board on this issue; the statement from the trustee board is necessary to provide a narrative on funding decision-making; and it would be necessary for the statement to be submitted to TPR to consider if regulatory action needed.

Will the policy be reviewed? It not be reviewed **If applicable, set review date: N/A**

Does implementation go beyond minimum EU requirements?		N/A		
Are any of these organisations in scope?	**Micro** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)		**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible Minister: ______________ Date: 6 February 2019

[5] Introduced by the Pensions Act 2004, the **statutory funding objective** (SFO) requires that an occupational pension scheme that is a salary-related scheme must have sufficient assets to cover its technical provisions (liabilities)

Summary: Analysis & Evidence

Policy Option 0

Description: Do Nothing.

FULL ECONOMIC ASSESSMENT

Price Base Year2017	PV Base Year 2020	Time Period 10 Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: N/A

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate	N/A		N/A	**N/A**

Description and scale of key monetised costs by 'main affected groups'

A do nothing option would have no impact on the behaviours of trustees, sponsor employers or The Pensions Regulator (TPR), as the current legislative framework is already supported by (non-statutory) guidance from TPR in a Defined Benefit Funding Code of Practice.

Other key non-monetised costs by 'main affected groups'

N/A

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	**Optional**
High	Optional		Optional	**Optional**
Best Estimate	N/A		N/A	**N/A**

Description and scale of key monetised benefits by 'main affected groups'

A do nothing option would have no impact on the behaviours of trustees, sponsor employers or TPR, as the current legislative framework is already supported by (non-statutory) guidance from TPR in a Defined Benefit Funding Code of Practice.

Other key non-monetised benefits by 'main affected groups'

A do nothing option would have no impact on scheme members' pensions.

Key assumptions/sensitivities/ risks	Discount rate (%)	3.5

BUSINESS ASSESSMENT (Option 0)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs: N/A	**Benefits: N/A**	**Net: N/A**	N/A

Summary: Analysis & Evidence — Policy Option 1

Description: Require all DB trustee boards to a) appoint a Chair who is responsible for signing the statement on behalf of the trustee board and b) prepare and review annually a funding and investment strategy and to submit the statement to TPR in accordance with the requirements to be set out in secondary legislation. In addition c) we will require trustee boards to submit their actuarial valuation (with the new Statement) to TPR even when there is a Statutory Funding Objective surplus.

FULL ECONOMIC ASSESSMENT

Price Base Year 2017	PV Base Year 2020	Time Period 10 Years	Net Benefit (Present Value (PV)) (£m)		
			Low:	High:	Best Estimate: - 168.5

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0.3	1		
High				
Best Estimate	1.0		19.5	**168.5**

Description and scale of key monetised costs by 'main affected groups'

There will be minimal costs to schemes (and ultimately their sponsoring businesses) attached to the appointment of a Chair - because most DB trustee boards already have a Chair, and where they don't, we expect most to be able to appoint one of their existing trustees[1]. There will be some ongoing extra costs in the form of the appointed Chair being paid more than other trustees. The extra cost per scheme is not likely to be significant. However, we anticipate that the total annual cost of having a Chair could be approximately £19.5 million, this is derived in the main body of the IA. We expect there to be some familiarising with the requirement to submit a statement signed by the Chair, we estimate this to be approximately £1m. There will be minimal costs to schemes attached to submitting actuarial valuations to TPR, together with the new Statement, when there is a funding surplus (Statutory Funding Objective) because trustees are already required to prepare valuations annually, and the cost of submitting the valuation is marginal. We estimate this to incur a total cost to business of approximately £9,354 per annum.

Other key non-monetised costs by 'main affected groups'

We have not quantified the cost of producing funding strategy statement as the detailed requirements (e.g. the content) are not known at this stage. However, we do not anticipate these to be substantial as there is already a clear expectation placed on trustees in the current DB code[2] to document their approach to funding (e.g. Statement of Funding Principles), investment (e.g. Statement of Investment Principles) and risk management. The new Statement would just clarify and formalise this requirement.

