

Summary of the key messages from the 2017 Annual Funding Statement

May 2017

The Pensions
Regulator

Approaching scheme valuations

- The Annual Funding Statement highlights some of the key issues we have identified facing schemes with 2017 valuations.
- Schemes will have been affected differently by market conditions and our analysis has identified groups of schemes which have been impacted in particular ways.
- Trustees and employers should use this statement to identify good practice approaches for their scheme type and take appropriate action.

Market conditions and IRM

- The continuing uncertainty over future economic conditions and the persistent low interest rate environment highlight the importance of effective risk management.
- All schemes need to have contingency plans which should involve taking appropriate action to recover their funding position and to mitigate against any further downside events.

Affordability and managing deficits

Trustees should take appropriate action depending upon the group they fall into as outlined in the table below.

Scheme employer type	Scheme characteristics	We expect trustees
With strong or tending to strong employers	Where the scheme's funding position is on track to meet their funding objectives and where technical provisions are not weak and recovery plans are not unduly long.	As a minimum to continue with their current pace of funding by not extending their recovery plan end dates unless there is good reason to do so.
With strong or tending to strong employers	With a combination of weak technical provisions and long recovery plans.	To seek higher contributions now to mitigate against the risk of the employer covenant weakening and other scheme risks materializing in the future.
With weaker employers	Who assume that they have a strong covenant because they are part of a stronger and larger group of companies but have no formal support in place.	To reduce risk to an appropriate level, or secure additional funding or seek legally enforceable support.

Stressed schemes

- The least detrimental impact for members' benefits in these circumstances may be for the scheme to continue and reach the best possible funding outcome.
- Trustees of stressed schemes need to fully evidence to us that they have taken appropriate measures.

Notifiable events

- Trustees and employers have a duty to notify us in respect of certain circumstances or decisions which may affect the long term security of the scheme.

Valuation assumptions

- Scenario planning and sensitivity analysis are may help given the uncertainty of future economic developments.

Discount rate assumptions

- We expect trustees to seek and duly consider robust advice from their scheme actuary
- When reviewing the discount rate approach, trustees should consider its suitability taking into account their plan for achieving their long-term objective and their current position relative to it.
- Where trustees are looking to change the method we expect them to have a sound rationale behind the change and to document it clearly.
- This also applies where trustees continue to use the same method as before, documenting why the method remains prudent.

Risk management

- Trustees need to monitor risks and take action when required, irrespective of the scheme's funding position.
- Trustees need to have a contingency plan in place and it needs to be agreed with the employer in advance and should be legally enforceable.

The employer covenant

- Trustees should focus on the ability of the employer to contribute cash to the scheme while there remains good visibility of covenant.

Scheme maturity

- Trustees need to have an appropriate cash flow management policy in place.
- Trustees should regularly monitor and assess the scheme's cash flow focusing on the scheme's long term objective

Fair treatment between schemes and shareholders

- We are likely to intervene where we believe that schemes are not being treated fairly.
- Trustees need to ensure that contributions to the scheme feature prominently in their employer's considerations and that its legal obligations to the scheme as a creditor are recognised ahead of shareholders.
- We expect schemes where an employer's total distribution to shareholders is higher than deficit reduction contributions being paid to the pension scheme to have a relatively short recovery plan and that the recovery plan is underpinned by an appropriate investment strategy that does not rely excessively on investment outperformance.