

A review supported by the
Better Regulation Executive
and National Audit Office

The Pensions Regulator

A Hampton Implementation Review Report

Foreword

Philip Hampton's report: Reducing administrative burdens: effective inspection and enforcement, published in 2005, is one of the cornerstones of the government's better regulation agenda. The principles of effective inspection and enforcement set out in the report, putting risk assessment at the heart of regulatory activity, are designed to encourage a modern regulatory system which properly balances protection and prosperity. Since 2005, the Government has established an expectation that regulators will embed these principles in their approach to regulation.

In November 2006, the Chancellor of the Exchequer invited the National Audit Office and the Better Regulation Executive to develop a process of external review to assess how much progress regulators had made in implementing the principles of Hampton.

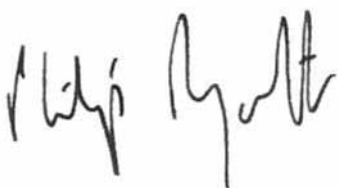
"Hampton Implementation Reports" covering the work of five major regulators were published in March 2008. The review process is continuing. At this point in the cycle we are publishing the results of reviews of two regulators, each of which has a significant impact on its specific economic sector. Together, the Pensions Regulator and Maritime and Coastguard Agency cover a wide range of economic activity, and work to protect our interests. How they carry out their regulatory activities matters.

Full implementation of Philip Hampton's recommendations is a journey that could take several years. This review is a 'snapshot' in time of the progress of each regulator towards his vision.

Each of the reviews found examples of innovation and initiative by regulators who continue to move the regulatory agenda forward, as well as areas for further improvement.

The assessments were carried out by teams of reviewers with wide ranging experience and expertise in the field of regulation. Talking to a wide range of stakeholders, to staff at all levels within the regulator's organisation, through visits to business sites and analysis of data and papers, the Review Teams have reached the findings and conclusions set out in these reports. The reports reflect the judgement of these Review Teams on the basis of the evidence put before them.

We would like to thank all of those who have continued to make these reviews a success. In particular, we are grateful to the regulators and their staff for providing support and making evidence available to the Review Teams, and to all the organisations that generously gave their time to offer evidence to the reviews. Finally, we are extremely grateful to all our reviewers, and their employers, for their involvement, enthusiasm and commitment to this project.



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Summary and conclusions

This is one of a series of reviews of regulatory bodies focusing on the assessment of regulatory performance against the Hampton principles and Macrory characteristics of effective inspection and enforcement. It was carried out by a team drawn from the Better Regulation Executive, the National Audit Office (NAO), the Northern Ireland Trading Standards Service, and the Environment Agency. See Appendix 1 for Review Team membership.

The Hampton Report, published in 2005, is one of the cornerstones of the Government's better regulation agenda and regulators have been working since its publication to embed the principles set out in the Report in their approach to regulation. The review process is designed to identify where a regulator is on the road to full implementation of the principles and the issues each needs to address to become fully Hampton-compliant. This report examines the implementation of the Hampton principles by the Pensions Regulator ("the Regulator").

The Review Team is grateful to the staff at the Regulator for their work before and during the Review, in facilitating our work. Staff throughout the Pensions Regulator participated enthusiastically and helpfully with the Review process.

We are also grateful to the Regulator's stakeholders for their helpful insights into the nature of the sector and the wider context within which the Regulator operates.

What we found

The Review Team concluded that the Hampton principles are thoroughly embedded in the Regulator's work, both at strategic and operational levels. In particular, we were impressed with the way in which risk-based thinking is integrated into the culture of the organisation. Its overall approach is one of continuous improvement, developing systems and services with a view to implementing

an approach which readily identifies and subsequently manages risks in a manner consistent with better regulation principles.

There are factors working in the Regulator's favour here: it is a relatively small regulator with a clearly defined remit, and it is seeking to secure regulatory outcomes which are closely aligned with the incentives of many members of its regulatory community. These include the trustees and administrators of pension schemes and their advisers, and the majority of these will be working within a context set by – in general – good employers that have chosen to set up occupational pension schemes for their staff. Tensions can arise however between businesses' legitimate desire to balance the needs of stakeholders, including shareholders, and the need to meet the financial commitments to their pension scheme.

We found that the Regulator brings a number of specific strengths to its work:

- The Regulator takes a pragmatic approach to regulation. It has been highly responsive in reacting to changing economic circumstances, and in considering the specific circumstances of particular pension schemes when reaching regulatory decisions;
- Stakeholders were particularly complimentary about the quality of the Regulator's consultation processes – they felt that it is a listening organisation, and consults meaningfully, responding to many points raised in consultation processes, and explaining its reasoning in a clear way where it does not accept the arguments put forward in consultation responses;
- The Regulator has developed an effective system for monitoring risks, and for allocating its resources to the most serious issues based upon an assessment of these risks;

- The Regulator has a clear and developing evidence base as a foundation for regulation;
- The Regulator has a learning culture, seeking honest feedback from its stakeholders and routinely publishing meaningful data on its performance.

Looking ahead, the Regulator faces important challenges from the growth of defined contribution-based pensions and the change to the Pensions Regulator's role resulting from the implementation of the Pensions Act 2008. These challenges may require it to adopt different regulatory models for the new measures since its duties will include a requirement to address risks of non-compliance with relatively straightforward duties across all UK employers. The Review Team found the Regulator to be fully alive to the risks and challenges that these significant changes pose.

Issues for follow-up

The following table sets out the key issues that the Review Team believes the Pensions Regulator needs to address to meet the

Hampton criteria more fully, measured against some of the symptoms¹ that we were looking for as evidence of Hampton compliance.

Issue to be addressed	Hampton symptom
<p>Developing effective guidance channels for reaching smaller pension schemes and employers</p> <p>To date, the Regulator has focused the bulk of its efforts on larger defined benefit pension schemes, and has developed a range of innovative and effective means of raising awareness of the law, particularly for scheme trustees. This reflects the balance of risks within schemes.</p> <p>Looking ahead, the Regulator will need to further increase the penetration of its advice and guidance to reach trustees of smaller pension schemes who are less likely to be well versed in the law, and possibly less responsive to their duties under it.</p>	<ul style="list-style-type: none"> There is a strategic approach to the provision of advice and guidance, and appropriate resources are devoted to delivering it.
<p>Communicating the Regulator's approach to the regulation of trust-based Defined Contribution (DC) schemes</p> <p>The Regulator's information and case management systems have been developed largely with the risks associated with defined benefit (DB²) schemes in mind. Its focus on this area to date reflects the scale of the associated risks and the number of pension funds involved. Many stakeholders thought that the risks of DB schemes are very well covered by the existing regime, but that more needs to be done to ensure that regulation of defined contribution (DC) schemes is addressing risks effectively.</p> <p>We discussed the issues with the Regulator's staff, whose strong view is that its approach is robust and appropriate to the distinctive risks involved. The Review found that the Regulator recognises the challenges inherent in the DC landscape and since 2005 has taken a number of relevant steps focusing principally on educating and enabling through codes of practice, guidance and training, and monitoring the impact of this work. Given the long-term trend for employers to move away from DB provision and towards hybrid or DC provision, and the evidence of a parallel shift from trust-based to contract-based schemes, this is likely to become a more significant issue in the coming years.</p> <p>Changes to the regulatory regime in 2012 are also likely to result in the creation of a very significant number of new DC schemes. The Review welcomes current work to establish a formal strategy</p>	<ul style="list-style-type: none"> There is a strategic approach to the provision of advice and guidance, and appropriate resources are devoted to delivering it.

¹ From Hampton Implementation Reviews: Guidance for Review Teams, National Audit Office and Better Regulation Executive, May 2007

² An explanation of DC and DB schemes can be found at page 10

Issue to be addressed	Hampton symptom
<p>group involving DWP, the Pensions Regulator, HM Treasury and the Financial Services Authority to strengthen arrangements for joined up and effective regulation of DC pensions. This is similar to the joined-up DWP, the Pensions Regulator and Pension Protection Fund (PPF) “tripartite” group in place for the regulation of DB pensions. It will be important that the Regulator plays a full role, commensurate with industry and stakeholder expectations.</p> <p>We recommend that the Regulator do more to communicate its thinking about the handling of the risks inherent to trust-based DC schemes. We welcome in particular the publication of the first in a series of annual analyses of data in relation to trust-based schemes.</p>	
<p>Clarity on the Regulator’s approach to its new responsibilities for regulating employer compliance under the Pensions Act 2008</p> <p>The implementation of the Pensions Act 2008, in 2012, will create a significant change in the pensions regime, and a significant departure for the Regulator from the way it has operated in the past as it takes on new responsibilities to regulate employers’ duties under the Act.</p> <p>We discussed the Regulator’s plans and found that it understands the scale of the challenges it faces and is alive to the need to demonstrate it is managing the uncertainty associated with adapting to this new role. We have made a number of comments on this point throughout this Report.</p> <p>Many stakeholders emphasised the scale of the task confronting the Regulator as it is developing plans for implementation of its new responsibilities in relation to the new employer compliance regime, and expressed concerns that this could affect the quality of its existing regulatory work.</p> <p>Many of the choices facing the Regulator will depend on completion of the legislative process to implement the Pensions Act 2008, which is currently under way. Nevertheless, we would encourage the Regulator to share its emerging thinking with stakeholders on how it proposes to deal with the new provisions and manage the associated risks as soon as possible.</p>	<ul style="list-style-type: none"> • There is transparency in the decision-making process

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Introduction

The Pensions Regulator

- 1 This review of the Pensions Regulator aims to provide a structured check on performance against the principles and characteristics set out in the Hampton and Macrory reports (see Appendix 2). The Team reviewed the Regulator against a performance framework³ developed by the Better Regulation Executive and the National Audit Office (NAO), which provides a guide for reviewers on the kind of evidence to look for and questions to consider. However, the process is not the same in scope or depth as a full value for money audit of economy, efficiency and effectiveness and the Review Team's conclusions are based on a combination of evidence and judgement. A brief description of the scope of the Review and methods employed is at Appendix 3.
- 2 The Pensions Regulator is the UK regulator of work-based pension schemes. This covers any scheme that an employer makes available to employees, including all occupational schemes and any stakeholder or personal pension schemes where employees have direct payment arrangements. Its website gives the following high level statement of its purpose and objectives:

“Working to improve confidence in work-based pensions by protecting members' benefits and encouraging high standards and good practice in running pension schemes.”
- 3 The Pensions Regulator is a statutory Non-Departmental Public Body sponsored by the Department for Work and Pensions (DWP).
- 4 The Regulator was established in April 2005, replacing the previous occupational pensions regulator, the Occupational Pensions Regulatory Authority (OPRA). Its creation was one of the key elements of the Pensions Act 2004 (PA 2004), which also set out the main objectives of the Regulator, as follows:
 - to protect the benefits under occupational pension schemes of, or in respect of, members of such schemes;
 - to protect the benefits under personal pension schemes of, or in respect of, members of such schemes;
 - to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (PPF), and;
 - to promote, and to improve understanding of, the good administration of work-based pension schemes.
- 5 The Regulator has been given an additional objective under the Pensions Act 2008 to maximise employer compliance with the employer duties introduced through that Act and with the safeguards against prohibited recruitment conduct and inducements to opt out of pension saving.
- 6 Its budget for 2009-10 is £28.2 million. Its income is largely derived from a levy on occupational pension schemes that are required to register with the Regulator under the 2004 Act. This general levy also covers the costs of the Pensions Ombudsman, the Pensions Advisory Service, the legal assistance scheme for the Pensions Regulator Tribunal and any grants made to advisory bodies. The Regulator collects this general levy. The Regulator's activity in respect of its objectives under the Pensions Act 2004 is funded by grant-in-aid from DWP

³ Hampton Implementation Reviews: Guidance for Review Teams, National Audit Office and Better Regulation Executive, May 2007

with running costs recovered through a general levy on pension schemes. Total grant-in-aid for 2008-09 was £25.3m.

