Introduction to pension legislation for trustees

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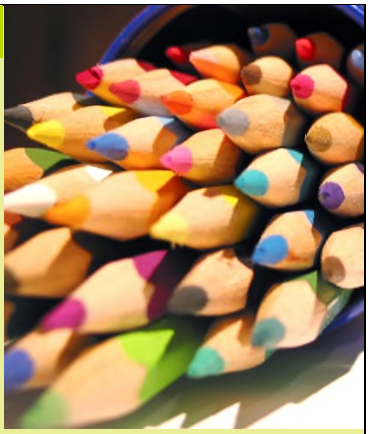
HIGHLIGHTS



There are two levels of legislation:

- **primary legislation**: high level statutes called "Acts", which are passed by both Houses of Parliament;
- **secondary legislation**: created under delegated powers, usually by the relevant Secretary of State or HMRC. Secondary legislation often comes in the form of "Regulations" or "Orders" and contains the technical detail needed to support the high level principles contained in an Act.

The Courts do not create legislation but are frequently asked to interpret it.

Why should trustees be concerned with pension legislation?

Legislation can override a scheme's trust deed and rules, so it is important to be are aware of when and how this can happen and how it may affect the running of a particular scheme.

The main statutes which concern occupational pension schemes are:

- The Pension Schemes Act 1993
- The Pensions Act 1995
- The Welfare Reform and Pensions Act 1999
- The Pensions Act 2004
- The Finance Act 2004
- The Pensions Act 2008
- The Pensions Act 2014
- The Taxation of Pensions Act 2014
- The Pension Schemes Act 2015
- The Pension Schemes Act 2017
- The Financial Guidance and Claims Act 2018
- The Pension Schemes Act 2021

PENSION SCHEMES ACT 1993

The Pension Schemes Act 1993 ("PSA93") is a consolidating Act, bringing together various provisions relating to pensions into a single legislative instrument. Areas covered by the Act include:

- **Contracting-out**: schemes used to be able to contract-out of the earnings-related part of the State pension (currently the State Second Pension (S2P)). Contracted-out schemes had to provide members with minimum benefits set out in the Act and regulations. Contracting-out on a defined contribution (DC) basis was abolished in April 2012. Contracting-out on a defined benefit (DB) basis was abolished from 6 April 2016, although detailed requirements still apply to DB contracted-out benefits already built-up.
- **Guaranteed minimum pensions (GMPs)**: members in contracted-out service before April 1997 built up rights to GMPs. Many schemes still hold GMPs and complex rules apply in relation to them.
- **Preservation**: rights to a deferred pension for members who leave pensionable service before their scheme's normal pension age.
- **Revaluation**: giving members with deferred pensions some protection against inflation in the period before their pension comes into payment.
- **Cash equivalent transfer values (CETVs)**: members with a deferred pension who meet certain conditions have a right to transfer the value of their benefits out of their current scheme to an arrangement willing to accept transfers in.
- **Cash transfers**: members who leave pensionable service with between three months and two years of pensionable service, but without a right to a deferred pension, may transfer the value of their benefits to another arrangement or take a refund of their own contributions. However, refunds of contributions from occupational money purchase (defined contribution) arrangements for members with at least 30 days pensionable service were prohibited from 1 October 2015.
- **Pensions Ombudsman**: with powers to investigate pension disputes and to direct disputing parties to take particular action.
- **Independent trustees**: an independent trustee must be appointed on the insolvency of the sponsoring employer.

PENSIONS ACT 1995

Areas covered by the Pensions Act 1995 include:

- **Investment powers**: power to invest the assets of a pension scheme rests with the trustees, overriding any obligation in the scheme rules for the employer's consent.
- **Investment requirements**: including that trustees must take proper advice before making investment decisions; must not breach statutory limits on employer-related investment; and must prepare a statement of investment principles (SIP).
- **Advisers**: requiring trustees to appoint an auditor and (for defined benefit schemes) an actuary and setting out obligations for how they and other specified advisers are appointed.
- **Dispute resolution**: a requirement for trustees to operate an internal dispute resolution procedure (IDRP) for members, or prospective members, with a complaint about the scheme.
- **Disclosure**: trustees must give specified information to members at particular times and must make other specified information available upon request.
- **Pension increases**: a statutory requirement to increase some pensions in payment built up from April 1997 to give some protection against the effect of inflation.
- **Scheme amendments**: section 67 of the Act prohibits using scheme amendment powers to make changes which would have a detrimental effect on members' subsisting rights (broadly, rights they have built up before the date of the change), without the member's consent or a certificate of actuarial equivalence from the scheme actuary.
- **Scheme amendments**: section 68 of the Act allows trustees to be given statutory power to modify schemes for particular purposes, regardless of section 67 or any restrictions in the scheme's amendment power.
- **Employer debts**: section 75 of the Act sets out circumstances in which, where a defined benefit (DB) scheme is in deficit, a debt will be due from the employer(s) to the trustees. Section 75 debts can arise on an employer's insolvency, on the scheme entering winding-up, or on an employer in a multi-employer scheme ceasing to employ active members.
- **Schedule of payments to money purchase schemes**: trustees or managers of occupational money purchase (DC) schemes must ensure that a schedule of payments due to the scheme is maintained and must notify the Pensions Regulator if payments are not made in accordance with the schedule (unless certain conditions apply).