We will produce a full assessment of these impacts to support the subsequent secondary legislation, once the detail of these statement is known.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	0		0	**0.0**
High	0		0	**0.0**
Best Estimate	0		0	**0.0**

Description and scale of key monetised benefits by 'main affected groups'

[1] Secondary Source White Paper- Link p.58

[2] TPR Code of Practice Code 03 Funding Defined Benefits: Link

Other key non-monetised benefits by 'main affected groups'

The key non-monetised benefit is the greater protection and improved outcomes for DB scheme members, via the following mechanisms:

a) The requirement to appoint a Chair and for the Chair to sign the Statement is anticipated to improve scheme governance generally.
b) The requirement for a new Statement is intended to improve the trustee board's scheme funding decisions and to support TPR's enforcement.
c) The amendment to existing legislation to ensure actuarial valuations are submitted when there is a scheme surplus is also expected to improve the security of the members' pensions, because the information can be scrutinised by TPR. Also, it may benefit sponsoring businesses in the form of improved scheme running efficiency and associated cost reduction.

Given the lack of available quantitative evidence on the direct causal link between scheme governance and the impact of the new Statement on trustee board decision making, and the value of member protection/outcomes, it would be disproportionate to produce an estimate of monetised benefits.

Key assumptions/sensitivities/ risks	**Discount rate (%)**	3.5

There are a number of sensitivities around the estimate for the ongoing cost of having a Chair. The estimate is based on a survey produced by PwC on the difference in annual pay for Chair's and Trustees[3]. It is possible, however that some Chairs may not be paid for their services at all- if this is the case then this estimate would be lower.

In addition, the increased cost associated with having a Chair is based on the Chair having to work more hours and therefore receiving more pay for this, and a 'premium' for being a Chair rather than a trustee. It is the choice of the scheme whether to pay a 'premium' or how much of a 'premium' to pay for a Chair compared to a trustee.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			**Score for Business Impact Target (qualifying provisions only) £m:**
Costs: 19.6	**Benefits:0.0**	**Net: 19.6**	86.5 (In 2016 prices, 2017 present value)

[3] PwC Trustee Survey 2017- Link here.

Evidence Base (for summary sheets)

1. Background

In the White Paper "Protecting Defined Benefit Pension Schemes" ("the White Paper")[1], the Department proposed a package of measures to optimise scheme funding. In particular to improve accountability and decision making of the trustee board of a DB pension scheme in relation to scheme funding in order to better protect member's pensions.

2. Rationale for Intervention

In the Green Paper consultation (Defined benefit pension schemes: security and sustainability)[2] and subsequent White Paper (Protecting defined benefit pension schemes)[3] we identified a problem, shared by some stakeholders, about a lack of accountability and clarity on scheme funding standards as currently set out in the DB Funding Code resulting in poor scheme funding and investment decision-making, and insufficient assessment of risks. There was a view that the current quantitative process of submitting an actuarial valuation of the scheme's funding position would benefit from a qualitative narrative from the trustee board that explained their decision making, how they are complying with legislative requirements and their approach to risk management. Requiring trustees to set out their scheme funding strategy clearly for themselves and explain it to the Regulator should lead to improved decision-making from trustees, more informed discussions between trustees and their sponsor employers, and ultimately give TPR the information it needs to regulate more effectively in order to protect members' pension.

3. Policy objective

The White Paper makes clear that all DB Boards should appoint a Chair to support good practice and governance. It also outlines the dual purpose of the funding strategy Statement as a:

- Decision-making management tool for the trustee board which will support engagement with the sponsor employer; and
- Key measure to enable TPR to enforce a stronger "comply or explain" regime for all DB schemes on scheme funding, complementing the scheme funding information already submitted to TPR every three years.

4. Preferred option – Option 1

Require:

- All DB schemes[4] to appoint a Chair of the trustee board or of managers, with the Chair to sign the statement on behalf of the trustee board;
- Each DB board of trustees to prepare an annual statement to demonstrate how clearer funding standards are being met; and
- The trustee board to submit the statement to TPR with the scheme actuarial valuation or as prescribed, including on request by TPR.

The detailed requirements regarding the content of the statement will be set out in subsequent secondary legislation. The intention is that the Statement will contain the scheme's long-term goals and the trustee's strategic plan for achieving the scheme funding objective (SFO) within the context of the long term goals. Further information on the likely content, subject to further consultation is included in Table 3. A statement is also a requirement for Defined Contribution (DC) pension schemes. While we draw on information available from implementation of the DC statement, the two statements have different purposes and focus

[1] Pensions White Paper (March 2018) Protecting Defined Benefit Pension Schemes. Link - See in particular Chapter 2.

