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Draft DB Funding Code of Practice

Response to consultation

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Covering note

We appreciate the opportunity to respond to the draft Funding Code of Practice (the "Code") and Fast Track regulatory approach consultations.

This paper sets out our responses to the detailed questions raised, together with our high-level comments below.

Overall approach

As an organisation we are supportive of the principle that schemes should have a journey plan in place for meeting their objectives with risk being taken at a supportable level. Therefore, we welcome the direction of travel of the draft Regulations and Code, subject to the time and cost burden on schemes being proportionate to the outcomes achieved.

First consultation

We were pleased to see that TPR had reflected on the feedback on the first code of consultation and made Bespoke compliance principle based and not compared against Fast Track compliance.

Interaction with Regulations

We were also encouraged to see that TPR has taken a pragmatic interpretation of the draft Regulations in a number of areas, e.g. the low dependency investment strategy, and the resulting flexibility in the draft Code to reflect scheme specific circumstances.

We would request that TPR and DWP work together ensure the Regulations are compatible with the principles set out in the draft Code. We understand that the Code reflect Government policy. However, in line with other industry stakeholders, we have concerns that compliance with the Code does not automatically infer compliance with the Regulations and these, as currently drafted, could be interpreted by a Court with less flexibility than contained in the Code.

We are also supportive of TPR and DWP amending the calculation of duration for deriving the point of Significant Maturity so that it is less sensitive to changes in interest rates. This would help provide stability to pension scheme journey plans and business planning.

Covenant assessment

The Code introduces a more formulaic funding regime compared to the existing position, particularly in relation to the covenant strength assessment. We have some concerns about the level of assessment of sponsor business plans on how involved trustees should be in these plans.

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For larger/multi-national groups the guidance on assessing cashflows and the value of guarantees feels over simplified. Also, how trustees should assess the value of contingent assets and allow for them within their overall approach is an area where greater clarity is required.

One concept that is formalised in the Code and highly significant to the setting of an acceptable journey plan is covenant reliability. In our view it will be difficult for trustees (or covenant advisors) to provide a single figure for this due to its subjective nature.

Therefore, we recommend TPR adopt a simpler approach and set a default value (e.g. 6 years). This would allow trustees/covenant advisers to consider whether they are comfortable that their reliability period is at least this value, which is an easier question to consider rather than what the specific reliability period is. If the answer is that the reliability period is shorter than the default, then this value should be adopted.

Equally, trustees should be able to provide evidence if they believe a longer reliability period was justified. The latter will be important in ensuring the viability of schemes with resilient sponsors and supporting robust open schemes.

Other areas

In addition, we believe the following areas are worthy of consideration in refining the draft Code:

- We would prefer to see less prescription in the draft Code around the setting of assumptions. We suggest that the assumption Appendices are moved to into the Fast Track guidance with the Code containing less detail and requiring evidence-based/consistent assumptions with an overall appropriate level of prudence.

- TPR will have to set its preferred balance between how easy it is to comply via Fast Track and the appropriate level of tolerable risk it is willing to accept. If TPR wants to encourage schemes to adopt Fast Track, we would suggest that the level of compliance is minimised. This should come in the form of a simplified Statement of Strategy, lighter touch reporting and minimal covenant analysis requirements (as effectively the approach is covenant neutral).

- A yield curve approach means different things to different people. For example, a yield curve approach can be a single equivalent basis derived from yield curves using sample or scheme cashflows. To provide flexibility and enhance pragmatism we would welcome clarification that advisors can use their judgement when adopting a suitable 'yield curve' approach.

- As noted above it is important to reduce the burden on smaller schemes, therefore we recommend that the small scheme definition is extended in both the Code and Fast Track to capture more schemes. A scheme should be classified as small if it has 100 members or less or the asset size is less than £25M.