- 7 The development of the Regulator's new Employer Compliance Regime (ECR) to meet its new objective under the Pensions Act 2008 is separately funded from Government expenditure. The grant-in-aid in respect of this activity was £7.2m in 2008-09 and the budget for 2009-10 is £13.6m.
- 8 The Pensions Act 2004 makes provision for the composition of the Regulator Board. The Chair of the Board is David Norgrove. The Board also comprises six non-executive members, the Chief Executive, Tony Hobman, and four executive directors. On 31 March 2009, the total number of staff was 333.
- 9 The Pensions Regulator is one of a range of bodies with pensions responsibilities. The text box below explains the functions of some of its main partners.

Work-based pensions

- 10 The Regulator's role is restricted to the regulation of pensions which are offered or facilitated by employers. It has no responsibility for the regulation of non-work based pensions: that is, it has no role in relation to the Basic State Pension, the State Second Pension (where DWP is responsible) and individual personal pensions (which are the responsibility of the Financial Services Authority). It also has limited responsibility in respect of public sector pensions.
- 11 A range of pensions are covered by its remit. Defined Benefit (DB) schemes typically pay the scheme members a proportion of their final salary on retirement. Money purchase (or Defined Contribution, or DC) schemes typically pay out a sum based on the value of the member's fund at the time of retirement. There is a well-established trend away from the provision of DB and towards the provision of DC-based occupational schemes. Some employers also offer hybrid schemes which offer a pension based on a combination of final salary and returns on investments made by the scheme member.
- 12 Most of the pension schemes involved are trust-based: that is, schemes where the assets are held by one or more persons (trustees) for the benefit of the members of the scheme. Trust-based schemes can take the form of defined benefit, or defined contribution, schemes.
- 13 Employers may also have a role in contract-based schemes (where there are no trust-based arrangements, and where the pension is, generally speaking, managed by an insurance company). Contract-based pensions are more akin to personal financial services, and the FSA also has a regulatory role in these cases. The risks, and therefore the regulatory issues, associated with each form of work-based pension are different.
- 14 The Regulator's Annual Report 2008-09 estimated that there are currently some 19.94 million members of workplace private pension schemes.
- 15 As of 31 March 2009, membership of private sector occupational DB schemes stood at 8.6 million, and that of private sector trust-based DC schemes stood at 1.54 million. There were a further 6.62 million memberships of private sector hybrid schemes which have both DB and DC scheme members. There were (in 2008) 3.18 million memberships of contract-based (group personal, group stakeholder, and group self-invested personal) pension schemes.

The regulatory framework

- 16 Regulatory provisions relevant to its work are derived from the Pensions

OTHER BODIES WITH PENSION RESPONSIBILITIES

The Department for Work and Pensions (DWP) is responsible for implementing Government pensions policy and reform, and has responsibility for the legislative framework which governs the Pensions Regulator.

Like the Pensions Regulator, the **Pension Protection Fund (PPF)** was established by the Pensions Act 2004. The PPF's main function is to provide compensation to members of eligible defined benefit and hybrid pension schemes, when there is a qualifying insolvency event in relation to the employer, and where there are insufficient assets in the pension scheme to cover the PPF levels of compensation. The PPF is funded by an administration levy on eligible schemes, collected by the Regulator. This is separate from the general levy which funds the Regulator. The PPF collects a risk-based levy from schemes to help fund PPF compensation. The quantum of the levy is informed by data collected in the Regulator's scheme return and on other factors set out each year by the Pension Protection Fund as required under section 175 of the Pensions Act 2004.

The Financial Assistance Scheme (FAS) offers help to some people who have lost out on their pension because they were a member of an under-funded defined benefit scheme that either:

- a) started to wind-up between 1 January 1997 and 5 April 2005, and:
 - (i) did not have enough money to pay members' benefits, and
 - (ii) the employer cannot pay the shortfall because it is insolvent, no longer exists or no longer has to meet its commitment to pay its debt to the pension scheme.

or

- b) started to wind up after 5 April 2005 but is ineligible for help from the Pension Protection Fund due to the employer becoming insolvent before this date."

Assistance is also payable to the survivor of a pension scheme member and to certain surviving dependants.

On 10 July 2009 responsibility for the management and administration of FAS was conferred from the DWP to the Pension Protection Fund.

The Board of the PPF is also responsible for the administration of the **Fraud Compensation Fund (FCF)**, which provides compensation to occupational pension schemes where the sponsoring employer is insolvent and the scheme has suffered a loss that can be attributable to dishonesty. This responsibility was inherited from the Pensions Compensation Board on 1 September 2005.

The **Financial Services Authority (FSA)** regulates firms that provide, promote, market, advise on or sell personal (including stakeholder) pensions and annuities. Work place contract-based schemes fall under the remit of both the FSA and TPR. However, their primary stakeholder groups are different: the FSA focus is on providers and advisers whereas TPR's main focus is on the employer and the administration of the pension scheme.

The **Pensions Ombudsman**'s role is to investigate and decide pension complaints between members of pension schemes (including personal pensions) or their beneficiaries, employers, trustees, managers and scheme administrators. It is independent, and settles specific pension complaints. It was established in April 1991. The Pensions Ombudsman is also appointed as the Pension Protection Fund Ombudsman (PPFO). PPFO work is handled from the same office as the Pensions Ombudsman's work. The PPFO can deal with disputes in relation to the PPF and the Financial Assistance Scheme:

- the PPFO is responsible for investigating PPF reviewable matters and complaints of maladministration by the PPF Board.
- the PPFO can consider appeals against decisions made by the scheme manager under the Financial Assistance Scheme's internal review procedure.

The Financial Assistance Scheme (FAS) offers help to some people who have lost out on their pension because:

- they were a member of an under-funded defined benefit scheme that started to wind up between 1 January 1997 and 5 April 2005, and either:
 - their scheme began to wind up (ended) and did not have enough money to pay members' benefits, and;
 - the employer cannot pay the shortfall because it is insolvent, no longer exists or no longer has to meet its commitment to pay its debt to the pension scheme.

The scheme is managed by the DWP and is administered by the FAS Operational Unit (FAS OU). It makes payments to top up scheme benefits to eligible members of schemes that are winding up or have wound up.

The **Personal Accounts Delivery Authority** (PADA) is also a DWP NDPB, created to deliver a new occupational pension scheme that employers may use to fulfil their duties under the workplace pension reforms being introduced from 2012. This pension scheme, previously known by the working title 'personal accounts', will be called NEST (National Employment Savings Trust). PADA is a time-limited organisation which will hand over the management of NEST to a new organisation called the NEST Corporation.

Act 1993, the Welfare Reform and Pensions Act 1999, the Pensions Act 1995, the Pensions Act 2004, and the Pensions Act 2008.

- 17** The Pensions Act 1995 was enacted in the aftermath of the Maxwell pensions scandal. It set rules for the funding of occupational pension schemes, and created a regulator, the Occupational Pensions Regulatory Authority (OPRA). By the early 2000s, there was a widespread perception that the regime created by the 1995 legislation was failing to offer the protection to pension scheme members that had been anticipated. In particular, OPRA was perceived as being reactive and insufficiently risk-based. Its powers were also found to be limited. There were also perceived failures with the wider regulatory framework, in particular, its funding requirements had not prevented some pension schemes winding up with insufficient assets to secure their liabilities amidst considerable publicity.
- 18** The Pensions Act 2004 introduced a new regulatory framework, and a number of new bodies with powers of oversight and intervention, including the Pensions Regulator. Key elements of the framework introduced by the Act and overseen by the Pensions Regulator are summarised below:

Anti-Avoidance Powers

- 19** The Pensions Act 2004 also established the Pension Protection Fund (“PPF”), which operates to compensate pension scheme members who have lost (or may lose) their pension entitlement as a result of a sponsoring employer of their defined benefit pension scheme becoming insolvent.
- 20** In order to protect against claims on the PPF, the Pensions Act 2004 introduced new anti-avoidance provisions. The two

main anti-avoidance powers available to the Pensions Regulator are:

- Contribution Notices, which require payments to be made to a scheme or to the PPF by employers or someone associated or connected with the employer. A Contribution Notice requires the recipient to pay a specified amount of money to the pension scheme; and
- Financial support directions which may be served on an employer or someone who is connected or associated with the employer, which would require that the recipient put in place appropriate financial support for an occupational pension scheme, where the sponsoring employer of the scheme is a service company, or is insufficiently resourced.

Funding arrangements for Defined Benefit (DB) Schemes

- 21** The Pensions Act 2004 replaced the “minimum funding requirement” which had been a feature of the regime for DB schemes under the previous legislation with new scheme-specific funding arrangements. The intention behind the new requirements was to adapt regulation more flexibly to individual schemes’ circumstances whilst at the same time protecting members’ benefits. Schemes are now required to hold sufficient and appropriate assets to cover their ‘technical provisions’ i.e. an estimate made on actuarial principles of the assets needed at any particular time to make provision for benefits already accrued under the scheme. These include pensions in payment (including those payable to survivors of former members) and benefits accrued by other members which will become payable in the future.
- 22** The Pensions Act 2004 created a voluntary “Clearance” process which enables an employer to gain assurance, in the form of a clearance statement from the regulator,

that it is not at risk from these anti-avoidance powers before undertaking a specific corporate transaction that could be detrimental to the pension scheme.

Internal controls

- 23** The Pensions Act 2004 included a range of provisions to improve internal controls, with a view to protecting members' benefits. These controls must be sufficient to ensure that the scheme is administered and managed in accordance with the scheme rules and the relevant legislation.

Trustee knowledge and understanding

- 24** The trustee knowledge and understanding requirement states that individual trustees of an occupational pension scheme must have appropriate knowledge and understanding of the law relating to pensions and trusts, the principles relating to the funding of occupational pension schemes and the investment of the assets of such schemes.

The Pensions Act 2008: the Employer Compliance Regime (ECR)

- 25** This framework underpins the Regulator's existing responsibilities. It will acquire new responsibilities from 2012. When implemented, the Pensions Act 2008 will introduce new requirements on employers to automatically enrol workers who meet age and earnings criteria into a pension scheme, and pay a minimum three per cent contribution. The Act gives the Regulator responsibility for maximising employer compliance with these requirements, and new enforcement powers to enable them to deliver this role.

The Hampton vision

26 Both the Hampton and Macrory reports are concerned with effective regulation – achieving regulatory outcomes in a way that minimises the burdens imposed on business. Key to this is the notion that regulators should be risk-based and proportionate in their decision-making, transparent, accountable for their actions and should recognise their role in encouraging economic progress.