[2] Security and Sustainability in Defined Benefit Pension Schemes (February 2017)- Link

[3] Pensions White Paper (March 2018) Protecting defined benefit pensions Link

[4] Excluding those that are exempt from the funding requirements in Part 3 of the 2004 Act- as they will also be exempt from these changes.

on different information. Table 3 below provides a comparison of the DB and DC chair statements for reference.

5. Costs and benefits to businesses.

There are approximately 5,524 private sector DB schemes[5]. Legislation[6] currently exempts certain schemes from the funding requirements in Part 3 of the 2004 Act- for example schemes with fewer than a 100 members who are not registered for tax relief. For consistency, we want to exempt such schemes from the requirement to appoint a chair and for the board to prepare or review and submit a Chair Statement to TPR with the scheme valuation. There isn't any figures for the exact number of schemes that will be exempt under this legislation, however we anticipate that the number of schemes exempt under these requirements to be minimal.

In 2014, TPR published research relating to a survey on the costs of administering DB pension schemes. Of the 316 private sector schemes which completed the survey the mean annual running cost of schemes varied between £52,126 and £547,877 dependent on scheme size[7]. DB schemes are sponsored by sponsoring businesses, and so we assume that any costs incurred by schemes/trustees would ultimately be incurred by sponsoring businesses.

5.1 Costs of appointing a Chair.

We assume that there are no familiarisation costs attached to the appointment of a Chair. Schemes will be made aware that they are required to have a Chair of their trustee board- familiarisation with this requirement is expected to be negligible especially given the large proportion of DB schemes that already have a Chair.

Currently, having a Chair (of a scheme's trustee board) is not a legislative requirement in DB, but schemes may have a requirement in their individual scheme's rules. According to TPR's 21st Century Trustee Survey[8] in 2015, 85% of DB schemes (and 92% of hybrid schemes) already have a Chair of their trustee board. However, the proportion varies by scheme size – 74% for small, 87% for medium, 97% for large schemes.

The above figures suggest that only approx. 15% of DB schemes would have to establish a Chair as a result of the proposed legislation (the others already have one). Based on our engagement with TPR and the industry we anticipate that costs of establishing a Chair will be minimal, especially given that in many cases we expect that a Chair could be appointed from amongst the existing trustees.

A requirement to have a Chair for Defined Contribution (DC) type schemes was introduced in 2015. DWP's Impact Assessment on the new DC Chair's statement requirement[9] concluded that "*There may be some costs associated with establishing a chair of a trustee board. Evidence provided by pension providers in response to the consultation suggest that where a chair does not already exist the associated costs with establishing a chair would be minimal – as a chair could be* appointed *from amongst the existing trustees*".

5.2 Ongoing costs of having a Chair.

A member of a trustee board may work more and be paid more after becoming a Chair, for example, taking up the responsibility on behalf of the trustee board of ensuring the Statement is produced on time, that it accompanies the actuarial valuation and in accordance with other requirements to be prescribed in subsequent secondary legislation. According to PWC Trustee Survey 2017[10], for schemes that pay trustees, the average pay of the Chair of trustees is approximately £50,000 per annum, and for other board members this is approximately £15,000 per annum – but this varies by size (set out in the table below).

[5] The Purple Book 2018: Link, page 10.

[6] Regulation 17 of The Occupational Pensions Schemes (Scheme Funding) Regulations 2005

[7] DB Schemes running cost research 2014- Link

[8] Trustee Landscape Quantitative Research 2015- Link (see table B9 in page 53)

[9] Minimum Governance Standards for DC trust-based schemes – Impact Assessment (link: here)

[10] PwC Trustee Survey 2017- Link: here

Table 1: Difference in average annual pay for Chair and Board Members[11].

	Average of Annual pay for Chairman of board.	Average of annual pay for board members.	Difference in average annual pay
Under £0.5bn	£24,429	£5,856	£18,573
£0.5bn-1.5bn	£38,927	£10,418	£28,509
£1.5bn-5bn	£51,500	£10,813	£40,687
Over £5bn	£59,159	£20,658	£38,501

As discussed above, there are proportionally fewer large schemes that do not have a chair. Below we have applied the proportion of schemes without a Chair by size (shown in section 5.1) to the Purple Book 2018's estimate of the number of schemes by size[12].

Table 2: Estimated number of schemes without a chair by size[13].

