SLAUGHTER AND MAY/

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PENSIONS BULLETIN

QUICK LINKS

One Bunhill Row
London EC1Y 8YY
United Kingdom
T: +44 (0)20 7600 1200

In this month's Pensions Bulletin, we cover:

1. Immediate new significant restrictions on statutory transfers.
2. Significant changes to grandfathering provisions for the new Normal Minimum Pension Age of 57.
3. From 2023 scheme returns will need to include new scheme asset information.
4. Government is proceeding with a £100 minimum pot size for charges from April 2022.
5. High Court has allowed trustees to rectify scheme rules so that the employer cannot reduce pension increases.
6. Our Watch List: new additions for the January 2022 CMA deadline for submitting compliance statements; and the new scheme asset information in scheme returns.

IMMEDIATE NEW RESTRICTIONS ON TRANSFERS OUT

New rules on transfers, intended to help protect members from pension scams, took effect on 30 November. There are no transitional measures so trustees need to update their procedures for transferring members' benefits immediately. There have been significant changes from the draft regulations issued for consultation. Whilst the merger of three conditions into a single test is billed as a simplification, and trustees can now decide to make a transfer without asking for evidence about red or amber flags, trustees may still be in a difficult position where there is a suspicion of a flag.

The Department for Work of Pensions (DWP) has published revised Regulations to be made under Section 125 of the Pension Schemes Act 2021 (amending Section 95 of the Pension Schemes Act 1993), together with its response to its May 2021 consultation on the draft regulations.

The Regulations, which came into force on 30 November 2021, introduce new restrictions on individual statutory transfers out. Trustees will only be able to make a statutory transfer if one of the conditions is satisfied. Transferring in breach of the restrictions may still be possible as a discretionary non-statutory transfer, but without a statutory discharge. The Regulations apply to transfers where the date of the member's application is on or after 30 November 2021.

There are significant changes from the consultation draft, as a result of which trustees must decide that one of two conditions is satisfied before the member acquires a statutory transfer right:

- **First Condition: transfer to certain receiving schemes.** Condition 1 from the previous draft, where the transfer can go ahead with no further checks, is now restricted to transfers where the receiving scheme is an authorised master trust, a public service scheme or an authorised Collective Money Purchase (CDC) scheme. The list previously included transfers to schemes operated by FCA-registered insurers; these have been removed following pressure from Self-Invested Personal Pensions (SIPP) providers concerned that they were not included. DWP has concluded that the only way to deal with the difficult issue of which schemes to include is to remove all but the three main categories.

  The trustees must satisfy themselves "*beyond reasonable doubt*" that the receiving scheme is one of the listed schemes but must not require any further checks, apart from details necessary to confirm the scheme's identity.

- **Second Condition: transfers to all other schemes.** Draft Condition 2 (demonstrating an employment link for transfers to another scheme), Condition 3 (demonstrating residency for transfers to a qualifying recognised overseas pension scheme - QROPS) and Condition 4 (all other transfers where there is no amber or red flag) have been merged into a single Second Condition. This requires a holistic consideration of the employment and residency links (where applicable) with the red and amber flags. There are no major changes to the red and amber flags (set out in the table below and divided into "evidentiary" and "substantive" categories). One concern that has not been addressed is the amber flag relating to overseas investments, which seems to catch any receiving scheme arrangement that holds overseas investments. It was thought to be the intention only to catch jurisdictions where there are lax regulations or opaque corporate structures.

  Under the Second Condition, the trustees must be satisfied "*on the balance of probabilities*" that:

  - No **red** flags are present
  - If any **amber** flags are present, the member has taken pension transfer scams guidance from MoneyHelper (formerly known as MaPS). MoneyHelper will provide the member with a unique reference number to supply to the trustees as evidence that guidance has been given – trustees cannot transfer without this.

  In addition:

  - Where the transfer is to an occupational pension scheme (OPS), the member must demonstrate the **Employment link**.

- Where transfer is to a QROPS the member must demonstrate the **Residency link**. (If a QROPS is an OPS, then either the Employment or Residency Link is required.)
- Detailed evidence is required to demonstrate the Employment and Residency links: complete failure to provide it is a **red** flag; partial failure is an **amber** flag.

If the trustees decide there are red flags, or amber flags and the member has not taken advice, there is no statutory transfer right. However, unless the transfer is to an OPS or QROPS, there is no requirement for trustees to call for flag evidence; if they are confident that a particular receiving scheme does not constitute a scam risk, they may make the transfer without further evidence.