Risk-based

27 The Pensions Regulator was set up to mitigate a number of key risks posed in the occupational pensions sector. These differ according to scheme type, but key risks include:

- In DB schemes the principal risk to members is that the scheme has insufficient funds to meet the promised level of income on retirement and the sponsoring employer is unable to make up the deficit. Alongside this, the Regulator focuses on the risks, to members and to the PPF, of employers seeking to avoid their pension liabilities.
- DC schemes do not promise a particular level of pension to be paid on retirement. The principal risks are to members, rather than employers. These relate mostly to a lack of understanding of the levels of contributions needed to ensure an adequate pension on retirement, or insufficient understanding of the options open to them at the point of retirement, and issues relating to the governance and administration of schemes.

28 With DC schemes, there is some overlap with the work of the FSA which has a general responsibility for increasing consumer understanding of financial services.

29 The need for a truly risk-based occupational pensions regulator was prominent in debates at the time of the Regulator's creation. The Pensions Regulator has placed a high strategic priority on focusing its efforts on areas where the risks are most acute. An understanding of risk imbues its work both at strategic and operational levels. The section on "Inspections" below addresses the Regulator's risk-based case management system.

30 A risk-based regulatory framework is dependent on high quality information. The reporting structure created by the Pensions Act 2004 has given the Regulator a very strong picture of performance and risks across DB pensions schemes. Schemes are required to submit regular returns, and recovery plans, in cases where they are in deficit. Schemes and sponsoring employers are also required to inform the Regulator of certain notifiable events which suggest that there may be a risk of a call on the PPF being made. Additionally, there is a whistleblowing duty on all those involved in running pension schemes to report suspected breaches of the law to the Regulator. The annual publication (published jointly by the Regulator and the PPF), the "Purple Book" (*DB Pensions Universe Risk Profile*) reflects this strong evidence base.

31 Some of the stakeholders that we spoke to were less convinced that there is a strong a system of risk management in place to deal with DC schemes. There are risks that are likely to become more prominent given the long-term trend towards DC provision: many of these impact on individual members, but there are risks for employers as well. The administration of DC schemes is also complex and there is a risk of costs to employers where mistakes need to be rectified. Some stakeholders

argued that more could be done within this area. We discussed the position with senior management in the Regulator, who put it to us that the regulatory issues have taken longer to “unpack” here than in the DB context where the issues are clearer, and more widely recognised.

- 32** The Review Team welcomes the fact that the Regulator has embarked on a series of annual publications relating to DC scheme data.
- 33** We have a number of comments about the handling of DC regulation throughout this report.

We found that:

- **The Pensions Regulator has made considerable progress in working as a risk-based regulator, particularly with regard to DB Schemes.**
- **The Pensions Regulator’s development of systems for allocating operational resources to issues in proportion to the risks that they present is particularly impressive.**
- **The systems and structures for managing risks to DC pensions do not at present inspire the same levels of confidence and assurance amongst some stakeholders.**

Good practice: Continuous improvement and focus on emerging risks

The Pensions Regulator is committed to continuous improvement as a means of helping all staff to identify and develop ideas to improve the performance of the organisation.

More broadly, the Regulator acknowledges the need for continuous improvement at an operational level. In particular, it is focused on refining, on an ongoing basis, its approaches to identifying and addressing risks to pension schemes, as well as the business rules and staff training which support this process.

This focus is embedded in the Regulator’s operational approach. For example, its regulatory practice teams hold regular meetings across case teams to enable discussion, sharing of knowledge, identification of broader trends and risks etc. The regulator also uses software to capture, update and store case information and learning points from cases. These practices help ensure a consistent approach over time, and enable the Regulator to learn lessons and update operational policies, business rules and processes etc where appropriate. The Regulator has also used continuous improvement techniques to focus on operational efficiency, delivering considerable internal cost savings which have enabled it to respond effectively to the risks to pension schemes in the downturn, without significantly increasing its budget (funded by a levy on pension schemes).

Moreover, the Regulator proactively seeks to identify emerging risks and develop regulatory responses, where necessary and appropriate. Good recent examples of this are:

- analysis work undertaken by the Regulator to ensure that its scheme-specific regime for regulating the funding of Defined Benefit pension schemes remains fit for purpose in the economic downturn; and
- a review, now underway, of risks to defined contribution schemes to examine how the Regulator’s approach might need to evolve in light of changes to the pensions landscape.

Transparency and Accountability

- 34** We were struck by the extent to which stakeholders were consistent in their view that the Regulator is a transparent, open, organisation. Its approach to consultation, in particular, was praised. We have some relevant comments under ‘Design of Regulations’ below.
- 35** There have been concerns in the past about the amount of detail that the Regulator has been prepared to publish about its decision-making in specific circumstances. There are reasons why it may be inappropriate to publish decisions: the regulatory system that it oversees is deliberately designed to allow for a flexible approach which is specific to the circumstances of particular schemes. The Regulator has therefore been conscious of the need to avoid giving the impression that there is only one approach which is acceptable to the Regulator. However, it is starting to develop anonymised case study material which is helping give practical guidance to pensions schemes while avoiding this risk. See relevant comments under ‘Sanctions’ below. The Pensions Regulator Board’s policy is to publish all Determinations Panel decisions unless there are good reasons not to do so. It has done this online, including retrospectively, following a recommendation from the Public Accounts Committee in 2007.
- 36** The Regulator also attaches importance to developing an open, evidence-based debate about regulation and the associated issues within the sector. It has published comprehensive annual analyses of issues raised by DB schemes, and is starting to develop comparable work on the DC side.
- 37** We were also impressed by the extent to which the Regulator has opened itself up to wider engagement, and to external challenge. At the time of the Review, the Regulator was in the middle of a

campaign focusing on the regulation of DB schemes and, in particular, dealing with issues for these schemes raised by the economic downturn. This involved a series of national workshops to engage with stakeholders, principally trustees and others involved in DB schemes, to reaffirm its approach to DB scheme funding in the economic downturn. The Regulator also publishes an annual survey about its work, the “perceptions tracker”, which analyses views from its stakeholders, including the regulated community, about the whole range of the Regulator’s work. It contains open and meaningful questions about its work in practice and the results form a key part of management information within the Regulator.

- 38** The Regulator also has an Advisory Panel, a quarterly forum that involves a range of major stakeholder representatives, including employer representatives, from across the Pensions Community.

We found that:

- **The Regulator’s stakeholders regard it as a transparent and listening organisation.**
- **The Regulator has been open to external comment and challenge on its work.**

Economic Progress

- 39** The regulatory model behind the Regulator’s work is unusual; it works to secure the interests of members of pensions schemes that employers have chosen to set up.
- 40** This generally means that it regulates schemes sponsored by larger employers with a commitment to their staff. The viability of defined benefits pension schemes is dependent on employers’ continued solvency. To an unusual

degree, therefore, the achievement of its fundamental objectives depends on the continuing vitality of the companies that are subject to regulation. The Regulator therefore has a strong incentive to regulate in such a way that unnecessary burdens on schemes and employers are reduced. As a result, it places high importance on a pragmatic and flexible approach to regulation in practice.

- 41** The Pensions Regulator regulates in a complex area, and needs to keep abreast of developments in the pensions field and in the wider economy. It has deliberately adopted a policy of inward secondment to secure a strong basis of understanding of conditions within the sector. Over 100 secondees have worked at the Regulator since this programme was launched in 2006 and secondees currently make up around 5% of the workforce. The Regulator also actively recruits non-secondee staff from a variety of relevant backgrounds.
- 42** We found that the Regulator is also responsive to specific developments in markets. We reviewed the Regulator at a time when the economic effects of the downturn on pension schemes were starting to become apparent. There had been significant impacts, both on the viability of particular employers and, given stock market movements, on the assets of schemes that they sponsor. In this context, the way in which the Regulator exercises its responsibility for approving recovery plans for DB schemes which are significantly in deficit is a matter of critical importance for companies. The Regulator was in the midst of a campaign to raise awareness of the issues involved through a series of statements about its approach to regulation of DB schemes in the context of the downturn. It stressed its commitment to adopting a flexible approach in assessing recovery plans given the other pressures on many employers, and encouraged employers

to discuss cases with pension scheme trustees where they thought an existing recovery plan had become unaffordable.

We found that:

- **The Regulator has a strong grasp of the economic issues facing the sector it regulates, and takes a pragmatic approach to the use of its powers.**
- **The Regulator has been responsive in reacting to the business needs of the regulated community.**

Design of regulations

Hampton principle

“All regulations should be written so that they are easily understood, easily implemented, and easily enforced, and all parties should be consulted when they are being drafted”

“When new policies are being developed, explicit consideration should be given to how they can be enforced using existing systems and data to minimise the administrative burden imposed”

Key findings:

- The Regulator’s approach to consultation is widely regarded by stakeholders as effective and meaningful.
- The Regulator plays an active role in the development of policy with partners, both in central government and the EU.
- The Regulator has co-ordinated its work well with its major delivery partners and other regulators; more could be done by all parties, however, to present ‘joined-up’ information for the general public who may not be aware of its specific responsibilities.

Background

Context

- 43** The Regulator works closely with a number of bodies in the delivery of its objectives. These include the PPF, reflecting its statutory responsibilities to minimise calls upon the fund, and the Financial Services Authority, with its shared interest in aspects of DC scheme regulation.
- 44** The Regulator has a number of mechanisms for consulting stakeholders on its developing policies: key stakeholders take part in a quarterly Advisory Panel, and more informal discussions also play an important part.
- 45** DWP has overall responsibility for the legislative framework within which the Regulator operates. It was responsible, for instance, for the Pensions Acts and was (at the time of the Review) working on statutory instruments which will provide the detailed legal framework

under which the Pensions Regulator will regulate employers’ compliance with their duties under the Pensions Act 2008.

Codes of Practice

- 46** The Regulator’s main responsibility in relation to the design of regulation (as defined for the purposes of the Hampton Implementation Reviews) has been performed under its power to issue Codes of Practice under the Act which do not have legislative effect; the Regulator explains this function as follows:

“Codes of practice are not statements of the law and there is no penalty for failing to comply with them. It is not necessary for all the provisions of a code of practice to be followed in every circumstance. Any alternative approach to that appearing in the code of practice will nevertheless need to meet the underlying legal requirements, and a penalty may be imposed if these requirements are not met. When determining whether the

legal requirements have been met, a court or tribunal must take any relevant codes of practice into account.”

- 47** The Regulator is empowered to issue Codes under sections 90-92 of PA 2004; indeed the Act requires them to do so in certain circumstances. Echoing the above explanation, the Act also specifies that failure to follow a Code is not in itself an offence, but must be considered in any legal proceedings. Codes of Practice have been issued on a range of subjects (for instance, Internal Controls). The Codes are subject to approval by the Secretary of State for Work and Pensions, and must be laid before Parliament before they come into effect.