- While we don't believe the code should be expanded to try and deal with every type of scheme specific circumstance, it would be worth including a comment to say that trustees should look to apply the principles in non-standard scheme designs. Examples include hybrid arrangements (DB with a DC underpin and vice versa), cash balance, shared cost, etc.

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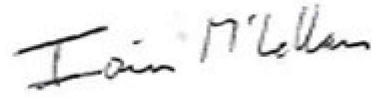
We would be happy to discuss any queries on our response you have.

I can confirm that we are comfortable for our response to be made public and for our name to be included in any public list of respondents.



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Funding code of practice consultation responses

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1)Are there any areas of the summary you disagree with or would like more /less detail? If yes, what areas and why?

In paragraph 20, it is worth noting that there are situations where trustees don't need to obtain employer agreement

2) Do you agree with the principles for defining a matching asset that i) the income and capital payments are stable and predictable; and ii) they provide either fixed cash flows or cash flows linked to inflationary indices? If not, why not and what do you think is a more appropriate definition?

The principles for defining a matching asset are reasonable and allow for a degree of judgement. However, please note many assets will have varying degrees of matching characteristics. TPR should consider whether their goal is literal cashflow matching or reducing reliance on employer contributions. If the latter a focus on strong funding with hedging of key risks may be more appropriate.

3) Do you agree with our approach for defining broad cash flow matching? If not, why not and what would you prefer?

We welcome the clarification and flexibility versus a more literal reading of the funding Regulations.

The funding Regulations can be interpreted as a requirement to hold high quality bonds. Therefore, we suggest TPR work with DWP to better align the funding Regulations to the Code to avoid any confusion.

4) Do you think draft adequately describes the process of assessing cashflow matching? What else would be appropriate to include in the code on this aspect?

Yes, the process is adequately described.

To reduce the burden on smaller schemes, we recommend that the small scheme definition is extended in both the Code and Fast Track to capture more schemes. A scheme should be classified as small if it has 100 members or less or the asset size is less than a nominal amount (by reference to, say, the lowest asset value in the last three years' Trustee Report and Accounts). The nominal amount could be set by TPR, but we would suggest something in the region of £25m.

5) Should the code set out a list of the categories of investments into which assets can be grouped for the purposes of the funding and investment strategy? If so, what would you suggest as being appropriate?

No, the judgement of advisors based on the Code is appropriate.

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6) Do you agree that 90% is a reasonable benchmark for the sensitivity of the assets to the interest rate and inflation risk of the liabilities?

Yes, for fully funded schemes or schemes at least 90% funded at the relevant date this is reasonable. However, given the restrictions on leverage we believe it is more appropriate to loosen the definition to reference a high level of hedging. This would provide additional flexibility for trustees and advisors to reflect scheme circumstances whilst ensuring material hedging is in place e.g. where 89% hedged may be deemed optimal.

7) Should we, and how would we, make this approach to broad cash flow matching more proportionate to different scheme circumstances (eg large vs small)?

In our view the approach is sufficient flexible therefore there is no requirement to tailor to different scheme circumstances.

However, in practice, there will be some schemes where a proportionate approach will be required. For example, there are a number of schemes that are still fully invested in historic with-profits (due to them retaining valuable Guaranteed Annuity Rates) where the considerations will be different.

8) Do you agree with our approach that a stress test is the most reasonable way to assess high resilience?

Yes. Advisors and trustees are familiar with stress testing in the pensions market.

9) Do you agree that setting the limit of a 4.5% maximum stress based on a one year 1-in-6 approach is reasonable? If not, why not and what would you suggest as an alternative?

Yes.

A 4.5% change in funding level is reasonable, recognising that it won't be possible (or desirable) to overly focus on minimising any funding volatility.

10) Do you agree that we should not set specifications for the stress test but leave this to trustees to justify their approach? If not, what would you suggest as an alternative?

Yes, as this provides greater flexibility to capture scheme circumstances / different analytical tools. In addition, it is important that schemes can continue with or develop their current approach.