In effect, there are two types of Second Condition transfers:

Type 1: a transfer (not to an OPS or a QROPS), where the trustees decide "*on the balance of probabilities*" that there are no substantive red or amber flags.

Type 2: where the trustees are required to carry out additional due diligence (where the Employment or Residency links apply) or choose to do so because of concern that flags may be present. There are two different standards of proof in relation to flags: the trustees have to be satisfied "*beyond reasonable doubt*" that there is an evidentiary flag but "*have reason to believe*" there is a substantive flag. "*Reason to believe*" is defined as "*a reasonable foundation for the belief, on the basis of all the evidence and information available*".

In deciding whether flags are present, the trustees can rely on:

- Information provided directly by the member
- An omission of evidence or information from the member's formal response
- Any evidence or information already held by the trustees, including that obtained in the course of carrying out their duties in relation to the transferring scheme or another scheme.

Amber flags
(transfer right only if MoneyHelper advice is received)

Evidentiary flags:

- The member's response to the trustees' request for information/evidence is incomplete

Substantive flags:

- The evidence provided by the member does not demonstrate an Employment or Residency link
- The response to the trustees' request for information/evidence may not be genuine/may not have been provided directly by the member
- The receiving scheme includes high risk, overseas or unregulated investments; the fees are high or unclear; or it has unclear, complex or unorthodox investment structures
- There has been a sharp or unusual rise in transfer requests to a single receiving scheme or involving a single adviser or advisory firm

Red flags
(no transfer right)

Evidentiary flags:

- The member fails to provide a substantive response to the trustees' request for information/evidence about Employment or Residency link or flags
- Amber flags have been raised but the member has not provided evidence of MoneyHelper guidance

Substantive flags:

- Financial advice has been received from an unauthorised person
- The transfer request arose from an unsolicited approach
- The member was offered an incentive to transfer
- The member has been pressured to transfer

The Regulations set out requirements for notifications to the transferring member and on the timing of requests for evidence. These are summarised in the table below.

Communications and timings

Notification to member	Timing	Details
Notification of Conditions for a transfer	Within one month of a request for a statement of entitlement/application for transfer value	Not required if transfer is made within one month
Where the First or Second Condition for a transfer is met	Confirmation no later than the date on which the member is sent confirmation that the transfer has been made	
Where a member has been asked for information and has not provided it	Further request must be sent after at least one month	If a further month passes after the further request with no response, trustees may determine that the red flag is present
If the member provides incomplete information	Further request must be sent	Trustees may determine that the amber flag is present provided at least one month has passed since the further request
Neither the First or Second Condition is satisfied (so that transfer right is lost)	Notification within seven working days after the date of the decision	

TPR guidance

The Pensions Regulator (TPR) has published guidance (including a useful decision tree, although it does not cover the complexities of the three different standards of proof) on dealing with transfer requests under the new Regulations. The example questions to ask members when requesting additional information, included in the consultation paper, are now in the TPR guidance. TPR recommends compiling a "clean list" of low risk receiving schemes, where transfers can proceed without the need for additional checks.

One important point made by TPR is that trustees should consider the checks outlined in its guidance when assessing whether to make a non-statutory transfer (assuming the scheme rules allow it). TPR expects trustees to carry out enough due diligence on a non-statutory transfer to be confident that they have fulfilled their fiduciary duties to the transferring member.

Next steps for trustees: The new requirements should help trustees in those situations where they suspect a scam but are currently required by legislation to make a transfer (because the member has a statutory right). However, trustees may still be in a difficult position where there is a suspicion of a red or amber flag. For example, the amber flags require trustees to make subjective assessments, such as whether the investment is "high" risk. Trustees are likely to err on the side of caution when considering whether additional checks are required. Legal advice may be needed in cases of doubt.

Ultimate responsibility for the judgment calls on red and amber flags lies with the trustees, even if transfer procedures are within the ambit of the administrators. Penalties for non-compliance include TPR fines, possible maladministration claims to the Pensions Ombudsman and reinstatement of benefits if they transfer where there is no statutory right. Trustees should record all evidence requested and received and document the basis of their decision, with reference to the appropriate standard of proof. Immediate action includes:

- The new procedures, including the notification requirements, need to be inserted into the existing transfer process; pre and post-30 November requests must be distinguished.
- Data protection privacy and fair processing notices may need to be amended.
- Trustees may want to prepare a general member communication to explain the changes.
- In accordance with TPR's guidance on scams, trustees should continue to follow the Pension Scams Industry Group's voluntary Code of Good Practice (which will be updated) and to warn members regularly about the risk of pension scams, including sending them the ScamSmart leaflet with annual benefit statements.