Review Findings

The Regulator’s approach to consultation is widely regarded by stakeholders as effective and meaningful

- 48** While DWP is formally responsible for much of the regulatory framework, the Regulator has developed a number of Codes of Practice and other documents which have a practical impact upon the way in which pension schemes are regulated in practice. For instance, in recent months statements for the guidance of trustees and employers about the Regulator’s approach to issues raised by the economic downturn have been published.
- 49** The stakeholders that we interviewed were generally consistent in their view that the Regulator consults meaningfully in the development of such documents, and takes their views seriously. The Pensions Regulator, like many other regulators, has signed up to the Government’s Code of Practice on Consultation. However, stakeholders felt that the informal aspects of the relationship worked particularly well: there was some scepticism about the nature of communication through
- the more formal mechanisms, like the Regulator’s Advisory Panel, but the overall relationship was deemed to be strong. The keynote of the relationship appeared to be one of trust, and stakeholders said that the Regulator is willing to share developing proposals with experts from many key stakeholder groups informally at an early stage in the process, and responded meaningfully to comments they made in the process. This did not mean that the Regulator would inevitably change its position on important issues, but rather that it generally gave a clear account of its reasons in instances when it did not change its view.

The Regulator plays an active role in the development of policy with partners, both in central government and the EU

- 50** At the time of the Review, DWP was in the process of drafting statutory instruments which will give effect to the Employer Compliance Regime in 2012. We found that the relationship with DWP appears to work well, with a clear demarcation of responsibilities. DWP takes the Regulator’s expertise in the occupational pensions sector seriously, and the Regulator staff that we spoke to said that the sponsor Department had been responsive to issues raised by them.
- 51** EU law also has an impact on the regulatory framework within which the Regulator operates. The profile of occupational pensions in the UK differs strongly from most other European models, which means that work by the Regulator to influence the EU agenda is particularly important. Its Chief Executive is chair of the Occupational Pensions Working Group of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), which is composed of high level representatives from the insurance and occupational pensions supervisory authorities of the EU Member States,

and the Regulator has also played an effective role, alongside HM Treasury and DWP, in negotiations to secure European legislation which acknowledges the distinctive character of UK pensions provision, including by ensuring that occupational pensions are not covered by the Solvency II Directive which is due to come into effect from 2012.

The Regulator has co-ordinated its work well with its major delivery partners and other regulators; more could be done by all parties, however, to present ‘joined-up’ information for the general public who may not be aware of its specific responsibilities

- 52** One of the major challenges facing those responsible for pensions policy and regulation is the level of public understanding of pensions. From the Regulator’s perspective, this is likely to become more important given the current trend towards DC schemes, where individual choices are important and where responsibilities are divided between the FSA and the Pensions Regulator.

- 53** The relationship between FSA and the Regulator appeared to be working well: they have published a clear public statement setting out how their regulatory regimes overlap and how they work together. However, a number of stakeholders felt there needed to be more co-ordination of work to raise awareness amongst the wider public. Going forward, high quality information will be needed for individuals who have no background in pensions administration, which will need to be as clear and free of jargon as possible. This includes information about the law, but also about the respective roles of the regulatory bodies concerned. The Pensions Regulator is beginning to work more intensively with employers and DC pension schemes to improve the quality of information available to scheme members in making such choices. We would encourage the Regulator, DWP, HM Treasury and FSA to continue to work together to address this issue.

Advice and guidance

Hampton principle

“Regulators should provide authoritative, accessible advice easily and cheaply”

Key findings:

- **The Regulator has used innovative approaches to raise trustees’ understanding of the requirements that the law places on them.**
- **The Regulator will need to explore means of reaching smaller schemes and employers.**
- **The Regulator’s stakeholders feel able to approach it about specific issues without fear of adverse consequences.**
- **The Regulator’s website is well structured, but needs more signposting.**

Background

54 The Regulator’s website (www.thepensionsregulator.gov.uk) contains a range of guidance broken down by likely user group. These groups include trustees, employers, and scheme members.

55 In many respects, trustees of pension schemes act as the primary guardians of members’ interests, with the Regulator standing behind them. In trust-based schemes, they are responsible for day-to-day oversight of the scheme’s management. Their task has in many ways become more complex as pensions provision has itself become more complex. To a large extent their duties derive from wider trust law, but the Pension Act 2004 imposed new requirements upon them in terms of knowledge and understanding of the law.

56 The quality of advice and guidance offered to trustees by the Regulator is critical to the achievement of its objectives. Guidance needs to give a clear statement of the law, provide support to trustees and others in understanding their complex responsibilities and give scheme members confidence that the

regulatory regime is protecting their interests (in an atmosphere where many of the public are sceptical about the benefits of pensions). The subject matter is inevitably technical and complex.

57 A number of the Regulator’s “products” are relevant to its role to support trustees. The relevant Code of Practice sets out the basic legal position, and guidance documents accompany it, and there is additional guidance available on trustees’ duties and responsibilities. The Regulator has also developed a “Trustee Toolkit”, a free and interactive e-learning facility, which offers a modular programme of learning covering the scope of the requirement in the Pensions Act 2004 for trustees to be conversant with their schemes and to have appropriate knowledge and understanding.

58 As part of its “educate and enable” approach the Regulator has adopted a campaigns strategy to ensure that the emphasis of its communications and wider engagement with the pensions community is focused on each of the core strategic themes in its corporate plan for 2009-12. These are: risks to DB schemes, risks to DC schemes, improving standards of governance and administration, and

delivering the Employer Compliance Regime and preparing for 2012. To do this it groups its products (guidance etc) into logical groups and promotes related messages to specific audiences through a range of channels at specific times. The objective is to give stakeholders clear and consistent sets of messages and ultimately to drive behavioural change in line with the Regulator's objectives.

- 59** For employers, advice on the use of the Regulator's anti-avoidance powers (see page 13) is particularly important. As well as general guidance in the form of Codes of Practice, the Regulator offers a bespoke "clearance" service. This is an unusual service based on provisions in s42 and s46 of the Pensions Act 2004, which allow applications to be made to the Regulator for assurance that formal action will not be taken by it in specific circumstances. Certain types of corporate transactions can be detrimental to members' benefits in DB schemes, and can result in calls on the PPF. The Regulator's "anti-avoidance" powers are designed to guard against these situations. Where it considers that there has been a deliberate attempt to avoid pension liabilities, the Regulator can issue a contribution notice requiring payment of any amount up to the full buy-out debt. This can be a very significant power, and a voluntary clearance procedure was introduced to provide more certainty for businesses considering such transactions, who can gain certainty, through a clearance statement issued by the Regulator, that it will not use its anti-avoidance powers in relation to the specific circumstances described in the application for clearance. It should be noted, however, that should circumstances change, or should undisclosed material information come to light, the Regulator might then exercise its powers.
- 60** As well as guidance on its own areas of responsibility, the Regulator's website has a Frequently Asked Questions

section which, as well as providing basic information on the Regulator's work, directs those accessing its website to the relevant body (for instance, it directs those with a query about a possibly mis-sold pension to the Financial Services Authority). It also hosts a Customer Support telephone line.

Review Findings

The Regulator has used innovative approaches to increase trustees' understanding of the requirements that the law places on them

- 61** The Regulator places a high priority on education as its main means of securing good regulatory outcomes and compliance with the law. It has deliberately sought to work through trustees as co-regulators. Trustees' responsibilities are complex, however, and the Review Team was impressed by the range and quality of the material that the Regulator has supplied for their use. Much of this is available in "plain English" on the website, and also at workshop events that the Regulator organises as part of its unfolding series of campaigns.
- 62** We found the Trustee Toolkit to be a significant example of regulatory good practice. It is free to subscribers (available at <http://www.trusteetoolkit.com>), and presents a series of modules introducing trustees to their roles and responsibilities. There are different learning paths through the toolkit so that, for example, trustees of small, fully insured schemes only have 6 modules to complete of the 11 available. The toolkit is also designed to allow experienced trustees to skip over tutorials they already know and can test themselves against the assessment questions at the end, potentially further reducing the time such trustees will need to invest. Learning can be handled at the user's own pace. Modules include general introductions to Trust Law and Pensions Law as well as more detailed guidance

Good practice: The Trustee toolkit

The Trustee toolkit forms part of the Pensions Regulator's focus on education, as part of an approach described as *"educate, enable and enforce only where necessary"*. It is a free, online training package to help trustees to access the learning they need to meet their legal requirements for trustee knowledge and understanding, introduced in the Pensions Act 2004. It is freely accessible on the Internet, and can be completed individually, at the user's own pace.

It was developed with the trustee community, and others involved in pensions provision, in response to a gap in the market for trustee training and provides a flexible, modular training tool with role plays, tutorials and case study examples. It has been very successful – it has some 30,000 registered users and a 98% satisfaction rating. Much of the Trustee toolkit is relevant to both defined benefit and defined contribution schemes, but specific modules and tutorials are provided covering each type of scheme. The toolkit then enables trustee users to tailor their learning path to the type of scheme relevant to them.

A certificate is provided to those who have completed the toolkit, and while this does not represent a formal qualification, the toolkit should provide the learning required to then complete the Pensions Management Institute's award in Pensions Trusteeship. Indeed, the toolkit is part of a wider framework of guidance issued by the Regulator which comprises a Code of Practice on how to meet the requirements and supporting guidance and an indicative "syllabus" which together provide details of what trustees need to know.

on DB and DC schemes, and investment and fund management. The toolkit covers all the knowledge and understanding requirements for trustees as set out in the Regulator's Code of Practice and scope guidance on how to comply with the requirements of the Pensions Act 2004. The Pensions Management Institute follows the Regulator's scope guidance as the basis for its Awards in Trusteeship. The toolkit is therefore useful for those seeking this accreditation. The stakeholders that we spoke to were complimentary about the quality of the material that they had found and used on the site.

The Regulator will need to explore means of reaching smaller schemes and employers

63 The Regulator's annual governance survey (which gathers opinions from scheme trustees and administrators) gives it a relatively clear picture of the levels of penetration its guidance has

achieved. The results of the 2008 survey suggest that more could be done to reach the trustees of smaller schemes who are likely to be less familiar with the law. While just over a quarter (28%) of respondents said that most or all trustees had used the toolkit, a fifth of the schemes surveyed (20%) said that none has used it. Amongst smaller schemes, this was the most common response.

64 We discussed this issue with senior management at the Regulator, who acknowledged the difficulty of reaching out to the very large number of small schemes. As they argued, interventions here need to be taken on the basis of a cost-benefit calculation, and, to date, the Regulator had focused on the larger schemes where the impacts of regulatory failure would be much greater. Looking ahead, however, we believe that extending the reach of the Regulator's guidance should be a priority, particularly in the

context of DC schemes as these become more common (and where schemes, to date, have made less use of the toolkit than their DB equivalents).

- 65** The Regulator's new role in the Employer Compliance Regime from 2012 will also pose challenges in the reach and form of its guidance. To date, it has worked with a relatively small number of larger employers who sponsor occupational pension schemes; in the future, it will have a compliance role with regard to all businesses. Meeting the challenge of communication with smaller businesses, and ensuring that they understand their new responsibilities, will be a particular challenge. It will involve developing new channels, languages and styles of communication to reach audiences that at present have only limited, if any, interest in pensions law. We discussed the Regulator's plans for tackling the ECR. Implementation lies some way in the future, and we are not in a position to comment in detail on these plans.

The Regulator's stakeholders feel able to approach it about specific issues without fear of adverse consequences

- 66** A number of regulated stakeholders put it to us that their relationship with the Regulator was such that they felt able to seek advice from it on issues where there was uncertainty about the law, or about how to comply with it, without fear of any adverse consequences.
- 67** We found that the "clearance" process – which amounts, in effect, to the provision of bespoke guidance about the way that regulation will impact in very specific circumstances – had been particularly welcomed by businesses and had helped create an open and trusting relationship.
- 68** Clearance statements have been helpful in giving certainty to businesses on the

treatment they can expect from the Regulator when managing complex transactions which might raise compliance issues. This allows for significant decisions to be made with confidence, where these might otherwise be inhibited by the prospect of costly enforcement action. We found that this was a good model of guidance that other regulators should be encouraged to explore within their different operating contexts.