11) Do you agree with our approach for not expecting a detailed assessment of liquidity for the low dependency investment allocation (LDIA) since we have set out detailed expectations in relation to schemes' actual asset portfolios?

Yes.

12) Do you agree with our approach for not expecting a stochastic analysis for each assumption to demonstrate that further employer contributions would not be expected to be required for accrued rights, but rather focussing on them being chosen prudently? If not, what would you suggest as an alternative?

Yes, an evidence-based approach to setting assumptions combined with a check that the overall level of prudence across the assumptions is appropriate and reasonable.

Schemes can still adopt a stochastic approach if they wish.

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13) Do you agree that the two approaches we have set out for the discount rate for the low dependency discount rate (LDFB) are the main ones most schemes will adopt? Should we expand or amend these descriptions, if so, how?

Yes, the two approaches are the main ones that are used. No further expansion is required.

14) Should we provide guidance for any other methodologies?

Yes, in relation to what constitutes a 'yield curve' approach.

A 'yield curve' approach means different things to different people. For example, a 'yield curve' approach can be a single equivalent basis derived from 'yield curves' using actual scheme cashflows or proxy cashflows with a similar profile. To provide flexibility and enhance pragmatism we would welcome clarification that advisors can use their judgement when adopting a suitable 'yield curve' approach.

15) Do you agree with the guidance and principles set out in Appendix 3 and 4? Are there any specific assumptions here you would prefer a different approach? If so, which ones, why and how would you prefer we approached it?

For a principle-based approach we would prefer the Appendices are moved to Fast Track and the Code contains only commentary requiring evidence-based/consistent assumptions, based on best estimates, with an overall appropriate level of prudence (irrespective of where/how this is built in).

Expenses

Overall, the principle of including an expense reserve is sensible if you are going to be "self-sufficient". However, it should be up to advisors and trustees to determine an appropriate reserve and the time-period the reserve covers.

A pragmatic and proportionate scheme specific approach is required to avoid unintended consequences, e.g. trapped surplus as a result of low dependency prudence plus an expense reserve. For example, if an expense allowance is to be included it may be more sensible for trustees to consider reflecting this over shorter periods such as the length of the Schedule of Contributions or period until the next valuation date.

If the requirement for an expense reserve is retained, it would helpful if you could confirm the definition of an immature scheme in this section. Specifically, we would like to see greater proportionately to capture open scheme who are immature and do not expect to mature when considering calculation of a mandated expense reserve.

Yield curve

As noted in our response to question 14, a yield curve approach means different things to different people. For example, a yield curve approach can be a single equivalent basis derived from yield curves using sample or scheme cashflows. To provide flexibility and enhance pragmatism we would welcome clarification that advisors can use their judgement when adopting a suitable 'yield curve' approach.

Actuarial factors

Capturing actuarial factors in the future i.e. over the journey to significant maturity will be difficult from both an assumptions and calculation point of view. Confirmation that trustees and advisors are free to adopt reasonable factors over the journey plan would be welcome.

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16) Do you agree that a simplified approach to calculating duration for small schemes is appropriate?

Yes, as it provides additional flexibility for small schemes and has a lower burden. Although, we believe the definition of small schemes should be extended to less than 100 members or assets less than a nominal amount, say £25m.

17)Do you think setting an earlier point for significant maturity within Fast Track as compared to the code (as described in option 3 in this section of the consultation document) would be helpful for managing the volatility risk of using duration? If yes, where would you set it and why?

Of the options presented we would prefer option 1, but recognise this will require the Regulations to be amended.

If the Regulations are not amended to facilitate option 1, option 3 if preferable. However, given recent changes in market conditions, TPR should consider reducing the durations proposed in option 3, i.e. 8 years instead of 10 years.

18) Do you agree with the definitions for visibility, reliability, and longevity? If not, what would you suggest as an alternative?

Yes.

We welcome TPR's view that covenant reliability and longevity can roll over at each valuation. It would be helpful to capture this in the final Code.