INCREASING NORMAL MINIMUM PENSION AGE TO 57: REMOVAL OF THE TRANSFER WINDOW

The earliest age at which pension benefits can be taken in authorised form for tax purposes, Normal Minimum Pension Age (NMPA), will rise to 57 on 6 April 2028. The provision that would have given individuals the opportunity to grandfather an earlier NMPA until 5 April 2023 has been removed.

HM Treasury's response to consultation in July 2021 set out the proposed approach to legislating for the changes. One of the proposed additional features to the scheme-specific grandfathering regime was for there to be a window running up to 5 April 2023 in which individuals would have the opportunity to grandfather an earlier NMPA, by joining a pension scheme with rules that included an unqualified right to take a benefit before age 57 on 11 February 2021. This would have been consistent with the approach taken when NMPA rose from 50 to 55. However, HM Treasury has decided to amend this provision.

The Finance Bill (published on 4 November 2021) includes the draft legislation for the proposed change in NMPA. The provision that would have given individuals the window until 5 April 2023 has been removed. A protected pension age will be restricted to those who became members of a scheme before 4 November 2021, or where a transfer is made on or after 4 November 2021 in execution of a request made before that date. An HM Treasury statement explains that this change was made in response to industry concerns about the risk of individuals being the victims of pension scams. (Note the protected pension age is preserved on bulk transfers and protection for past service is offered on individual transfers.)

There are no other changes to the proposed approach outlined in the response to consultation. For details, please see our Pensions Bulletin September 2021.

Next steps for trustees: Trustees should consider whether any communications to members need to be amended in the light of this announcement.

CHANGES TO REPORTING OF ANNUAL ASSET CLASS INFORMATION BY DB SCHEMES

The Pensions Regulator (TPR) is going ahead with proposed changes to the information about scheme assets collected through scheme returns, in order to improve the measurement of scheme risk. Trustees need to be ready to collect the information in time for the 2023 scheme return. The changes are derived from the detailed set of asset categories used in the stress calculation for the PPF levy and those asset categories appear likely to be used as the basis for measuring investment risk in TPR's new defined benefit (DB) scheme Funding Code.

TPR and the Pension Protection Fund (PPF) have responded to consultation and announced changes to the asset class information collected by TPR from DB schemes through the annual scheme return. TPR uses this information to help measure investment risk and the PPF to help calculate its risk-based levy. Developments in pension scheme investment and in the types of growth assets have triggered the need for a better assessment of investment risk. The new data collection will operate from the 2023 scheme return.

In TPR's first consultation on a revised DB Funding Code, there was strong support for the use of a PPF stress test to measure investment risk, to enable trustees to determine the appropriateness of the risks being taken, in the context of their scheme's maturity and covenant. TPR's response notes that the new disclosures will form an important component of the changes feeding into the new Funding Code. (The second consultation, on the wording of the draft Code, is expected early in 2022.) TPR believes that, in order to get a clearer picture of investment risk (part of the information required to meet the standards expected under the new regime), trustees should report their asset data in a more granular way.

TPR will gather the additional information via scheme returns, using a tiered approach based on scheme size (by liabilities on a Section 179 basis):

- A simplified approach (Tier 1) will apply to smaller schemes with liabilities at the latest valuation below £30m. In the light of feedback received, the £30m boundary has been increased from the proposed £20m, although it will be kept under review with the possibility of reducing it to £20m (or less) in future.
- Larger schemes (Tiers 2 and 3) will be asked for more detailed data, with Tier 3 schemes (£1.5bn or more in liabilities) continuing to carry out the bespoke stress calculation, as required under the PPF levy rules.

The PPF plans to consult on related rule changes in the 2023/24 levy consultation process (in Autumn 2022), including consultation on the proposed stress factors for each asset class.

Next steps for employers and trustees: Trustees will need to be ready to collect the new information in time for the 2023 scheme return. The more detailed asset breakdown should be relatively straightforward for most schemes to provide and, in many cases, will already be included in regular reporting from investment managers. Sponsors and trustees will shortly need to consider the next stage of the new TPR DB Funding Code.