Size of Scheme	Number of schemes without a Chair
2-99 Members	516[14]
100-999 Members	313[15]
1,000-4,999 Members	23[16]

To estimate the total costs to businesses of having a Chair we multiplied the difference in average annual pay shown in Table 1 by the number of schemes for the associated size of the scheme in Table 2[17]. This generated a total cost to business per annum of £19.5 million[18].

Key risks/sensitivities

- It is possible that Chair's and Trustees may not receive a salary at all for the hours they work.
- The increase in salary for a Chair compared to a Trustee is expected to come from two separate changes. Firstly, that the Chair may be required to work more hours in their role in order to make arrangements for the preparation of the statement and also signing it off on behalf of the trustee board. Secondly, they may be paid a 'premium' for being the Chair of the board. Introducing the requirement for a Chair, does not require schemes to pay them more- it is up to the scheme as to what role the Chair performs and the 'premium' applied to this role.

5.3 Costs of producing the Statement – familiarisation and ongoing.

5.3.1 Familiarisation with the requirement of a Statement.

We expect that all schemes will have to familiarise with the new requirements for the statement- even if they already have a Chair in place in the baseline. Resources invested (time etc.) in familiarisation with depend on the exact detail of the requirements for the new Statement and guidance made available by TPR- which will be known at the secondary legislation stage. However, as discussed above the majority of schemes already comply with the requirements in the baseline we expect the familiarisation process to be relatively straight forward.

[11] PwC Trustee Survey 2017- Table adapted from chart on page 3 - Link: here

[12] The Purple Book 2018- Figure 2.1 'The Purple Book 2018 dataset' link

[13] Note: We have excluded schemes with more than 5,000 members from this table. This is based on the assumption that schemes with that many members are likely to have a Chair.

[14] = 1985 schemes with 2-99 members multiplied by 0.26.

[15] = 2411 schemes with 100-999 members multiplied by 0.13.

[16] = 759 schemes with 1000-4999 members multiplied by 0.03.

[17] Note: We have excluded schemes with asset size of over £5bn difference in trustee chair pay from this analysis. This is based on the assumption that schemes of this asset size are likely to already have a Chair.

[18] = (18,573*516.1) + (28,509*313.43) + (40,687*22.77) = 19,447,544.

Here we assume that it will take all trustees 2 hours to familiarise with the requirements of a statement. For DB schemes there are an average of 3.2 trustees per scheme.[19] The average hourly wage of a trustee of £28.50 per hour[20]. This gives a total familiarisation cost for the statement requirements of £1m[21].

We believe this is a cautious approach because not all trustees may need to familiarise. Assuming only one per scheme needs to would give an estimate of approximately £0.3m[22].

5.3.2 Ongoing Costs

Costs of preparing and reviewing the Statement will directly depend on the content required and support (guidance) available. The content will be set out in secondary legislation. We will determine the costs and the Equivalent Annual Net Direct Cost to Businesses (EANDCB) more fully at the secondary legislation stage. At this stage we do not quantify the costs of producing statement.

However, we do not anticipate these costs to be significant as there is already a clear expectation placed on trustees in the current DB code to document their approach to funding, investments and risk management, and the Statement would essentially clarify and formalise this existing requirement. Also, as set out in the Government's White Paper, some costs of producing the Statement may be offset by removing other requirements on trustee boards to report information to TPR.

Cost of producing the Statement will depend on whether they currently comply and therefore schemes will fall into two groups:

a) Those trustees already complying with the current DB code will already take a long-term view of their funding strategy, manage risks in an integrated way and document their approach. This means the costs of formalising what they already have in place should be less than if they are not already compliant with current expectations. TPR's DB Survey[23] results show that 92% of trustees are in a position to evidence how they have taken an Integrated Risk Management (IRM) approach (but note not all of them actually apply all IRM principles to its full extent);

b) Those who are not complying with the current DB Funding Code may have higher upfront costs to reach the level of compliance already expected. From TPR's case experience and their latest DB governance survey we know that the DB code principles are not universally applied: a) two thirds (64%) of trustee boards reported that they carried out all five activities asked about with the aim of managing funding, investment and covenant risks[24], b) the proportion of schemes that are closed to future accrual that had in place a journey plan or long-term target (in addition to legally mandated technical provisions) stood at 76% among trustee boards and 79% among employers[25].