In our view the key measure under the Code is the covenant reliability period. It will be difficult for trustees and covenant advisors to provide a single figure for this due to its subjective nature. Therefore, we recommend TPR adopt a simpler approach and set a default value for the covenant reliability period (e.g. 6 years to align with Fast Track).

This would allow trustees/covenant advisers to consider whether they are comfortable that their reliability period is at least this value, which is an easier question to consider rather than what is the actual reliability period. If the answer that the reliability period is shorter than the default, e.g. a distress situation, then this value should be adopted. Equally, trustees should be able to provide evidence if they believe a longer reliability period was justified, e.g. a sponsor with multiple long term contracts. The latter will be important in ensuring the viability of strong established open schemes and schemes that are sponsored by not for profits.

19) Do you agree with the approach we have set out for assessing the sponsors cash flow? If not, what would you suggest as an alternative?

Yes.

20) Do you agree with the approach we have set out for assessing the sponsors prospects? If not, what would you suggest as an alternative?

Yes.

21) Do you agree with the principles we have set out for contingent assets, i.e. that i) it is legally enforceable and ii) it will be sufficient to provide that level of support? If not, what would you suggest as an alternative?

The principles are reasonable and in line with current practice.

However, under the draft Code, it isn't exactly clear how a contingent asset can be reflected in the shape of the journey plan, the low dependency strategy and/or the recovery plan. While look-through guarantees effectively allow for the covenant

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assessment to be based on the guarantor, it isn't clear what happens in other situations (e.g. if they were capped, time-bound or subject to other restrictions).

We appreciate updated covenant guidance is going to be published, but it would be helpful for trustees to be given a greater steer within the code of how they should be aiming to reflect the presence of a contingent asset, i.e. should they look to reflect in covenant reliability periods, maximum affordability assessments, low dependency strategy or a combination of all of them.

22) Do you agree with the approach we have set out for valuing security arrangements? If not, what would you suggest as an alternative?

Yes, there is sufficient flexibility for the trustees to work with their advisors to determine an appropriate valuation. However, see our response to Question 21 on how security arrangements are reflected.

23) Do you agree with the approach we have set out for valuing guarantees? If not, what would you suggest as an alternative?

Yes, there is sufficient flexibility for the trustees to work with their advisors to determine an appropriate valuation. However, clarification on whether the look through guarantee is intended to be stronger than full S75 debt on insolvency would be helpful.

24) Do you agree with the approach we have set out for multi-employer schemes? If not, what would you suggest as an alternative?

Yes, as it provides Trustees with the flexibility to adopt a proportionate approach as needed. However, it would be helpful to include further details for multi-employer schemes with both open and closed sections. It would also be helpful for the guidance to highlight differences in approach (if any) for multi-employer schemes where the employers are non-associated.

25) Do you agree with the approach we have set out for not-for-profit covenant assessments? If not, what would you suggest as an alternative?

It would be helpful to acknowledge situations where the non-commercial nature of organisations can be positive, e.g. long-term evidence of public funding and individual donations of third-sector organisations, organisations (e.g. Housing Associations, Universities, Charities) which have significant asset bases, lack of natural competition, have oversight from the Charities Commission, are non-dividend paying, etc.

We also believe that it would be reasonable for explicit reference to charities being able to undertake their charitable purpose as being a reasonable use of cashflows when trustees are assessing affordability.

26) Do you agree with how we approached how maturity has been factored into the code? If not, what would you suggest as an alternative in particular with reference to the draft Regulations?

Yes, more risk can be allowed for where the employer is further away from the relevant date. Please note it is important the relevant date remains as stable as possible to ensure proper planning, hence our preference for option 1. See our response to Question 17.

27) Do you agree with the way in which we have split the journey plan between the period of covenant reliability and after the period of covenant reliability? If not, what would you suggest as an alternative?

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Yes, this is sensible in the context of the proposed approach. Although please see our response to Question 18 on setting the period of covenant reliability.