The Regulator's website is well structured, but needs more signposting

- 69** The Regulator's website is generally structured on common sense lines and most key information is easily accessible within a few clicks of the front page. Stakeholders felt that more could be done to make technical information easier to find, however. The Regulator has provided extensive guidance material since its foundation, particularly through its Codes of Practice, but there is at present no effective index to the key issues contained within them.
- 70** This was an issue for schemes and their administrators in particular, who routinely need clear information on specific points of the law, but found that the increasing quantity of information, codes, and guidance documents, is making it harder to track down specific references.
- 71** A related issue raised with us by stakeholders was that changes of detail to guidance documents were not always signposted within the documentation. This could in practice create burdens for users who would need to cross-refer to the previous document to work out the implications for them.
- 72** We would encourage the Regulator to explore how information could be more clearly indexed with these users in mind.

Data requests

Hampton principle

“Businesses should not have to give unnecessary information or give the same piece of information twice”

Key findings:

- **The Regulator imposes significant data requirements on many pension schemes, but there is a clear understanding and acceptance as to why the information is necessary**
- **The Regulator publishes key data in an accessible and useful form**
- **The Regulator is making use of innovative methods like cost measurement methodologies to reduce data burdens**
- **There are overlaps between the data required by the Regulator and some of its partners which it should explore with a view to reducing costs**

Background

73 The Regulator’s regulatory model is dependent on access to high-quality information about pension schemes. The Regulator imposes a number of data requirements on businesses and others:

- Most occupational schemes that have been registered with HMRC and have more than one member are required to register with the Regulator.
- The legislation requires that all regulated schemes submit a scheme return at least every three years but no more than once a year. The Regulator has discretion to set the frequency of these returns and chooses to collect data from most schemes annually as the basis for its risk-based approach. DC schemes with fewer than 12 members may submit every 3 years.
- The legislation requires that a DB scheme must have sufficient and appropriate assets to cover its “technical provisions” – that is, an estimate of the amount needed to pay the benefits as and when they become due. Where a DB scheme’s valuation shows it is in deficit, the trustees must put in place a recovery plan and submit details of the valuation and the plan to the Regulator.
- The legislation imposes a duty on trustees and their advisers, employers, scheme administrators, and professional advisers, to report in writing to the regulator any significant breaches of the law.
- There are a number of notifiable events (which must be reported to the Regulator) designed to help the Regulator identify risks. These include issues which may affect members’ benefits, instances of poor scheme administration, or risks of a possible call on the PPF. The regime also gives the PPF early warning of possible calls on the fund.
- Clearance is a voluntary process whereby a clearance statement can be sought from the Regulator giving assurances that the Regulator will not use its anti-avoidance powers in relation to a particular transaction such as an acquisition or a merger.

- 74** Much of the data required by the Regulator under these various headings may be submitted via the Regulator's online system, Exchange, which feeds into its internal SCORE database. Exchange has resulted in a number of benefits, including an overall reduction in the amount of data collected, as well as better quality data informing its overall risk-based approach to regulation.

Review Findings

The Regulator imposes significant data requirements on many pension schemes, but there is a clear understanding and acceptance as to why the information is necessary

- 75** The Regulator's regulatory regime (particularly for DB pension schemes) is built upon the submission of data. It carries out very few inspections, and the quality of its understanding of issues confronting the sector is dependent on the submission of high quality information (much of which needs to be verified by an actuary) regarding pension schemes. Accordingly, the data requirements on DB schemes in particular are relatively heavy. The majority of DB schemes are required to submit an annual return which includes information on scheme assets and liabilities, asset allocation, the participating employers, scheme type and status, membership details, the trustees and their advisers. Where a DB scheme is in deficit, there are requirements to submit further data as part of the process of agreeing a recovery plan with the Regulator.
- 76** This is not widely regarded as a significant burden. The stakeholders that we interviewed were aware of the reasons for the Regulator's data requirements and, despite the volume of information required, did not question the need for its collection. This also reflected the fact that
- much of the data involved is required for ordinary business purposes in any case.
- The Regulator publishes key data in an accessible and useful form**
- 77** The Regulator has a policy of publishing key data in an accessible form. Its most important data compilation, the "Purple Book" (DB Pensions Universe Risk Profile, published jointly with the PPF), has been produced annually with a view to increasing knowledge and understanding of DB schemes in the UK, the risks they present, and the way they are changing. This has provided a significant addition to the evidence base on occupational pensions, particularly in relation to small and medium sized schemes. At the time of the Review, the Regulator had published (January 2008) an initial summary of research on DC schemes; since the Review took place, it has published its first annual publication setting out data and analysis of DC trust-based schemes.
- 78** Data on recovery plans and clearance applications was also published in December 2008: the publication included a number of case studies to illustrate the Regulator's approach to some specific regulatory issues. We found that initiatives like these had helped secure buy-in to the Regulator's data requirements, as well as providing a good foundation for the development of policy on a clear evidence base.
- The Regulator is making use of innovative methods like cost measurement methodologies to reduce data burdens**
- 79** The Regulator has worked hard to reduce the burdens involved in data submission. It has been estimated that the aggregate costs associated with the submission of data in annual returns has been reduced by 50 per cent.⁴ The Regulator has explored a number of mechanisms for reducing the

⁴ The Government's Admin Burden Measurement Exercise in 2005 produced an indicative estimate for the burden of the Regulator's scheme return of £2m per annum. Although the Regulator believes this is an underestimate, the fact that the burden has been reduced by 50 per cent is supported by independent validation with stakeholders and details of the process changes the Regulator has introduced.

burden of specific submissions, including for instance pre-population of online forms, and a requirement that information only needs to be updated on a “by exception” basis, where the position has changed since the time of the last return.

- 80** The Regulator has established a data panel which scrutinises individual proposals for new data requests. Members of staff who are making a bid for new forms of data request must attend the panel, and justify their request on the basis of an assessment of costs and benefits. The Panel includes PPF representation.
- 81** At the time of the Review, the Regulator was also developing internal processes for measuring and reducing data burdens based on the Standard Cost Model (SCM) – a methodology which attributes a cash cost to regulatory data requirements, by measuring the time involved in the processes for the businesses affected. Like many regulators, the total administrative burden associated with occupational pensions regulation was measured at an early stage of the Regulator’s work as part of the Government’s Administrative Burdens Measurement exercise in 2005.

The exercise gave indicative aggregate costings for specific regulatory information obligations. The Regulator is seeking to develop a more precise and tailored tool which will allow for more informed decision-making on the detail of data requirements within the data panel. The Regulator aims to use the outcomes of this cost measurement exercise to help schemes to further reduce the burden of information obligations, including by addressing the costs of obtaining external advice.

There are overlaps between the data required by the Regulator and some of its partners which it should explore with a view to reducing costs

- 82** The stakeholders that we interviewed were positive about the work that the Regulator had done to reduce unnecessary data requests. They felt that this had been a strong achievement compared to the work of its predecessor body, OPRA, where the regulatory regime depended on much more frequent submission of routine information.
- 83** A number of stakeholders drew our attention to areas where other public bodies imposed data requests which to some extent overlapped with the

Good practice: The Data Panel

As part of its ongoing programme to minimise the burdens of its scheme return process, the Pensions Regulator has established a “Data Panel” to review and approve the addition of any new requests for data to scheme return for all types of pension scheme. The objective is to ensure that the data collected is only that which is necessary for the effective operation of the Regulator, and cannot be collected from alternative sources. The focus is on ensuring that the burden on schemes is kept to a minimum and is justified by the benefit of data collected.

The panel has representatives from across the Regulator, as well as from the PPF, to ensure that it has appropriate expertise and that the operational needs of these organisations are considered in the round. External stakeholder feedback is also built into the process via a quarterly panel meeting with representatives of trustees, insurers, advisors and scheme administrators. This ensures that the pensions community has an opportunity to comment on the panel’s decisions, and the resulting proposed changes to the scheme return.

requirements already being imposed by the Regulator. Some of the Regulator's most important partners here are HMRC, Companies House and the Office of National Statistics. We spoke with the Regulator's staff about work it is undertaking with its partners to reduce such overlaps: it has already used data sharing arrangements to reduce the volume of data collected through its scheme return. It is currently taking this work further, in particular working with HMRC to reduce the unnecessary duplication involved in the current requirement to register with both bodies. It is difficult to comment on the outcome of this work at this stage, but we would encourage the Regulator to continue to build upon its achievements to date with regard to its own data in seeking to secure a more co-ordinated approach amongst the bodies concerned.

Inspections

Hampton principle

“No inspection should take place without a reason”

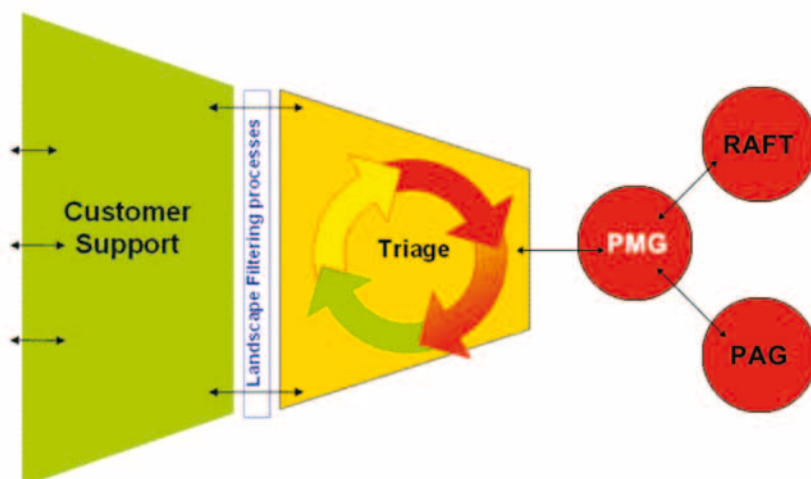
Key findings:

- The Regulator makes relatively little use of inspection, for good reason, but it has extensive engagement with many larger pension schemes.
- The Regulator’s systems for allocating investigation and compliance resources to specific cases on the basis of an assessment of risk are strong, and have benefited from a “continuous improvement” approach.
- The Regulator also has good systems for “horizon scanning”: identifying, assessing and acting upon new and emerging risks.
- The changing balance of the Regulator’s work may mean that more conventional inspection methods could be needed in the future.

Background

- 84 There are around 62,000 private sector trust-based occupational pension schemes regulated by the Regulator. With the limited resources available to it, and the alignment of the Regulator’s interests with those of trustees, decisions on the allocation of resources need to be made according to a risk assessment; a universal inspection policy would not be a realistic or cost effective option.
- 85 The Regulator only rarely conducts inspections in the conventional sense of visits in person to business premises to

check for compliance. There is no statutory requirement on it to visit businesses routinely, and its level of resourcing is such that routine visits would be impractical. It does have powers to inspect premises (under s.73 of PA 2004), but these are not used as a matter of routine. Indeed, the Regulator regards this power as a form of formal action which requires internal sign-off, like forms of enforcement action. There is of course a need for additional scrutiny of some specific pension schemes where these are deemed to represent particularly high risks in relation to its regulatory objectives, particularly the protection of members’ benefits.