When a Statement requirement was being introduced for DC schemes, TPR estimated that the additional cost of producing and attaching this statement to the audited report and accounts could be between £350 and £3,250 per scheme per annum on average depending on scheme size[26]. <u>However, we highlight that requirements in relation to the DC Chair's Statement will be fundamentally different to that in DB, and so the costs mentioned here are for very broad illustrative purposes only.</u>

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19 Trustee Landscape Quantitative Research 2015- Estimate based on Figure 3.2.3 Number of trustees by scheme size. Link

20 The median hourly wage for a corporate manager or director is £22.44 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. Link This is uplifted by 27% for overheads from the previous version of the Green Book, no updated estimate is available.

21 =28.4988*2*3.2*5,524

22 = 28.4988*2*1*5,524

23 TPR DB Schemes Research: Summary Report 2017- Link

24 TPR DB Schemes Research 2018: Report- Link, page 18.

25 TPR DB Schemes Research 2018: Report- Link, page 5.

26 Source: Minimum Governance Standards for DC trust-based schemes, link

Table 3: Comparison between DB and DC Chair Statement

Comparing the Statements for DC schemes with DB schemes

Defined Contribution	Defined Benefit
Annual Statement Regarding Governance, essentially to reduce the amount of members' pension lost through investment costs and charges	To be submitted to TPR on a triennial basis even with actuarial valuation to improve scheme funding decision and enforcement, safeguards on calls for more contributions from employers
Statement reports on: • Timely scheme transactions • Trustee knowledge and understanding • Investment Strategy for default arrangements • Investment costs and charges, and impact Statement is published	Subject to further consultation, the Statement is intended to report on: • The long term funding and investment strategy for the scheme • Trustee's approach to scheme funding, investment and risk management in light of the long term destination for the scheme • To assists TPR's comply and explain regime: the Statement should explain how trustees are demonstrating the good practice set out in the revised DB Funding Code, and where they cannot they must show they are complying with legislative requirements. Statement is not published

As mentioned above, we will produce a full assessment of the requirements that will be set out in secondary legislation stage.

5.4 Cost of submitting actuarial valuation when there is an SFO surplus

Baseline Scenario: All DB schemes are required to conduct an actuarial valuation of their scheme every year. Schemes that are in deficit are required to submit their valuation and recovery plan to TPR at least every three years[27]. Those schemes that are in surplus are not required to submit their valuation but are required to provide some information to TPR through the 'Schemes in surplus' form as part of the Scheme Return[28] - this includes basic information used in the valuation such as discount rates, RPI/CPI assumptions etc.

The proposed change here is that schemes that have completed a valuation which shows them to be in surplus in respect of the Statutory Funding Objective, will now also have to submit that valuation to TPR. The administrative burden of this is expected to be minimal as this would replace the already existing 'Scheme in surplus' form. The costs associated with this proposed change are described below.

5.4.1 Familiarisation with submitting the actuarial valuation

Valuations are submitted to TPR via their exchange service. Schemes already use this service for a variety of scheme related activities including submitting their annual Scheme Return. In addition, schemes should also be aware of how to submit the valuation in case their scheme was to be in deficit. As such, we believe that schemes will incur negligible familiarisation costs as they are already aware of the process of submitting their valuation.

[27] Recovery Plans- Link

[28] DB and Mixed Benefit Scheme Return Example Form- page 25 Link

5.4.2 Ongoing cost of submitting the actuarial valuation

It is difficult to estimate the exact ongoing cost of submitting the valuation to TPR at this stage. Based on TPR's experience, we expect the extra cost of this requirement for surplus schemes to comprise of:

The number of schemes in surplus multiplied by the (cost of uploading valuation documents on Exchange plus the cost of filling in valuation summary minus the cost of updating return). Schemes are already expected in the baseline to undertake a valuation and to upload some of this information in the 'Scheme in surplus' component of the scheme return. As such, we assume that the changes to the requirements will result in an extra hour of work for either a scheme administrator or actuary. This produces a total per annum cost of approximately £9,354 for businesses. This comprises of:

- Number of schemes submitting the valuation per annum*:* As at 31 March 2017, approximately 20% of DB schemes were in surplus on the SFO basis[29]. This estimates that approximately 1,105 schemes are in surplus. As schemes are placed into tranches, different schemes will conduct and submit their valuations in different years. For simplicity we assume that these 1,105 schemes in surplus are split evenly across the different tranches and that 1/3 (368 schemes) are conducting and submitting their valuations each year.
- Hourly wage for professional is equal to £25.40[30]- we use this as a proxy for the wage of both a scheme administrator and actuary.
- One hour of extra time spent as a result of the changes.