CHANGES TO CHARGES IN DC SCHEMES

The Government has decided to go ahead with its proposal to introduce a £100 "de minimis" pot size below which flat fees cannot be charged in default DC funds used for auto-enrolment, from April 2022.

The Government has published its response to the consultation on permitted charges within qualifying schemes for auto-enrolment. The consultation paper proposed that, from April 2022, providers should not be able to charge flat fees on small pots (of £100 or below) and that, longer-term, a universal charging structure should be introduced.

The response confirms that the Government will implement the de minimis cap from April 2022. The response suggests that there will be only minor changes to the proposals. On the basis of the consultation proposal, therefore, the cap will initially be set at £100 (and kept under review) and will apply to all members – active and deferred. If a member has multiple pots within the default arrangement, the assessment of whether a flat fee can be charged will be based on the combined value of the pots. A flat fee can be levied only once per member. Where a member has several small pots with different pension providers, then the de minimis will be applied according to the value of the members' pots, for each provider. The de minimis will relate only to the flat fee component of the combination charge used by providers - a percentage of funds under management charge can still be charged on all pots, irrespective of pot size.

The consultation also sought views on a proposal to change the current three permitted charging structures within the charge cap to a universal charging structure based on a single percentage annual management charge. The Government suggested that varied charging structures within the same auto-enrolment market might be acting as a barrier to members' ability to compare the costs of their pension with other pension products and schemes. The Government's response says that next steps will be published, in a separate response, "shortly". The response notes that there was a broad majority against the proposal to move to a universal charging structure, because of the risk it may cause fewer providers to offer pensions in the auto-enrolment market.

In the Autumn Budget, the Government announced it will consult on further changes to the charge cap for the default arrangements in auto-enrolment pension schemes, this time specifically considering amendments to the scope of the cap to "*better accommodate well-designed performance fees to ensure savers can benefit from higher return investments, while unlocking institutional investment to support some of the UK's most innovative businesses*". The consultation is promised before the end of the year. The Government will also continue wider policy work to understand and remove barriers to illiquid investment by pension schemes.

Next steps for trustees: Trustees need to be ready for administration changes (and costs) involved in monitoring small pots for the purposes of implementing the de minimis cap.

SUCCESSFUL RECTIFICATION OF PENSION INCREASE PROVISIONS IN SUCCESSIVE DEEDS

The High Court decided that, on the facts, mistakes in the pension increase rules in successive deeds, which had taken away the trustee power to select an index and replaced it with an employer power, were rectifiable. The corporate Trustee was able to provide convincing proof that its intentions, and those of the Principal Employer, were not properly reflected in the deeds. The case illustrates the importance when carrying out any form of Rules update or consolidation exercise of producing a careful contemporaneous "audit trail" of what was intended to change and what was intended to stay the same and of retaining that for future reference, as well as of following precisely the requirements of the amendment power.

In *Mitchells & Butler Pensions Limited v Mitchells & Butler Plc*, the High Court decided that "serial rectification" could be made where a mistake in changing the rule on pension increases had been replicated in later trust deeds. The original 1988 deed provided that the Trustee was entitled to select an index for determining the annual percentage increase to be applied to pensions in payment. An amended version of the deed and rules in 1996 erroneously contained a power for the Principal Employer (PE) to decide the rate of increase and omitted the Trustee's index-selection power. Subsequent deeds, in 2002 and 2006, perpetuated the error.

The Court conducted a detailed assessment of the evidence from 19 witnesses, 16 of whom gave oral evidence, and concluded that:

- The decision-makers for the Trustee and the PE had not intended to change the existing pension increase provisions in 1996. If any of them did read the new rule, they did not appreciate the effect of the words used; they assumed that the substance of the pension increase provisions remained unchanged.
- There was no intention to make any changes to the balance of power between the Trustee and PE, and no one had focused on the change to the pension increase provisions at this time.
- If such a change had been suggested, it would have been a major issue warranting detailed investigation and discussion, given the PE's "paternalistic" relationship with the members and the Trustee's view of its role as safeguarding members' benefits (particularly in the light of a possible hostile takeover).
- As regards the 2002 and 2006 deeds, "serial rectification" was available because the evidence of intention at the time of their execution was that the deeds should reflect the substance of the earlier provisions as their meaning was understood at the time of the later deed.