Good practice: The Pensions Regulator's operational approach to identifying and addressing risk to pension schemes

The Pensions Regulator has put in place, and continues to develop, an operational model to identify risks, escalate them appropriately, and determine the right approach to take. The diagram on page 30 represents this process.

The Customer Support team provides the main interface for contact with the Regulator, handling all incoming enquiries, taking a leading role in the provision of education and support activity to the regulated community. It conducts initial risk assessment of scheme risks.

The Triage team works very closely with Customer Support and its role is to identify and prioritise risks to pension scheme members and the PPF and make a judgement about how these risks should be addressed. This might be returning the referral to Customer Support for quick resolution or escalating the risk to the Practice Management Group (PMG) for more active intervention.

Together Customer Support and Triage also work to identify trends in types of contact, emerging risks, and thematic issues which they communicate to the rest of the Regulator.

PMG allocates cases and enquiries to one of two regulatory practices: the Risk and Funding Team (RAFT) or the Pensions Administration and Governance team (PAG). These practices are likely to be dealing with 600-800 cases at any one time, in interdisciplinary teams, comprised of case managers, business analysts, lawyers, actuaries and other specialists dependent on the case. Their focus is very much on preventing/resolving problems wherever possible in keeping with the *“educate, enable and enforce only where necessary”* approach.

RAFT's focus is on two areas. Firstly, it addresses risks to the funding of DB schemes by helping trustees and employers to agree prudent funding targets and, if necessary, reasonably affordable recovery plans. Secondly, it assesses corporate events such as mergers and acquisitions, or one-off dividends, to ensure that schemes receive appropriate mitigation for any detrimental effects from these events, and to grant clearance to proceed where appropriate.

PAG focuses on administration and governance issues such as appropriate internal controls and record keeping, management of conflicts of interest and processes for winding up schemes. The team covers both DB and DC schemes and works to address risks to members' benefits or the PPF arising from activity in specific schemes. It also manages trustee services, maintaining the Regulator's Trustee Register and appointing independent and member-nominated trustees to schemes where necessary.

Built into this process are a number of methods of trying to ensure that the Regulator is effective at identifying risks, and responding to them quickly, proportionately and consistently. For example, the operational model works using a common set of business rules and process maps to ensure consistent practice and enable quick judgements about whether a risk needs to be examined in more detail, and who is best placed to do so. The process involves secondary risk analysis and quality assurance which often acts as a double check on referral decisions. The practices hold regular meetings across case teams to enable discussion, sharing of knowledge, identification of broader trends and risks etc.

86 Since its foundation, the Regulator has developed and refined a system of regulatory “trriage”, which allows for an effective assessment to be made of the risks arising from a particular case, and for action to be prioritised accordingly. Work on specific cases is divided between two teams in the Regulator’s operational core: RAFT (Risk and Funding Team) and PAG (Pensions Administration and Governance Team). The former’s work centres on assessment of scheme funding valuations recovery plans, and handling requests for clearance; the latter focuses on pensions administration and governance issues, including the appointment of independent

trustees. Important cases are investigated and handled by multidisciplinary teams (typically made up of a case manager, a business analyst, an actuary and a lawyer).

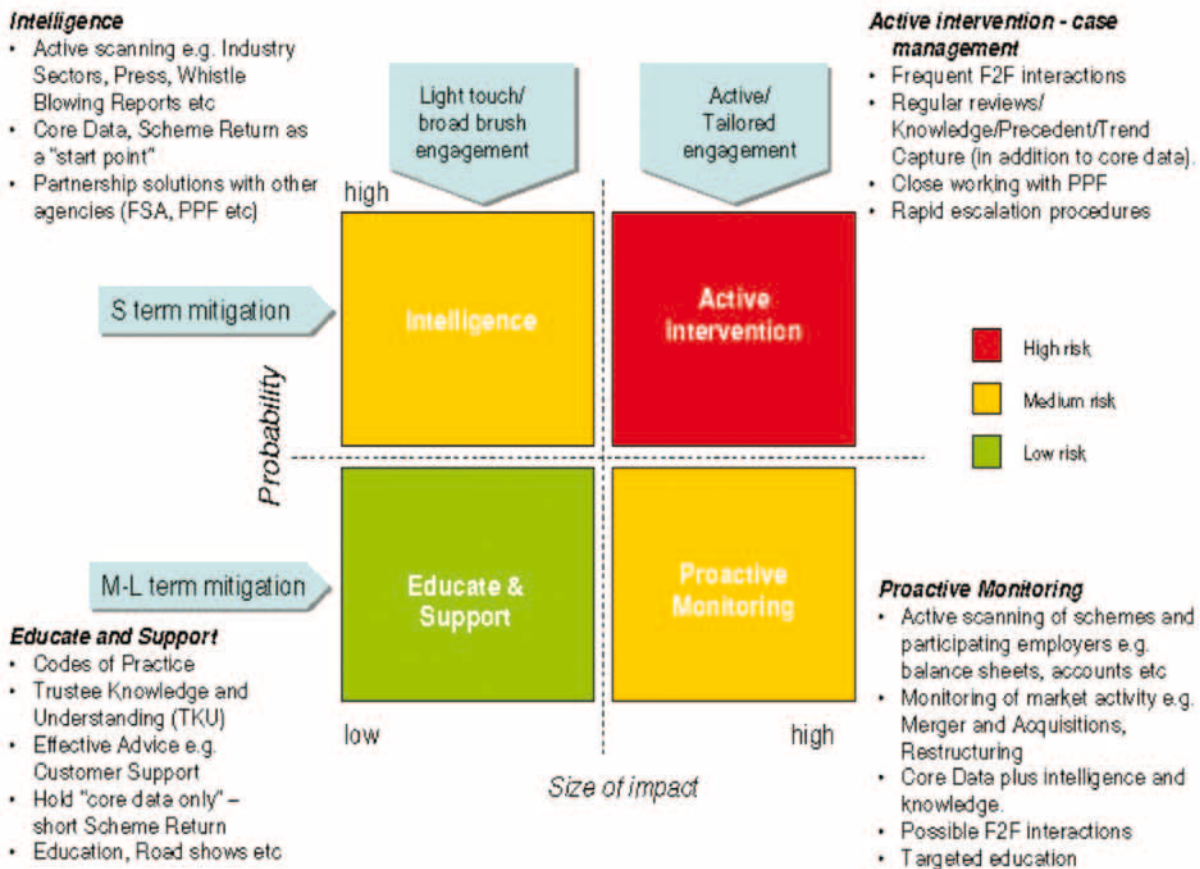
Review Findings

The Regulator makes relatively little use of inspection, for good reason, but it has extensive engagement with many larger pension schemes

87 The following diagram summarises the Regulator’s fundamental approach to prioritising its work according to risk:

88 The probability of failure, and the scale of the impact of failure, are taken into

Risk and Intervention model



account in determining the Regulator's level of engagement with specific schemes. While formal inspection as such is rare, the Regulator will spend more resource in continuing face-to-face interaction with the larger, high risk schemes.

- 89 There was no suggestion from business representatives that this scale of interaction was inappropriate: on the contrary, businesses are contributors via the Pensions Protection levy towards the PPF, and share the Regulator's concern to ward off any risks to it. In conversation with the Review Team, they were broadly supportive of the current balance of work.

The Regulator's systems for allocating investigation and compliance resources to specific cases on the basis of an assessment of risk are strong, and have benefited from a "continuous improvement" approach

- 90 We found that the Regulator's systems for allocating investigative resource according to risk were particularly impressive: this was less a matter of the use of a specific risk framework than the successful implementation of an organisational structure which is geared to sifting intelligence and ensuring that action is directed efficiently at the most important issues.
- 91 The Regulator's basic system is founded on the National Intelligence Model – a business model developed in the first place by the police which sets out a system for scrutinising intelligence and for "tasking" i.e. allocating resource to specific cases on the basis of an intelligence assessment.
- 92 The Regulator has however developed its own structures over several years on this basis, adopting an approach that has been inspired by continuous improvement and other techniques drawn from operations management to hone the tasking process. The system that is

emerging from this process has a number of characteristics and strengths, of which we would particularly note the following:

- the speed with which action is taken on the basis of incoming intelligence (which is usually processed on the day it is received);
- effective peer review of decision-making, both within multi-disciplinary teams and across them;
- intensive training and support for those working at the front end of the system, including staff on Customer Support lines; and
- the continuous development and refinement of a list of "business rules", internal guides to decision-making in more routine cases which are a distillation of lessons learnt from previous experience.

- 93 While we are not in a position to comment on the detail of the risk assessments involved, we found that the Regulator's approach was impressive, and that there are likely to be important lessons from its experience from which other regulators might learn.

The Regulator also has good systems for "horizon scanning": identifying, assessing and acting upon new and emerging risks

- 94 We reviewed the Regulator at a time when the prevailing assumptions underlying the regulation of financial services were being widely debated. One of the topical issues was the extent to which existing methods of regulation were capable of assessing "systemic" risks – i.e. risks that are intrinsic to whole financial systems and markets, as opposed to risks that are specific to particular businesses.
- 95 The Regulator is less exposed to some of the risks of the financial services market than other regulators with a financial focus. One of its findings during the downturn, for instance, was that very few

pension schemes had been exposed to the “toxic assets” which had impacted seriously elsewhere. Nevertheless, as with any regulator, there is a need in the occupational pensions sector for the Regulator to be able to move quickly to act in response to serious emerging themes, above and beyond its work with specific businesses.

- 96** We discussed the flexibility of the Regulator’s system of risk assessment with senior and front-line staff. They felt that existing systems were sufficiently flexible and robust to deal with emerging patterns of risk where new themes emerged from interaction with regulated businesses. One of the factors we discussed with front line staff was the impact of the threat of insolvency in the context of the economic downturn. This had engendered a range of new behaviours in practice that posed new cross-cutting risks –staff were satisfied that the feedback they had given to colleagues elsewhere in the Regulator had been taken seriously and action was being taken to reprioritise work accordingly, both at operational and at policy level.

The changing balance of the Regulator’s work may mean that more conventional inspection methods could be needed in the future

- 97** The Regulator’s existing systems have been designed largely around the risks associated with DB schemes. This reflects the underlying legislation which gives the Regulator significantly more information-gathering power in relation to DB schemes. The information available to it regarding DC schemes is different in character. Some stakeholders felt that this provided a less comprehensive evidence base for the assessment of risk. We put this view to the Regulator, whose strong view is that the information requirements on DC schemes are appropriate and an adequate basis for a risk-based system of enforcement. We are not in a position to comment on the detailed position, but the DC sector is likely to continue to grow, moving the balance of risks addressed by the Regulator. There may be a case in the future either for reviewing the use of this power or for considering a more inspection-based regime where this is not possible.

Sanctions

Hampton principle

“The few businesses that persistently break regulations should be identified quickly, and face proportionate and meaningful sanctions”

“Regulators should be transparent in the way in which they apply and determine administrative penalties”

“Regulators should avoid perverse incentives that might influence the choice of sanctioning response”

“Regulators should follow up enforcement actions where appropriate”

Key findings:

- The Regulator has a significant and effective range of sanctions and enforcement tools at its disposal, which it applies in a proportionate way.
- The Regulator has made relatively little use of formal enforcement action, but stakeholders feel that the alternative measures that it takes can have an equivalent effect in practice.
- The Regulator is regulating in a complex environment where a single high-level enforcement policy may not be appropriate; a published policy is much more likely to be necessary in clarifying its approach to its Employer Compliance Regime responsibilities.

