

Is your scheme ready for the new funding code of practice?

The Pensions Regulator's new funding code will mean a **collaborative approach** between employers and trustees will be needed. Employers should therefore look to **proactively engage with trustees ahead of the next funding valuation** to ensure appropriate decisions and long-term targets are made.

This edition of XPS Express is the **first in a series on setting long-term strategies** – look out for future editions.

At a glance

New requirements apply to all funding valuations with an effective date on or after 22 September 2024

For the first time, employers will be required to develop a formal funding and investment strategy

Opportunities exist for employers to take the lead to align long-term strategies with their broader corporate objectives

Covenant is more important than ever, with an assessment now a legal requirement and new concepts introduced

For schemes with increasing liabilities, TPR has previously estimated total contributions could increase by c.£7bn

For these schemes, there are significant risks of bad outcomes for employers who do not engage with trustees

Key risks for employers

Area	Risks	Mitigation steps
Strategy	Agreeing to long-term strategies that increase or create contribution requirements	Early engagement with trustees on long-term strategy and statement of strategy
Covenant	A prudent assessment causing contribution requirements beyond what is necessary	Engage on key areas of the assessment by providing suitable data and metrics
Investment	Too much de-risking that limits possibility of future returns	Discuss with trustees to agree acceptable risk/return for low dependency
Funding	Potential demands reduce other uses of cash (e.g. dividends)	Negotiate recovery plans in context of wider cashflow needs

Covenant importance

Weaker covenant	Stronger covenant
• higher liabilities	• lower liabilities possible
• lower risk investments	• greater investment flexibility
• shorter recovery plans	• longer recovery plans possible
• reduced active member allowances	• increased active member allowances

Key to demonstrating a stronger covenant will be the following new concepts:

Covenant longevity: for how long trustees can be reasonably certain that the employer will be able to continue to support the scheme.

Covenant reliance: for how long trustees can be reasonably certain that they can rely on an assessment of the employer's cash flows and prospects.

Actions employers can take

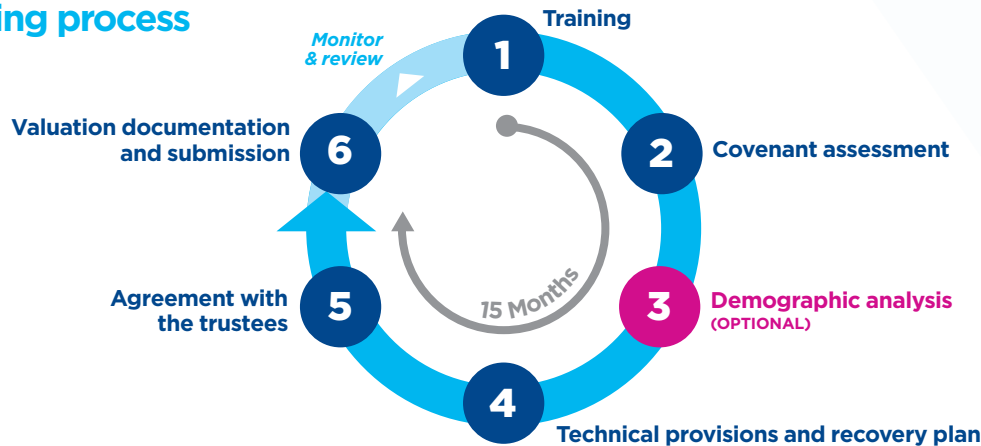
1. Determine how the funding and investment strategy can be aligned with broader corporate objectives.
2. Understand positions under previous and new regime. As part of this, we can help perform a 'Health Check' on key measures such as long-term targets, investments and covenant.
3. Consider how to present covenant and cash positions to trustees, including a consideration of whether independent covenant advice is required.
4. Proactively engage with the trustees as soon as possible to set the future strategy course and ensure outcomes aligned with corporate objectives.

Approach to valuations

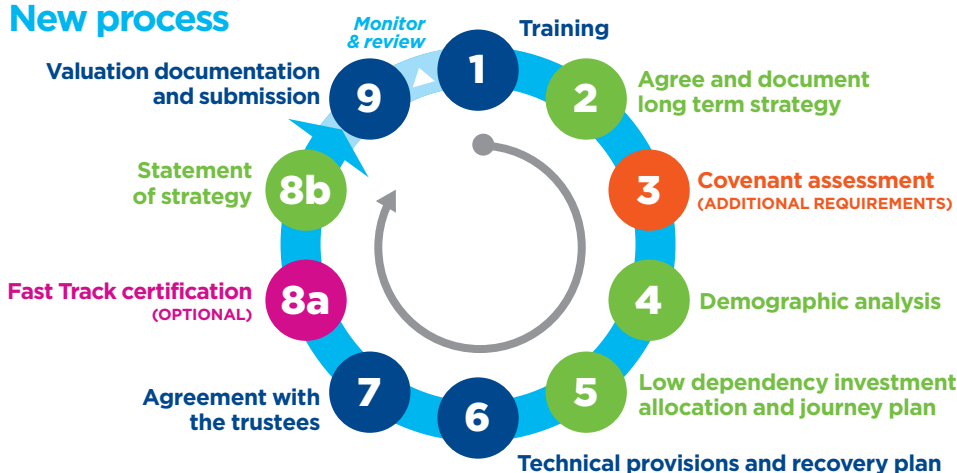
All schemes are now required to have a long-term funding and investment strategy. Central to this is the **requirement to be fully funded on a low dependency basis when significantly mature**, with an objective to invest in a low dependency asset allocation.

The impact of the regulations will vary significantly depending on each scheme's circumstances, but the below diagrams show the increased requirements under the new regime and highlight the importance of taking a proactive approach to upcoming valuations. **Previous valuation timetables are unlikely to allow sufficient time to fully consider new aspects.** We expect most of the discussions with trustees to take place before the valuation date **so early action is key** to ensure employers are prepared for these discussions.

Existing process



New process



Consider in advance of valuation date:

- What long-term strategy would fit with corporate objectives?
- What information can be provided for covenant assessment?

Key

- New requirements
- Additional requirements
- Optional

Upcoming valuations present a **significant opportunity for employers** to engage on their long-term strategies and align them with their wider corporate objectives.

Find out more

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