We think this a cautious approach as the time spent submitting the valuation should be minimal. In addition, TPR currently has an internal procedure for checking a cross section of surplus valuations every year and may already request a copy of the scheme's valuation for this assessment.

5.5 Benefits of appointing a Chair and the new Statement

As set out in the Department's White Paper, this measure is expected to support trustees and their sponsoring employers to make the best possible long-term decisions to meet the pension liabilities of all members of the pension scheme over time.

The Department's White Paper[31] stated 'The Chair's statement is expected to lead to better management practices and decision making. In essence, it is a form of accounting for decisions made and actions taken, and is expected to (a) 'remind' about, and (b) trigger compliance with the requirements and adequate amount of effort put in when making decisions such as investment decisions.'

It is not possible to quantify the benefits as many other factors drive improvements in governance and it is difficult to estimate the baseline. Quantifying the benefit would be disproportionate as isolating those impacts from other factors that drive scheme governance and cost efficiency would be a very complex and resource intensive exercise. However, there is evidence that an improvement in governance would lead to better pension outcomes:

- A study by Willis Tower Watson[32] concluded that they 'believe the investment case for improving governance is, for most funds, overwhelming'.
- Clark and Urwin[33] have also shone the light on the benefits of good governance and illustrated that their sample of 'best-practice' schemes achieved at least 2% per annum more return than their benchmarks.
- Ambachtsheer et al found a positive statistical relationship between good governance and investment performance (in a sample of 81 schemes from around the world). Schemes with good

[29] White Paper- Link page 52.

[30] The median hourly wage of a professional is £20.00 in the Annual Survey of Hours and Earnings 2017 revised, Table 2.5. This is uplifted by 27% for overheads from the archived Green Book- Link

[31] White Paper- Link page 59.

[32] Link

[33] Clark G & Unwin R (2008), Best-practice pension fund governance; secondary source: PPI Briefing Note 89, link

standards of governance (self-assessed by schemes and with size of scheme controlled for) added 1-2% per annum in investment performance when compared to less-well governed schemes[34].

- A study by Ammann and Ehmann 2014[35] constructed objective governance scores for Swiss pension funds (sample of 139) based on organisational structure, target setting and investment strategy, investment process, risk management, monitoring and transparency. The scores were then compared to investment performance and found a positive relationship.

The Statement is intended to result in better decision making in line with clearer funding standards over the long term and collaboration with employers through the Declaration of Intent (DoI)[36]. Given that DB pension schemes are sponsored by an employer (businesses), improved scheme governance and accountability as a result of the proposed requirements is likely to benefit the sponsoring businesses e.g. through improved efficiency and cost transparency – potentially reducing cost pressure on them.

6. Costs and benefits to scheme members

6.1 Costs of appointing a Chair and Cost of submitting a Statement and actuarial valuation every 3 years

These measures will not result in any costs to scheme members as they will not have to familiarise or implement any of the requirements.

6.2 Benefits of appointing a Chair

The requirement to have a Chair and for the trustee board to regularly produce and report their funding strategy to TPR is designed to improve scheme governance and decision making, which in turn is intended to ensure scheme running is both more efficient and more secure for members.

6.3 Benefits of a Statement with actuarial valuation (even when there is a scheme funding surplus) from the trustee board

As set out in the Department's White Paper, wider evidence coming from behavioural, management, and psychology related disciplines suggest clarification, commitment and external monitoring does tend to lead to positive outcomes. For example, FCA's Behaviour and Compliance in Organisations study[37] says that 'one of the lessons of the psychological literature on behavioural biases is that the 'bias blind spot' means that it is easier to spot such biases in others than it is to spot in oneself'. In some cases trustee decision making can be seen as a behavioural bias - this is where problems such as loss aversion can lead to decision makers becoming attached to poor practices[38]. One way of correcting these sorts of biases is to use decision making tools e.g. a checklist or, in this context, a Chair's Statement to increase internal scrutiny. Some psychologists argue that these work via increasing reflective decisions (those that are slow, deliberate and with effort) over intuitive decisions (those with minimal preparation, effortless and instinctive) which can help to reduce these biases.