Background

99 The Regulator’s publications all stress its primary emphasis on education and enablement as its preferred options in securing compliance with the law, with enforcement only used where this is necessary. Its website presents the following account of its approach:

“Our operational approach can be best summarised as ‘Educate, Enable, Enforce’. We use our powers when it is appropriate to do so – but only as a last resort. Our experience over the past three years confirms that the existence of our powers, and their potential use, is often a sufficient deterrent which helps us in delivering successful outcomes. We have seen evidence of this in our experience in handling many hundreds of clearance cases and enquiries and in

discussions with trustees, employers and advisers on recovery plans.”

100 The Regulator has a wide range of formal powers (many of which can have very significant implications for those who are subject to them) that it can bring to bear in more serious cases. The Regulator classifies their main enforcement powers under three headings.

Putting things right

101 Action to protect members’ interests may include:

- Formally requesting information
- Appointing a trustee, or independent trustees
- Suspending or prohibiting a person from being a trustee
- Issuing an improvement notice requiring specific actions to be taken in a given

timeframe where there has been a breach of the pensions legislation

- Freezing a DB pension scheme
- Directing that a scheme be wound up if this best serves members' interests
- Imposing a civil penalty
- Formally inspecting premises and retaining information

Acting against avoidance

102 The Regulator has a range of powers specifically designed to help tackle employers (which may be individuals) deliberately avoiding pension obligations and relying on the PPF to pick up their liabilities.⁵ Here, the Regulator may issue:

- Contribution notices
- Financial support directions
- Restoration orders

DB Scheme funding

103 Finally, the Regulator may intervene in cases where trustees and an employer cannot agree a mutually acceptable recovery plan. The Regulator may:

- Direct how a scheme's technical provisions⁶ should be calculated
- Impose a schedule of contributions or a period over which a deficit should be made up

104 The Pensions Act 2004 requires that decisions to use certain powers are subject to the consent of a Determinations Panel. The Panel is part of the Regulator, but constituted in such a way as to provide a rigorous, essentially external, check on the Regulator's reasoning behind a specific proposed action. The proceedings of the Panel are quasi-judicial, and evidence may be submitted to it by the parties involved, who may also request an oral hearing. Decisions of the Determinations Panel

may be appealed to the independent Pensions Regulator Tribunal. This model of decision-making parallels that in the FSA under its founding legislation.

105 The above powers all relate to the Regulator's current regulatory regime. It will acquire a range of new enforcement powers in 2012 under the ECR as provided for by the Pensions Act 2008. The Act creates a number of breaches for employers who fail to comply with their duties under the Act (for example, failing to auto-enrol employees, pay contributions, or inducing employees to opt out of pension saving). The Regulator will have the right to issue Compliance Notices or Penalty Notices in these cases. There will be a right of appeal to the Pensions Regulator Tribunal against the issuing of a Penalty Notice, as well as its amount. (However, it should be noted that the Pensions Regulator Tribunal is to be replaced with a new tribunal structure under the Tribunals, Courts and Enforcement Act 2007, and there will be similar appeal rights under this new arrangement).

106 The Regulator's statistics distinguish between the use of delegated powers and of determinations: the latter must be approved by the Determinations Panel, but the former can be approved elsewhere within the organisation at delegated level. These tend to involve less contentious interventions: for instance, the appointment of independent trustees to specific schemes can be a serious intervention in cases where this is a reflection upon the quality of the existing trust; in other cases this can purely be an administrative necessity which is no reflection on the business as such (for instance with appointments to "orphan" schemes).

⁵ The "clearance" process (see see paragraph 22 on p.13) is designed to give assurance that the Regulator will not use these anti-avoidance powers in relation to a particular corporate transaction.

⁶ For an explanation of technical provisions, see Paragraph 21 on p.13

- 107** From 1 April 2008 to 31 March 2009, the breakdown of determination hearings submitted to the Panel were as follows:

Determination requested	Number of hearings	Outcome
Appointment of independent trustee under s7 ⁷	5	Appointments made in five cases
Bulk appointments of independent trustees under s7	2	Eighty appointments made in total at two hearings
Appointment of independent trustee under s23(1)	1	One appointment carried out at the same time as a vesting order
Suspension of trustees under s4	1	Five suspension orders made concerning two trustees and three firms of trustees
Winding up of a scheme under s11	3	All granted
Vest in, assign and transfer of property under s9	1	Granted
Removal from the Regulator's trustee register under s23(4)	1	Granted

The Regulator has a significant and effective range of sanctions and enforcement tools at its disposal, which it applies in a proportionate way

- 108** The Regulator fulfils a distinctive regulatory role that is in many respects untypical. The general assumption underpinning the work of most regulators rests on a relatively straightforward “compliance” model whereby individual businesses are deemed to be compliant, or not compliant with the law, and the regulator’s duty is to secure compliance with them in cases where the rules have been breached.
- 109** The Regulator’s role is in many respects more complex. First, the Pensions Act 2004 deliberately avoids giving a “one-size-fits-all” standard of compliance, setting out a scheme-specific funding regime. Second, the Regulator’s objectives are in many respects the same as trustees of

pension schemes, and form an effective regulatory “front line” in this respect. Finally, the Regulator commonly works intensively to mediate between employers and scheme trustees to help secure the right outcomes in specific cases; in other words, it acts as a facilitator or negotiator rather than an enforcer in the narrow sense.

- 110** However, there will be cases where formal enforcement powers are required, and the range of powers available to the Regulator reflects this complexity. The Review Team believes that the range of sanctions available to the Regulator seemed appropriate, and its staff identified no perceived gaps in the enforcement “toolkit” available to it. Staff told us that there is regular engagement with DWP to monitor the current legislative framework in order to ensure that the legislative framework remains fit for purpose.

⁷ All section references are to provisions of the Pensions Act 2004.

The Regulator has made relatively little use of formal enforcement action, but stakeholders feel that alternative measures that it takes can have an equivalent effect in practice

- 111** The Regulator has made relatively little use of formal enforcement action in its work. In part, this reflects the unusual characteristics of its situation discussed above, but it also stems from a philosophy of regulation that puts a primary emphasis on education and enablement above enforcement except in the most serious cases.
- 112** We discussed the scale of the Regulator’s enforcement action with staff and a range of stakeholders. The common perception was that it was striking the right balance between work in support of compliance by informal means, and formal action, and that the Regulator had, in practice, sufficient teeth to secure the right outcomes. In many cases there was an informal settlement between the Regulator and prospective subjects of enforcement action at a late stage, shortly before matters would have gone to the Determinations Panel.
- 113** The Determinations Panel is an unusual requirement. Many regulators have informal internal sign-off mechanisms for the authorisation of specific sanctions, but the Panel is a statutory requirement and has a quasi-judicial mode of operation. It has formal hearings which consider proposals for enforcement action to which evidence may be submitted by those who are likely to be subject to action. The Regulator staff at working level did not question the need for formal sign-off of this kind. Many of the interventions available to the Regulator could have such a serious impact on employers (contribution notices, for instance, could amount to requirements to pay very large

sums into pension schemes), that a formal check of this sort is desirable.

The Regulator is regulating in a complex environment where a single high-level enforcement policy may not be appropriate; a published policy is much more likely to be necessary in clarifying its approach to its Employer Compliance Regime responsibilities

- 114** The Macrory Report recommended that regulators should publish an enforcement policy, which should:
- “have regard to the Principles of Good Regulation, the Enforcement Concordat, the Compliance Code (when established) and the Macrory Penalties Principles;
 - set out what a regulator may do to bring businesses into compliance without the need for taking punitive action;
 - explain the range of enforcement options available to the regulator;
 - explain the criteria upon which decisions are made when choosing what specific enforcement action to take in each case of non-compliance, including any aggravating or mitigating factors the regulator might take into account before applying a particular sanction.”⁸
- 115** At the time of the Review, the Regulator had no enforcement policy but was reviewing the case for issuing a single document addressing all of these issues. For reasons discussed above, the Regulator’s role is in many respects more complicated than that of many regulators, which means that some elements of a conventional Enforcement Policy fit poorly with its responsibility and duties.
- 116** Most importantly, the legislative framework overseen by the Regulator is deliberately

⁸ Regulatory Justice: Making Sanctions Effective, November 2006, pp.88-89.

designed to avoid over-specification of funding requirements. A scheme-specific approach to funding regulation was a key part of the 2004 legislation. Very specific statements of how the Regulator will act in given cases could have unintended consequences which work against the basic intentions behind the Pensions Act 2004. There are cases where the Regulator's comments have been over-interpreted by the regulated community. For instance, the Regulator has publicised a "trigger" point for additional scrutiny of recovery plans. Where a recovery plan exceeds 10 years, the Regulator has made it clear that this will be subject to additional scrutiny. The Regulator's public statements make it clear that this is not to be regarded as a target (and not to imply that plans of 10 years or longer are necessarily inappropriate). However, there is in fact a tendency as a result of the trigger for many plans to make provisions that fall just short of the ten year trigger – i.e. there is a widespread assumption that the Regulator "expects" recovery from a deficit to take place over a period shorter than ten years, and this has skewed the way in which schemes operate in practice.

- 117** The Regulator has gone some way to clarifying what the regulated can expect from it in a number of contexts: its website and key documents set out its basic philosophy of regulation, and at a more specific level, documents like its Codes of Practice set out circumstances where the Regulator can be expected to take formal action. The Regulator is working up a range of anonymised case studies to help illustrate its thinking in specific cases. These have featured, for instance, in published analyses of recovery plans, and in recent workshop events regarding scheme funding in the circumstances of the downturn.
- 118** At the time of the Review, the Regulator was considering whether a unified Enforcement Policy would be appropriate. Given the complexity of the Regulator's position there may be a case for more incremental improvements to its existing documentation.
- 119** The position is different however with the Regulator's role regulating employer compliance under the Pensions Act 2008. While the main focus of the Regulator's role will be on educating and enabling employers to comply, there is likely to be an increased need to take enforcement action to address non-compliance, both to protect employees' access to pension saving and to ensure fairness for employers. Enforcement powers set out in the Act include the ability to issue compliance notices, and fixed and escalating monetary penalties, which may be used to address more serious non-compliance.
- 120** Implementation of the Act is some way in the future, but our discussions with stakeholders revealed some anxiety about the ways in which the Pensions Act 2008 powers would be used, and in particular that this could result in behaviours that are less compatible with the principles of better regulation than the Regulator's approach to date. The Review Team would encourage the Regulator to prepare and consult on how it intends to use its enforcement powers as soon as possible.