28) Do you agree that trustees should, as a minimum, look at a one year 1-in-6 stress test and assess this against the sponsors ability to support that risk?

Yes, protecting against a 1 in 2 valuation cycle event is sensible, aligns with PPF stress testing and is a tangible event for trustees to consider.

Where sponsors of schemes in deficit are already paying deficit contributions that are at the maximum the employer can reasonably afford, it is not clear where and how they would also still have scope to support a further 1 in 6 downside event.

29) Do you agree that if trustees are relying on the employer to make future payments to the scheme to mitigate these risks, then the trustees should assess the employer's available cash after deducting DRCs to the scheme and other DB schemes the employer sponsors?

As noted in our response to Question 28, if employers are already making deficit contributions at the maximum level that is reasonably affordable, then it is not clear to us that there would be much cash available to offset further risk in the short term. In these situations, another consideration would be whether the current Recovery Plan could be extended if required to cover additional deficit contributions.

30) Do you agree that this approach is reasonable for assessing the maximum risk that trustees should take during the period of covenant reliability?

We would prefer the Code to include higher level principles, and more than one (mechanistic, but in practice potentially difficult to apply) approach to determining the level of risk which is supportable. These principles could include options for either stochastic or scenario analysis as appropriate to allow trustees to understand and form views on whether the risk being taken is supportable.

31) Do you agree with the considerations we have set out regarding de-risking after the period of covenant reliability?

Yes, the ability to adopt a different approach to linear de-risking is helpful. As noted in our response to Question 18 in certain cases we believe that it will be important for trustees to be able to adopt longer covenant reliability periods where justified.

32) Do you agree with our approach of not being prescriptive regarding the journey plan shape?

Yes. This provides greater flexibility and allows the journey plan to be tailored to individual scheme circumstances.

33) Do you agree with our approach that the maximum risk trustees should assume in their journey plan is a linear de-risking approach where they are taking the maximum risk for the period of covenant reliability?

Yes. In most cases this will be appropriate recognising in practice there will be volatility to the funding path and linear de-risking may not be appropriate in all situations.

34) Do you agree with our explanation of the statement of strategy and are there areas it would be helpful for us to expand on in this section?

Yes, although preparing and submitting the statement will be an important driver of the compliance burden under the new Code. We would welcome further comments relating to proportionality, i.e. clear guidance on what proportionately looks like for

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smaller / less complex schemes, and suggest a lighter touch approach for schemes that are adopting Fast Track.

35) Do you agree with how we have described the consistency of the TPs with the funding and investment strategy? If not, why not and what would you suggest as an alternative?

Yes.

36) Do you agree that open schemes could make an allowance for future accrual – thereby funding at a lower level - without undermining the principle that security should be consistent with that of a closed scheme?

Yes, we agree that open schemes should be able to make an allowance for future accrual. Indeed, in many cases it is imperative to retain viable open schemes.

We note though that for schemes open to new entrants, if the accrual allowance is limited to six years or less, this only modestly changes the relevant date, and still requires such schemes to fund as if they will be de-risking over time, when in practice this is unlikely to be the actual expected future strategy. Such schemes subject to appropriate evidence should be able to have longer than normal covenant reliability periods.

37) Do you agree that this should normally be restricted to the period of covenant reliability? If not, why not and what you suggest as an alternative?

Yes, although as noted in Question 18, it is important that trustees can adopt a longer covenant reliability period when they can demonstrate the costs can be supported over the period.

38) Do you agree with our principled based approach to future service costs? If not, why not and what you suggest as an alternative?

Yes, there should be suitable flexibility in the Code for setting the future service cost.

39) Do agree with our approach to defining Reasonable Alternative Uses? If not, why not and what you suggest as an alternative?

Yes. Although please see our response to Question 25 for not-for-profit employers.