WELFARE REFORM AND PENSIONS ACT 1999

The Welfare Reform and Pensions Act 1999:

- introduced the requirement for employers to provide access to a **stakeholder pension scheme** for employees who did not already have a workplace pension available. The stakeholder designation requirement was subsequently repealed when the auto-enrolment requirements came into force (please see Pensions Act 2008 below);
- introduced the option of **pension sharing** on divorce;
- protects pension rights under a registered pension scheme from vesting in the trustee in **bankruptcy** where a member is made bankrupt.

PENSIONS ACT 2004

The Pensions Act 2004 developed pension protection further. Areas covered include:

- **Member-nominated trustees:** the trustee board of an occupational pension scheme must include member-nominated trustees (MNTs), or member-nominated directors (MNDs) where the trustee is a corporate body. (A requirement to have MNTs / MNDs was first introduced by the Pensions Act 1995.)
- **The Pensions Regulator (tPR)**: replaced the Occupational Pensions Regulatory Authority (OPRA), with extensive regulatory powers.
- **The Pensions Protection Fund (PPF)**: funded by a levy on defined benefit (DB) schemes, takes over DB schemes whose sponsoring employers are insolvent where the scheme funding is below a certain (PPF) level. The PPF provides benefits to affected members, though these will normally be lower than would have been provided under the scheme rules.
- **The Financial Assistance Scheme (FAS)**: set up to provide a basic level of benefit to members of underfunded defined benefit (DB) schemes whose employers became insolvent before the PPF provisions were in force.
- **Moral hazard provisions**: empower tPR to issue "financial support directions" and "contribution notices" requiring group companies to put funding arrangements in place, or pay contributions, to support the financial position of underfunded defined benefit (DB) schemes. tPR's powers may be exercised against group companies of the scheme employers, whether or not the target companies have ever participated in the pension scheme.
- **Scheme specific funding**: trustees of defined benefit (DB) schemes are required to ascertain the value of the scheme's "technical provisions" (the benefits built up to date); to set a schedule of contributions; and, where the scheme is in deficit, to decide a recovery plan for eliminating the deficit. In most cases, the technical provisions, schedule of contributions and recovery plan must be agreed with the employer.
- **Trustee knowledge and understanding**: a requirement for trustees to ensure that they have the necessary knowledge and understanding to carry out their functions properly.
- **Consultation requirements**: before making a "listed change" to a pension scheme, employers must consult affected members for a minimum of 60 days. Trustees are prohibited from making a listed change unless the consultation requirements have been complied with.

FINANCE ACT 2004

The Finance Act 2004 overhauled the taxation regime for pension schemes. Most UK pension schemes are now "registered schemes" for tax purposes. The Finance Act 2004 sets out:

- The **annual allowance**: limiting a member's tax-free benefit accrual in a given tax year.
- The **lifetime allowance**: applicable when a member starts to draw benefits, applying an additional tax charge on lifetime benefits over the lifetime allowance (£1,073,100 for 2021/22).
- **Authorised payments**: that a scheme may make to members or the employer without additional tax charges applying.
- The **unauthorised payment charge** and **scheme sanction charge**: applicable where a scheme makes payments that are not authorised payments.
- The benefits that may be paid as authorised payments from defined contribution (DC) schemes have been substantially amended by the Taxation of Pensions Act 2014, which took effect from 6 April 2015.

PENSIONS ACT 2008

The Pensions Act 2008 introduced a requirement for employers to "**auto-enrol**" their workers who meet certain criteria into a suitable pension arrangement and to contribute to their workers' pensions. The auto-enrolment obligations apply from an employer's "staging date" which, for existing employers, ranged from 1 October 2012 to 1 February 2018, with the largest employers required to stage first.

PENSIONS ACT 2014

The Pensions Act 2014 provided for various aspects of pension reform including:

- **State pensions**: the replacement of the Basic State Pension and the State Second Pension with a single-tier State pension from April 2016.
- **Contracting-out**: the abolition of defined benefit (DB) contracting-out from April 2016.
- **Automatic transfer**: of small DC pots when individuals move between employers (not yet in force).
- **Pensions Regulator's objectives**: the addition of a new statutory objective for the Regulator to minimise any adverse effect on the sustainable growth of an employer when exercising its functions in relation to scheme funding.