Focus on outcomes

Hampton principle

“Regulators should measure outcomes and not just outputs”

Key findings:

- **The Regulator has clearly defined outcome-based objectives, which allow for a pragmatic approach to decision-making.**
- **Management systems appear strong; the process of continuous review should ensure the Regulator remains in a good position to deal with new and emerging risks.**
- **The Regulator’s new statutory objectives are less clearly related to outcomes, and it will need to work with partners to ensure effective delivery of the shared outcomes that the Pensions Act 2008 is designed to secure.**

Background

121 The Regulator has four main statutory objectives that underlie its current work on occupational pension schemes. These are:

- “to protect the benefits under occupational pension schemes of, or in respect of, members of such schemes;
- to protect the benefits under personal pension schemes of, or in respect of, members of such schemes;
- to reduce the risk of situations arising which may lead to compensation being payable from the Pension Protection Fund (PPF), and
- to promote, and to improve understanding of, the good administration of work-based pension schemes.”

122 Under the Pensions Act 2008, the Regulator is due to acquire a new statutory objective relating to its new powers to “maximise compliance with the duties under Chapter 1 of Part 1 (and the safeguards in sections 50 and 54) of the Pensions Act 2008”.

123 Reflecting these statutory objectives, the Regulator’s Corporate Plan for 2009-2012 sets out four strategic priorities:

- promote key aspects of good governance and administration;
- monitor and review scheme funding and monitor market transactions;
- build understanding of DC risks in a changing landscape;
- build capacity and consider wider impact of reforms (with a view to the new responsibilities that will be acquired in 2012).

124 The Plan also identified five key themes for the Regulator’s work:

- improving governance and administration;
- reducing risks to DB scheme members;
- reducing risks to DC scheme members;
- preparing for 2012;
- better regulation.

125 The Regulator has adopted a range of performance measures which form the backbone of its management information. These include “hard” quantitative measures (like information about DB schemes in deficit), as well as survey information. Two surveys, both conducted independently, are particularly important to its work:

- the **governance survey** is designed to monitor the standards of scheme governance of occupational pension schemes;
- the **perceptions tracker** has a set of outcome-focused indicators based on an annual perceptions tracker to address key stakeholders' perspectives on its work. The survey (which is based around a similar sample each year) involves interviews with a range of businesses. Amongst other things, the perceptions tracker addresses stakeholder understanding of the Regulator's powers, the extent to which they trust its information, the extent to which it is focused on the right risks, and the extent to which it is taking proactive steps to address the most serious of these.

The results of both surveys are published annually.

The Regulator has clear outcome-based objectives, which allow for a pragmatic approach to decision-making

- 126** The Regulator's objectives under the Pensions Act 2004 are clear, and capture the outcomes of the regulations well. We found that there was a high level of understanding of these outcomes amongst the Regulator staff, which meant that decision-making at operational level was made with a clear focus on the best way of securing these outcomes.
- 127** For instance, we discussed with enforcement staff the issues that they would take into account when assessing the case for taking formal action where an

Good practice: The Pensions Regulator's focus on strategic risks to regulatory objectives

The Pensions Regulator's risk-based approach to regulation applies at both strategic and operational levels. In addition to using risk assessment to identify and address risks to pension schemes (as described elsewhere), the Regulator's executive management team devote considerable attention to the identification and assessment of strategic and operational risks, in the context of the delivery of the Regulator's statutory and business objectives. Each of these risks is tracked on a strategic risk schedule, managed by a dedicated risk adviser to enable risk ratings and mitigating actions to be reviewed on a quarterly basis by relevant business leads, by the Regulator's executive management team and by its audit committee. This process informs decisions about allocation of resources and management of the organisation more generally.

Risks are "owned" by executive directors, with staff across the organisation encouraged to manage risk in their work. Strategic risk management is also integrated into the Regulator's planning and performance measurement tools which enable all staff to understand how their own objectives, and those of their particular team, map to the organisation's statutory and strategic objectives, and how the organisation plans to mitigate risks to those objectives. Performance against these objectives is also regularly assessed by the executive management team and the Board using a range of outcome-focused measures, or key performance indicators, from both internal and external sources. These are categorised into the Regulator's five strategic themes: reducing risks to DB scheme members; reducing risks to DC members; improving administration and governance (which cut across both DB and DC schemes), preparing for 2012, and better regulation.

employer had failed to meet some of their legal duties. It was clear that the obligation to protect members' interests was the most important consideration here. Where there were conflicts in practice between this and other objectives (for instance ensuring that procedures had been followed to the letter by employers) it was clear that the ultimate outcome, as defined in the statutory objectives, took priority.

Management systems appear strong; the process of continuous review should ensure the Regulator remains in a good position to deal with new and emerging risks

- 128** The Review Team considered a range of corporate documentation designed to update senior management on developments in the sector, and to prioritise the work of the organisation as a whole. We found that the range of Key Performance Indicators (KPIs) available to the senior executive team presented a good picture of the main issues confronting the Regulator. Indicators include a range of measures: quantitative data on DB scheme funding, for instance, as well as measures of trustees' understanding of their responsibilities and the funding regime.
- 129** KPIs are also used to determine the allocation of resources at a strategic level. The Regulator has a "policy pipeline" which amounts to a project management system for new policy issues – KPIs have a role in determining the balance between new initiatives (for instance, between DB and DC issues), according to indicators of where key risks lie at any point in time.
- 130** We were impressed with the "line of sight" that was available to senior management, and the way in which the information involved was used to determine the Regulator's activities. The Regulator operates in a complex field, however, where there can be rapid developments (in financial markets and in occupational

pension scheme practice) that have a significant impact on its work.

- 131** There is a need for management systems to be reviewed and updated frequently to keep pace with such developments. We would encourage the Regulator to keep its current corporate documentation including its "dashboard" of key indicators and risk matrix updated, to ensure that this gives a comprehensive account of the fundamental risks facing the Regulator, particularly in the circumstances of the economic downturn.

The Regulator's new statutory objectives are less clearly related to outcomes, and it will need to work with partners to ensure effective delivery of the shared outcomes that the Pensions Act 2008 is designed to secure

- 132** Unlike its existing objectives, the new Pensions Act 2008 objective (that will take effect from 2012) is less clearly related to ultimate outcomes. It stresses securing employers' compliance with the law rather than the outcomes which are the ultimate purpose of the new enrolment regime. The Act seeks to set a framework within which access to personal pensions is enlarged. At the heart of the new system is a requirement that employers automatically enrol employees for a pension scheme. Employees may opt out of such provision, but only on the basis of an active decision not to take part. The Regulator will be responsible for ensuring that employers' comply with their responsibilities in relation to automatic enrolment, not with the ultimate success (including take-up) of pensions under the new system.
- 133** There are good reasons for this restricted role. The Regulator's responsibility as a regulator is different to that of DWP which has overarching responsibility for pensions outcomes, and to that of the Personal Accounts Delivery Authority

(PADA), which is responsible for setting up a national, trust-based pension scheme called 'Personal Accounts'.

- 134** Unlike its existing work, the Regulator will be required to take a more compliance-focused role than it has exercised to date. The Regulator could do an excellent job within the terms of its specific remit in ensuring compliance with the law, but this might not mean that take-up of work place pensions increases in practice. This depends on the success and attractiveness of the whole reform package. The overall regulatory outcome here will depend on the relevant agencies acting in unison. The Review Team found that the Regulator appeared to have strong relationships with DWP and PADA and we would encourage it to build upon these as thinking about the new regime develops.

Appendix 1: Review Team membership

Neil Davies is Head of Better Regulation at the Environment Agency and is responsible for embedding better regulation principles into all areas of the Environment Agency's business. He has some 14 years experience working as a regulator in both policy and operational roles. Prior to this he worked in the chemical industry and the coal industry.

David Livingstone is Head of the Northern Ireland Trading Standards Service (part of the Department of Enterprise Trade and Investment Northern Ireland). He has worked with both the UK and the Northern Irish governments on the implementation of the Hampton agenda in Northern Ireland. He has also worked on consumer protection and better regulation projects with the governments of Lithuania, Lebanon, Malta, Turkey and Armenia.

Charles Nancarrow is an Audit Manager at the NAO with responsibility for delivering value for money reports on the economic and sector regulators and their respective consumer bodies, and the competition authorities. He is a qualified Chartered Accountant and has also been involved with the NAO's work on Private Finance Initiative and privatisation. Prior to that he worked as a financial auditor and also spent some time working in the City.

Michael Williams is deputy director in the Innovation Directorate of the Better Regulation Executive. Michael is a member of the Government Economic Service and is the BRE's senior economist. Michael joined the BRE in 2005. He has previously worked at HM Treasury, the Office for National Statistics and the Foreign and Commonwealth Office in a range of economist and policy roles.

Appendix 2: Key findings and conclusions of the Hampton and Macrory reports

Hampton principles of inspection and enforcement

- Regulators, and the regulatory system as a whole, should use comprehensive risk assessment to concentrate resources on the areas that need them most
- No inspection should take place without a reason
- Regulators should provide authoritative, accessible advice easily and cheaply
- All regulations should be written so that they are easily understood, easily implemented, and easily enforced, and all interested parties should be consulted when they are being drafted
- Businesses should not have to give unnecessary information, nor give the same piece of information twice
- The few businesses that persistently break regulations should be identified quickly, and face proportionate and meaningful sanctions
- Regulators should recognise that a key element of their activity will be to allow, or even encourage, economic progress and only to intervene when there is a clear case for protection
- Regulators should be accountable for the efficiency and effectiveness of their activities, while remaining independent in the decisions they take
- Regulators should be of the right size and scope, and no new regulator should be created where an existing one can do the work
- When new policies are being developed, explicit consideration should be given to how they can be enforced using existing systems and data to minimise the administrative burden imposed

Source: Hampton Report, Box E2, pg7

Macrory's principles and characteristics of an appropriate sanctioning regime

A sanction should:

1. Aim to change the behaviour of the offender;
2. Aim to eliminate any financial gain or benefit from non-compliance;
3. Be responsive and consider what is appropriate for the particular offender and regulatory issue, which can include punishment and the public stigma that should be associated with a criminal conviction;
4. Be proportionate to the nature of the offence and the harm caused;
5. Aim to restore the harm caused by regulatory non-compliance, where appropriate; and
6. Aim to deter future non-compliance.

Regulators should:

1. Publish an enforcement policy;
2. Measure outcomes not just outputs;
3. Justify their choice of enforcement actions year on year to stakeholders, Ministers and Parliament;
4. Follow-up enforcement actions where appropriate;
5. Enforce in a transparent manner;
6. Be transparent in the way in which they apply and determine administrative penalties; and
7. Avoid perverse incentives that might influence the choice of sanctioning response.

Source: Macrory Report, Box E1 page 10.

Appendix 3: Review scope and methodology

The review focused on those aspects of the Pensions Regulator's activities where we considered that its actions have the most impact on business. This meant that the majority of the Authority's work was in scope.

Our methods included:

- interviews with a wide range of the Regulator's staff including senior managers;
- interviews with other stakeholders including Government departments, regulators and the trade bodies in the pensions sector and business representative groups;
- focus groups of the Regulator policy staff and compliance staff;
- observation of the the Regulator's work in practice; and
- document review, including the Regulator's high level strategies and plans.

The review process is described in *Hampton Implementation Reviews: Guidance for Review Teams*. It is not the same as a full value-for-money audit of economy, efficiency and effectiveness and the Review Team's conclusions are both evidence- and judgement-based. These judgements, however, have been made drawing on a range of evidence from different sources, including those described above. Judgements have not been based on evidence from a single source – the review team has sought to bring together evidence from a number of different businesses and organisations, and from the Regulator front-line staff, policy officials and senior managers.

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