40) Do you agree with the description in the draft Code of the interaction between the principle that funding deficits must be recovered as soon as the employer can reasonably afford and the matters that must be taken into account in regulation 8(2) of the Occupational Pension Schemes (Scheme Funding) Regulations 2005?

Yes, however the draft Code doesn't describe the interaction between the 'as soon as reasonably affordable' principle and the matters set out in regulation 8(2).

41) Do you agree that reliability of employer's available cash should be factored in when determining a scheme's recovery plan length?

Given the subjective nature of the assessment of the covenant reliability period, we foresee tensions between trustees, covenant advisers, employers and TPR around this point, and a tendency for covenant advisers to act cautiously when advising on covenant reliability periods. Therefore, we recommend a default value as per our response to Question 18.

42) Do you agree with the principles we set out when considering alternative uses of cash? If not, which ones do you not agree with and why? What other principles or examples would it be helpful for us to include?

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Yes, however the Code should clarify that after significant maturity any deficit does not have to be repaid immediately. A short period would be appropriate.

43) Do you agree with our approach to post valuation experience? If not, why not and what you suggest as an alternative?

Yes. Although we would remove any reference to a prudent allowance to avoid any excessive prudence. We would prefer an expectation that the trustees should be able to justify their approach.

44) Do you agree with our approach to investment outperformance? If not, why not and what you suggest as an alternative?

Yes.

45) Should we set out more specifics around what we would expect by way of security to protect against the additional risks?

No.

46) Do you agree with our approach that, while trustees' discretion over investment matters is not limited by the funding and investment strategy, we expect investment decisions by trustees should generally be consistent with the strategies set out in the funding and investment strategy? If not, why not and what you suggest as an alternative?

Yes.

47) Do you agree with the examples we have given for when trustees investment strategies may not mirror their FIS? Are there other examples we should consider?

Yes, this captures the key scenarios.

48) Do you agree with the expectations regarding trustees with stressed employers? If not, why not and what you suggest as an alternative?

Yes, the opportunity to take some risk beyond what is supportable as set out in the Code is welcome.

49) Do you agree with the principles we have set out regarding risk management? Are there other aspects it would be helpful for us to include?

The principles are sensible. However, the key will be how pragmatism is assessed by TPR and interpreted by advisors and trustees. The Code and single/general code has the potential to create a governance and risk management time/cost burden that is disproportionate to the outcomes achieved.

50) Do you agree with the principles we have set out regarding liquidity? If not, why not and what you suggest as an alternative?

Yes.

51) Do you agree with how we have approached security, profitability, and quality? If not, why not and what you suggest as an alternative?

Yes.

52) Are there other aspects it would be helpful for us to include?

No.

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53) Do you agree with the above considerations? If not, please explain.

You have captured the key considerations. The Code and single code of practice should create better run schemes. However, there is a risk more schemes behave in a similar manner which increases systemic risk.

Also, there is a risk that the Code leads to the accelerated closure of open DB schemes who otherwise would have stayed open.

54) Do you think there are any areas of systemic risk that should be considered further in in light of our draft code? If yes, please explain.

No.

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Fast Track consultation responses

1) Do you agree with how we have positioned Fast Track relative to the code of practice?

Positioning Fast Track separately from the Code as a filter mechanism is a sensible approach to take.

It is clear Fast Track is a view of tolerated risk and not minimum compliance. However, in practice, it is likely to become a key benchmark in ongoing funding discussions between trustees and sponsors.

The positioning of Fast Track no doubt provides greater flexibility to change Fast Track without requiring amendment to the Code. Although, it is our view that Fast Track parameters should not change without particularly good reason. Predictability and stability of Fast Track parameters is required to ensure an efficient funding strategy approach.

Finally, we recommend the assumption Appendices (i.e. 3 and 4) in the draft Code are moved to Fast Track.

2)Are there any aspects of this you think it would be useful for us to clarify further?