The PE tried to argue that it was a "bona fide purchaser for value" without notice of the earlier mistakes and therefore as an equitable matter took over free from the claim to rectify when it became PE in 2003 following a corporate reorganisation. The Court rejected this; the assumption of the rights and powers under a deed of substitution did not amount to a purchase of an interest in property (a requirement for the bona fide purchaser defence). In addition, the PE could not show that it did not have notice. Its assumption of the position of PE was in the context of a demerger and corporate reorganisation where there was continuity of management.

In any event, the erroneous amendments were void as invalid exercises of the power of amendment. There had been a failure to comply with the requirement to consult the scheme actuary. Consultation required sufficient information being supplied to enable the actuary to give advice. The Court noted that, where there has been a wholesale change in the drafting of a lengthy document, it may well be necessary for the nature of the alteration to be identified and explained in more specific terms; otherwise, there will not have been a proper consultation.

Next steps for trustees and employers: There are several well-established lessons here: producing an appropriate contemporaneous audit trail when conducting documentation update exercises (e.g. a table of destinations and derivations, with commentary on the intended effect of any differences and a clear statement that save as expressly stated in the table there is no intention to change benefits or the balance of power); and following precisely the requirements of the amendment power.

PENSION LEGISLATION AND REGULATION WATCH LIST

No	Topic	Expected effective date	Further information/action
1	Annual statement on compliance with policy on stewardship and engagement activities, and voting behaviour, on website	1 October 2021	DB schemes. The requirements for DC schemes applied to annual reports signed off on or after 1 October 2020.
2	Draft DB Funding Code of Practice	Regulations expected for consultation before end of 2021 Part 2 of consultation on draft Code expected in the first quarter of 2022; new Code expected to be operational December 2022	Once in force, the Code will apply to triennial valuations submitted thereafter.
3	TPR consolidated Code of Practice	By end June 2022	TPR consultation issued 17 March 2021 and interim response issued August 2021.
4	Climate risk governance and reporting requirements	1 October 2021	For all authorised master trusts and collective DC schemes and schemes with £5 billion or more in net assets on the first scheme year end date on or after 1 March 2020, governance to be in place for the scheme year underway and the first annual report to be published within seven months of the end of the scheme year.
5	Changes to DC scheme governance and disclosure, including the annual Chair's statement and the charge cap	First scheme year ending after 1 October 2021 (changes to Chair's statement); 5 October 2021 (changes to annual scheme return); first scheme year ending after 31 December 2021 (detailed value for money assessments for schemes with assets below £100m). April 2022: introduction of £100 de minimis pot size below which flat fees cannot be charged	DC schemes only. DWP to confirm whether look-through mechanism for charge cap compliance will be amended or removed. DWP to review whether fines for non-compliance with Chair's statement requirements should be mandatory. DWP proposals on universal charging structure to follow.

No	Topic	Expected effective date	Further information/action
6	Restrictions on transfers of a member's cash equivalent transfer value by trustees/managers of occupational or personal pension schemes unless prescribed conditions are met	Transfers where the date of the member's application for a statement of entitlement (DB schemes) or transfer request (DC schemes) occurs on or after 30 November 2021	Final regulations issued November 2021.
7	DB superfunds	Regulatory regime expected Winter 2021	Interim regulatory regime in place from October 2020.
8	Refer members to guidance before processing application to access or transfer flexible benefits	April 2022	For DC schemes only. Consultation on draft regulations closed 3 September 2021.
9	Trustee oversight of fiduciary managers and investment consultants	Under the Investment Consultancy and Fiduciary Management Market Investigation Order 2019, compliance statements, confirming the extent to which requirements have been met, have to be provided to CMA by 7 January 2022.	Consultation response and new DWP regulations have been delayed until June 2022.
10	Register certain trusts with the Trust Registration Service	Registration by 1 September 2022	Applies to some trusts relating to pension and life assurance benefits where no exemption applies (e.g. bare trusts set up on distribution of a lump sum).
11	Simpler annual benefit statements	1 October 2022	DC schemes used for auto-enrolment.
12	Changes to scheme asset information collected through scheme returns	Scheme returns from 2023	DB schemes.

London
T +44 (0)20 7600 1200
F +44 (0)20 7090 5000

Brussels
T +32 (0)2 737 94 00
F +32 (0)2 737 94 01

Hong Kong
T +852 2521 0551
F +852 2845 2125

Beijing
T +86 10 5965 0600
F +86 10 5965 0650

574695961