TAXATION OF PENSIONS ACT 2014

This Act introduced "pension flexibility" – extending the ways in which individuals may access their funds in defined contribution (DC) arrangements, with effect from 6 April 2015. The additional options include the ability to take DC funds as one or more uncrystallised funds pension lump sums (UFPLSs). In addition, previous limits on the amounts which could be drawn down from a DC fund were removed, as was the requirement to buy an annuity. Schemes are not required to provide the various options allowed by the reformed tax regime: in some cases, members may need to transfer to another scheme to access benefits in the way they wish.

PENSION SCHEMES ACT 2015

Areas covered by the Pension Schemes Act 2015 include:

- establishing the legislative framework for setting up shared risk (also called "defined ambition") pension arrangements (not in force);
- establishing the legislative framework for setting up collective defined contribution pension arrangements (not in force); and
- various changes needed to implement "pension flexibility" – the relaxation of the ways in which benefits may be taken from defined contribution arrangements with effect from 6 April 2015.

PENSION SCHEMES ACT 2017

The Pension Schemes Act 2017 sets out a framework for the authorisation and regulation of master trusts (broadly, private sector occupational pension schemes which provide defined contribution (DC) benefits and which are used (or intended to be used) by two or more unconnected employers.

FINANCIAL GUIDANCE AND CLAIMS ACT 2018

The Financial Guidance and Claims Act 2018 establishes a single financial guidance body (SFGB) to provide money and pensions guidance (and debt advice) to the public. The SFGB replaces Pension Wise, the Pensions Advisory Service and the Money Advice Service. The Act also gives power for regulations to ban cold-calling (unsolicited direct marketing) in relation to pensions.

PENSION SCHEMES ACT 2021

The Pension Schemes Act 2021 provided for various aspects of pension reform including:

- **Collective money purchase schemes:** these are a new type of DC scheme which allows members to benefit from a collective investment fund which has a greater proportion of high-return assets than a single member could risk in an individual investment fund. At retirement, members remain invested in the scheme and receive an income (not yet in force).
- **New civil penalty of up to £1m:** tPR will have new power to issue a civil penalty (a “section 88A penalty”) of up to £1m for breach of various requirements of pension legislation.
- **New criminal offences:** the Act creates new criminal offences (punishable by an unlimited fine or up to seven years’ imprisonment) for conduct intended to avoid a section 75 debt; or conduct risking accrued scheme benefits.
- **Contribution notices (CNs):** in addition to its existing moral hazard powers, tPR may now also issue a CN where a new “employer insolvency test” or a new “employer resources test” is met.
- **Notifiable events:** the existing requirement to notify tPR of certain employer-related events will be extended (not yet in force).

- **Pensions dashboards:** legislation to enable the development of pensions dashboards, to enable individuals to access information about all of their pension pots in one place (not yet in force).
- **Scheme funding:** a new requirement for trustees to adopt a written "funding and investment strategy", setting out how pensions and other benefits will be provided over the long-term (not yet in force).
- **Climate change:** new provisions which (together with regulations) from 1 October 2021 require trustees of schemes with at least £5bn assets to:
  - Take steps to ensure their own knowledge and understanding in relation to identifying, assessing and managing climate-related risks and opportunities;
  - identify, assess and manage climate-related risks and opportunities; and
  - report their scheme's governance framework, investment strategy, risk-management, metrics and targets in respect of climate-related risks and opportunities.

  The requirements will apply to trustees of schemes with £1bn assets from 1 October 2022 and may then be extended to smaller schemes.
- **Protection from scams:** new restrictions on members' statutory right to transfer will be introduced to combat pension scams (not yet in force). The DWP consulted on proposed new restrictions in May 2021.

BREXIT

The European Union (Withdrawal) Act 2018 established the legislative framework for the UK's withdrawal from the EU. It was implemented by the European Union (Withdrawal Agreement) Act 2020. Broadly, under these Acts, EU law (as it stood) was converted into UK law.

Subsequent regulations also made changes to the overseas pensions, cross-border pension and insolvency regimes in light of the UK's exit from the EU.

OTHER AREAS OF LAW AFFECTING PENSIONS

Pensions are not only affected by the statutes specifically relating to pensions – many other areas also influence the way that pension schemes are regulated and run, such as:

- trust law
- contract law
- tax law
- company law
- employment law
- anti-discrimination law
- European Union law
- financial services and consumer law
- data protection law
- anti-money laundering law
- criminal law.

This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

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