Two aspects are:

- How will TPR deal with changes made to Fast Track parameters, in particular, will sufficient notice be provided. For example, will TPR adopt an approach similar to PPF guidance when making updates?
- The level of covenant analysis expected under Fast Track compared to Bespoke?

3) Do you agree that Fast Track should come with a lower level of burden in terms of the explanations required as part of the trustees' valuation submission?

Yes. It is up to Trustees with input from their advisors to determine if Fast Track is the correct route to comply with the Code and an acceptable level of risk for the scheme. Therefore, if Fast Track is chosen after due consideration the explanation required should be less.

Fast Track will be more attractive to smaller schemes if less scheme specific analysis and justification is required (e.g. on the Statement of Strategy, level of covenant analysis, etc).

If TPR wants there to be an incentive for schemes to adopt Fast Track to reduce the level of schemes it has to engage with, it will be important that the compliance burden is lower for those who choose Fast Track.

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4) Do you see any unintended consequences from requiring the scheme actuary to confirm when a submission meets the Fast Track parameters?

We welcome that the Scheme Actuary is not being asked to confirm as to whether, in their opinion, the legislation and the principles in the Code are being complied with.

The Scheme Actuary may come under pressure from stakeholders to adjust assumptions to meet Fast Track especially where they are close to a trigger. However, professionalism and the Code help mitigate the risk that inappropriate assumptions are chosen. That said, areas of assumptions may become uncomfortable for actuaries, e.g.

- low dependency discount rate being 'reasonable' in the context of the investment strategy
- 'appropriate extrapolation' of yield curves
- 'a recent CMI model'

The cost of valuations will undoubtable increase due to the increased responsibility and subsequent risk exposure placed upon the Scheme Actuary.

5) Could we make Fast Track more proportionate for schemes in differing circumstances?

We agree with a proportionate approach for small schemes. However, the definition of a 'small' scheme is too narrow. The definition should be extended to capture asset size i.e. assets less than £25m or less than 100 members. This would help reduce the burden on 'smaller' schemes.

6) Are there other considerations not discussed in the consultation document we should be considering?

No. The Fast Track consultation captures the material points.

7) Do you believe it would be useful to include an additional set of parameters for schemes where the employer has a high insolvency risk? If yes, how should schemes in this category be defined and where should the Fast Track parameters be set?

No. One set of parameters for all simplifies the process and makes it easier to communicate Fast Track. For schemes in distress it is the responsibility of the trustees with input from their advisors to determine if Fast Track is the correct level of tolerated risk or if they should follow the Bespoke route.

8) Do you agree with our approach of setting the Fast Track technical provisions test as a percentage of the low dependency funding basis liabilities? If no, explain why and what would you suggest as an alternative?

Yes. It is easy to understand, communicate and apply.

9) Do you agree with the limits we have proposed? If no, explain why and what would you suggest as an alternative?

The Fast Track funding level limits appear reasonable.

10) Do you agree that for a Fast Track low dependency funding basis measure, the minimum strength of the discount rate basis should be gilts + 0.5% with no inflation risk premium?

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Yes, in the current environment this a reasonable minimum strength low dependency measure.

Please note there will be situations where Fast Track minimum strength basis may not be appropriate due to the covenant strength i.e. the low dependency measure should be, say, gilts flat for a weak covenant. At present these cases would still pass the Fast Track discount rate test.

It will be for TPR to consider whether it is comfortable with the benefits of a simple approach to Fast Track, which may have a lower compliance burden for schemes (and hence more attractive to adopt) versus the risk of a more complex Fast Track approach that ensures the discount rate is appropriate (but with a greater compliance cost). Our preference would be to adopt a simple approach.

11) Do you agree that our approach to other assumptions in the Fast Track low dependency funding basis (as set out in Appendix 1) is reasonable? If no, which assumptions would you suggest are amended and how?

Yes. There is suitable flexibility to incorporate scheme-specifics. However, as noted in Question 1, we suggest moving the detailed assumption appendices from the draft Code into Fast Track.