As mentioned above, the Chair's statement in DC pensions is a very different context, however evidence and experience from DC does help to reassure that it is reasonable to expect that the intended effects are achievable in practice. As set out in the White Paper, in the course of their 21st Century Trustee engagement exercise, TPR heard evidence from practitioners and stakeholders that the DC Chair Statement was having a positive impact – the requirement has helped focus trustees on governance and make improvements (transparency drives accountability).

Better scheme governance is anticipated to improve the security of members' pensions – i.e. to increase the likelihood of members ending up getting their pensions (promised to them) paid in full.

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[34] Source: Ambachtsheer et al 2006, link; secondary source: PPI Briefing Note 89, link

[35] Source: Ahmmann M & Ehmann C (2014) Is Governance Related to Investment Performance and Asset Allocation? Secondary source: PPI Briefing Note 89, link

[36] For more information on these policy changes see the separate LTO RIA and DoI RIA.

[37] Link

[38] Definition based upon FCA behaviour and compliance in organisations.

Additionally, preparing this information and submitting it to TPR for scrutiny, could lead to better informed products or clearer communication to members (through for example, the Statement of Funding Principles or the Summary Funding Statement).

7. Small and Micro Business Assessment SaMBA

The proposed changes will affect all DB schemes and their sponsoring employers regardless of sector or size. As discussed in section 5, legislation[39] currently exempts certain schemes from the funding requirements in Part 3 of the 2004 Act. For consistency these schemes will also be exempt from the proposed changes.

The majority of DB schemes have more than 100 members, as set out in table 4. Although this refers to scheme size and is not a direct measure of the number of employees in the underlying sponsoring employer, it indicates that small and micro employers (up to 49 employees) would not be disproportionately impacted by this measure.

Table 4: Number of DB schemes by scheme size[40]

Number of members	**Number of schemes (Purple Book-Estimated 2018 Universe)**
2-99	1,985
100-999	2,411
1,000-4,999	759
5,000-9,999	171
10,000+	198
Total	**5,524**

Source: PPF Purple Book 2018

As set out above, relatively fewer small schemes currently have a Chair of their trustee board compared to large schemes. Also, evidence suggests that smaller schemes, on average, tend to be less compliant with the current DB code and good practices – which means some of them may need to invest relatively more resources in meeting the new requirements. Therefore, the proposed changes will have a larger impact on those DB sponsoring employers that sponsor a smaller sized scheme. At the same time, this means they are likely to benefit relatively more given the scope they have for governance and management improvements.

The costs to business fall to the sponsoring employers of the DB schemes. Small and micro businesses that sponsor DB schemes may be affected. However, assessing the impact of the proposed changes in this IA on this group is difficult, as it is not necessary that small and micro pension schemes correspond to small and micro businesses. For example, a large firm may sponsor a small scheme with only a few members. Similarly, DB schemes can be sponsored by multiple employers so it could be that many small and micro businesses sponsor larger DB schemes. As this is likely to impact small pension schemes, and there is currently no robust evidence to link pension scheme size to employer size, it is difficult to accurately assess the impact on small and micro business.

The Annual Survey of Hours and Earnings (ASHE) data set provides information on the size of DB sponsoring employers with active members. This will only include those who are contributing to a DB pension so will exclude members who are in schemes closed for future accrual but it helps to provide an indication of the size of DB sponsoring employers. The table below shows the proportion of Private sector and Not for Profit active DB members by employer size.

[39] Regulation 17 of The Occupational Pensions Schemes (Scheme Funding) Regulations 2005

[40] PPF Purple Book 2018 Figure 2.1 Link

Table 5: Proportion of DB sponsoring employers, by employer size[41]

Size of Employers	Proportion of DB members[42]
0	0%
1-9	2%
10-49	10%
50-99	4%
100-499	14%
500-999	9%
1000+	61%
All sizes	**100%**

The above evidence shows that the majority of active DB members work in businesses with more than 50 employees. Approximately 10% and 2% of active DB members work in Small and Micro businesses respectively. If these employers sponsor smaller sized schemes then they may encounter a higher cost as a result of this measure relative to their overall costs, however they will also benefit from the introduction of this requirement. As discussed above in section 5.5, it is not possible to quantify these benefits due to the number of different factors that contribute to governance and the uncertainty of predicting future investment outcomes. It should also be noted here that the costs incurred to the scheme rise with the size of the assets of the schemes. As such, we don't expect that there will be a disproportionate impact on small and micro businesses as a result of the proposed changes in this impact assessment.