12) Should we allow more flexibility for smaller schemes in relation to any of the assumptions?

No. The level of flexibility is suitable.

13) Do you agree that the maximum recovery length after significant maturity should be set to three years rather than six? If no, explain why and what you would suggest as an alternative.

Given Fast Track is a filter mechanism, it is ultimately up to TPR to decide, but three years (i.e. one valuation cycle) seems a sensible period in the context of the overall approach.

14) Do you agree with our approach of using the valuation date as the starting point for the recovery plan length?

We agree the valuation date provides consistency across all schemes and removes any incentive to delay the completion of the valuation. Although where experience is allowed for the starting point should be the date to which experience has been allowed.

In addition, the period should be extended to allow for the time to complete the valuation (i.e. 4 and 7 years rather than 3 and 6 years).

15) Do you agree with our approach to how to allow for post valuation experience in Fast Track recovery plans? If no, explain why and what would you suggest as an alternative?

Yes.

16) Do you agree that annual increases to deficit repair contributions should not be more than CPI? If no, what would you suggest as an alternative?

This is a sensible limit given the aim is to set an appropriate level of tolerated risk in the filter mechanism. We assume that if all other Fast Track parameters were met with the exception of this point, it would be relatively straightforward for schemes to pass through the Bespoke route provided they can evidence sound logic behind greater back-end loading.

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17) Do you agree with our approach for the stress test? If no, explain why and what would you suggest as an alternative?

Yes. The approach is familiar to the UK industry and fairly simple to apply in practice.

The stress test where duration is greater than 30 years should be confirmed.

18) Do you agree with the limits we have proposed? If no, explain why and what would you suggest as an alternative?

Stress limits are reasonable.

19) Do you agree with how we have allowed for schemes in surplus within the stress test?

Yes.

20) Do you agree it is reasonable to use the Pension Protection Fund Tier 1 asset classes? If no, what do you suggest as an alternative?

Yes.

21) Do you agree that smaller schemes should not have to produce cash flows to calculate projected duration?

Overall it is appropriate to reduce the burden on smaller schemes, therefore we are supportive of this pragmatic approach.

22) Do you agree with the proxy we have proposed for smaller schemes?

Yes, we are supportive of duration and single equivalent discount rate (SEDR) approach.

Our understanding is that the SEDR could be based on either sample scheme cashflows or a similar duration or actual cashflows.

23) Do you agree with our definition of smaller schemes for this purpose?

It is important to reduce the burden on smaller schemes, therefore we recommend that the small scheme definition is extended in both the Code and Fast Track to capture more schemes. A scheme should be classified as small if it has 100 members or less or the asset size is less than, say, £25m.

24) Do you agree that six years is a reasonable Fast Track parameter for the allowance of extra accrual in open schemes? If no, explain why and what would you suggest as an alternative?

Yes. Based on the objectives of regime this would appear aligned with the expected maximum covenant reliability period under Fast Track.

25) Do you agree with our approach for new entrants? If no, explain why and what would you suggest as an alternative?

Up to the average number of new entrants in the three years preceding the valuation is reasonable.

26) Do you think having no additional restrictions on future service cost will weaken the Fast Track approach significantly?

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No, Fast Track is still a filter of tolerated risk for accrued benefits. The Code is more than sufficient to provide direction and protection for future service benefits.

27) Which of the options for reviewing our parameters do you prefer?

In line with our response to Question 1, our view is option 1 is the appropriate way forward.

28) Do you think a different approach to reviewing our parameters is preferred?

No, although in our view the key is stability and predictability of parameters as possible.

29) What further analysis do you think would be helpful to illustrate the potential impacts of any final Regulations and code?

The analysis you have provided is suitable. Ultimately the impact and behaviours of schemes will come through over time. We recommend that TPR report on those adopting Fast Track vs Bespoke (i.e. an expanded valuation tranche analysis reflecting the new Code / Fast Track).

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