8. Monitoring and Evaluation.

We will work with TPR and the industry in order to understand and review post implementation.

9. Implementation

We intend to introduce primary legislation as soon as parliamentary time allows. This legislation would require DB schemes to have a Chair and for them to produce a statement of Strategy. We provisionally assume in this impact assessment that this will be in 2020.

[41] Source: DWP estimates derived from ONS Annual Survey of Hours and Earnings (GB)

[42] Figures below are rounded to the nearest 1%,

Estimated direct costs

Table 6: Estimated impacts for introducing the requirement for schemes to have a Chair.

	Schemes	Cost	How often?	Assumptions	Rationale
Familiarisation with the requirements	516 Small schemes (2-99 members) 313 Medium schemes (100-499 members) 23 Large schemes (500-4999 members)	-	One-off	We assume that there are no familiarisation costs attached to the appointment of a Chair.	Schemes will be made aware that they are required to have a Chair of their trustee board- familiarisation with this requirement is expected to be negligible especially given the large proportion of DB schemes that already have a Chair
Appointing a Chair	516 Small schemes (2-99 members) 313 Medium schemes (100-499 members) 23 Large schemes (500-4999 members)	-	One-off	We assume that there are no costs attached to the appointment of a Chair.	Based on our engagement with TPR and the industry we anticipate that costs of establishing a Chair will be minimal, especially given that in many cases we expect that a Chair could be appointed from amongst the existing trustees. A requirement to have a Chair for Defined Contribution (DC) type schemes was introduced in 2015. DWP's Impact Assessment on the new DC Chair's statement requirement[1] concluded that "*There may be some costs associated with establishing a chair of a trustee board. Evidence provided by pension providers in response to the consultation suggest that where a chair does not already exist the associated*

[1] Minimum Governance Standards for DC trust-based schemes – Impact Assessment (link: here)

					costs with establishing a chair would be minimal – as a chair could be appointed *from amongst the existing trustees*“.
Ongoing cost of having a Chair	516 Small schemes (2-99 members) 313 Medium schemes (100-499 members) 23 Large schemes (500-4999 members)	516 Small Schemes multiplied by £18,573 (difference between Chair and Trustee annual pay for schemes with less than £0.5bn assets) equals £9.6m. 313 Medium schemes multiplied by £28,509 (difference between Chair and Trustee annual pay for schemes with £0.5bn to £1.5bn in assets) equals £8.9m. 23 Large schemes multiplied by £40,687 (difference between Chair and Trustee annual pay for schemes with £1.5bn to £5bn in assets) equals £0.9m.	Per annum		
Total Cost		£19,447,544 per annum.			

Table 7: Estimated impacts for the requirement for the Chair to sign a FIRM (Funding Investment and Risk Management) statement.

	Schemes	Cost	How often?	Assumptions	Rationale
Familiarisation with the requirements	5,524 DB Schemes	£1,007,535.	One-off	All schemes will choose to familiarise. Hourly wage of a trustee is £28.50 It takes 2 hours to read through and transpose the document about the new requirements. The average number of trustees is 3.2.	
Ongoing costs of complying with the requirements.	5,524 DB Schemes	To be estimated once detail and content is confirmed at the secondary legislation stage.	Per annum		
Total Cost		£1,007,535 in Year One.			

Table 8: Estimated impacts for the requirement to submit an actuarial valuation even if the scheme is in SFO surplus.

	Schemes	Cost	How often?	Assumptions	Rationale
Familiarisation with the requirement	1,105 DB Schemes	-	One-off		Schemes are already familiar with the Exchange service as this is where they have to submit their Scheme Return. Schemes should also be aware of how to submit the valuation in the case that their scheme would be in deficit.
Ongoing costs of submitting the actuarial valuation.	1,105 DB Schemes	£9,354	Per annum.	20% of schemes are in surplus. Schemes will submit the valuation triennially, we assume the schemes in surplus are evenly distributed across all the different tranches- so an additional 368 schemes per annum will be submitting their valuation per annum. The hourly wage of a Scheme administrator is approximated to be £25.40. Schemes will spend an additional 1 hour submitting this information compared to the baseline scenario.	
Total Cost		£9,354 per annum			