SQUIRE PATTON BOGGS

PENSIONS FIT
THE TRUSTEE'S GUIDE TO TRICKY TRANSFERS

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Processing member transfer requests is a routine task for those involved in the running of pension plans. However, recent changes in legislation and practice will dramatically impact on this process. Trustees of pension plans should be keeping track of developments and updating their transfer procedures, member communications and documentation to reflect the new regime.

In this publication we flag some of the important developments that trustees should consider when a pension plan member asks to transfer his benefits to another arrangement and actions that they will need to take in response to the new legislation and industry practice.

A Change to Statutory Transfer Rights

The legislation governing when a member has a statutory right to transfer benefits from one pension arrangement to another was overhauled on 6 April 2015 as a result of amendments contained within the Pension Schemes Act 2015.

The Pension Schemes Act 2015 introduced a right for a member to transfer a "category" of benefits, whilst leaving benefits belonging to another category behind in the pension plan, or even continuing to accrue rights to that other category of benefit. For these purposes "category" has a particular definition under the Act (benefits are split into three categories: "money purchase benefits", "flexible benefits other than money purchase benefits" and "benefits that are not flexible benefits"). In practical terms, the new legislation could, for example, allow a member of a hybrid pension arrangement, with both defined benefit and defined contribution elements, to transfer out just his DC benefits and retain his DB benefits within the pension plan (or vice versa). Many DB pension plans have an AVC facility that operates on a money purchase basis – the changes to statutory transfer rights means a member could potentially transfer his AVC pot in isolation.

In addition, the rules regarding transfers of "flexible benefits" (broadly speaking DC or cash balance benefits) are further relaxed, so that individuals with flexible benefits are able to exercise a statutory right to transfer those flexible benefits up to and beyond their pension plan's normal pension age.

Trustees of occupational pension plans should ensure their transfer processes are updated to reflect the new statutory right for members to transfer different categories of benefits. Legal advice may be necessary to identify the different categories of benefits in the pension plan. Member communications may require updating and trustees should consider how members will be informed of any new transfer rights. It is likely that transfer documentation, for example discharge forms, will also require updating.

The new statutory transfer rights will override contrary provisions in pension plan rules. However, trustees and employers may wish to amend pension plan rules so that they reflect the new legislation.

Transfers of "Safeguarded Benefits" – the "Appropriate Independent Advice" Requirement

Trustees of DB plans will need to familiarise themselves with another change to transfer processes introduced by the Pension Schemes Act 2015 – the requirement to confirm an individual[1] has taken "appropriate independent advice" before making a transfer payment in respect of his "safeguarded benefits" (broadly speaking, DB benefits) to another pension plan where the transfer is being requested with a view to acquiring flexible benefits in that other pension arrangement.[2]

Regulations[3] which came into force on 6 April 2015 stipulate how and when trustees must confirm the individual has received the necessary advice and when an employer must arrange or pay for the provision of that advice. Set out below are the key features of the new Regulations.

- Where the value of an individual's safeguarded benefits under a pension plan is more than £30,000, that individual must obtain appropriate independent advice regarding a proposed transfer and the trustees cannot process the transfer payment until they have received a statement from a suitably qualified adviser confirming that the individual has received that advice.
- The trustees must flag to the individual that they will need to check that the individual has received appropriate independent advice before the transfer can go ahead, provide information on the evidence that the trustees will need and explain that, unless the individual confirms otherwise, the trustees will assume the purpose of any transfer of the safeguarded benefits is to provide flexible benefits under another pension arrangement.

1 It is not just members who are caught by the requirement to obtain appropriate independent advice – the requirement also applies to survivors who are entitled to safeguarded benefits under the pension arrangement following the death of a member.

2 Note that a transfer payment relating to safeguarded benefits is not the only occasion where trustees are required to check that an individual has obtained appropriate independent advice – the legislation lists other occasions when this is necessary, including the conversion of safeguarded benefits into flexible benefits within the same pension plan.

3 The Pension Schemes Act 2015 (Transitional Provisions and Appropriate Independent Advice) Regulations 2015.

- Trustees do not need to check the content of the advice or whether the individual has decided to follow it.
- Trustees do, however, need to check that the company or business providing the advice has permission to carry on the regulated activity of "advising on conversion or transfer of pension benefits", by checking the Financial Services Register maintained by the Financial Conduct Authority.
- An employer must arrange or pay for the provision of the appropriate independent advice if it (or someone on its behalf - including the pension plan trustees) has written to two or more members or survivors, setting out the options available in terms that "encourage, persuade or induce" the individual to act in a way that triggers the requirement for appropriate independent advice to be obtained. Care must be exercised, therefore, when communicating with members and survivors about their options.

If the rules of a pension plan require trustees to pay a transfer of a member's safeguarded benefits without regard to whether the member has received the necessary advice, then a new statutory modification power may assist. The new power allows trustees to modify those rules by resolution to provide that they are not required to make the transfer if they are unable to confirm that the member received the appropriate independent advice (either because they were unable to check the position due to factors outside their control or because the checks they carried out did not confirm that the individual received the advice). Trustees should review the transfer provisions in their pension plan rules to assess whether rule amendments are appropriate.

New Pensions Regulator Guidance

The Pensions Regulator has issued guidance "DB to DC transfers and conversions", which provides further information on the issues that trustees of DB pension plans will need to address as more members wish to transfer out DB benefits in order to take advantage of the new DC flexibilities.

As well as explaining the appropriate independent advice requirement, the guidance also urges trustees to take a number of practical steps to ensure that the transfers are processed correctly and the impact of transfers on the plan is managed effectively. These recommendations include the following actions.

- Putting processes in place to implement transfer requests in a timely manner and maintaining accurate and complete records of transfer requests and transfers made.
- Monitoring and understanding demand from members for transfers and the subsequent impact those transfers could have on scheme funding and investments, including the liquidity required to pay large numbers of individual transfers and the impact of transfers by members with large transfer values relative to the plan.
- Balancing their responsibilities to transferring members with those remaining in the pension plan. In some situations reducing transfer values where a pension arrangement is underfunded may be appropriate.
- Conducting due diligence on the receiving pension plan to ensure that it is able and willing to accept the transfer and is a legitimate arrangement (see the section on Pension Scams below).
- Reviewing and updating member communications.

The new guidance is essential reading for trustees of pension arrangements providing DB benefits, who should check whether their plan meets the Regulator's expectations.

Pension Scams

Pension plan trustees are still struggling to prevent their members from becoming victims of pension scams (also known as "pensions liberation"). The Pensions Regulator has recently launched a new campaign, urging pension savers to "scamproof their savings" and HMRC is tightening up the rules regarding the registration and running of pension arrangements. However, trustees are still left in a difficult situation if a member insists on exercising a right to transfer benefits, even if the trustees suspect that this is part of a scam.

The Pensions Ombudsman is facing a flood of pension scam member complaints and has recently issued a series of determinations on this difficult area. Its determinations cover complaints from disgruntled members whose transfer requests were refused due to suspected pension scam activity and complaints from members whose pension savings were transferred and now claim that the original pension plan should have warned them against doing so.

Of particular interest are the determinations relating to complaints that transfer requests have been blocked by a pension arrangement[4]. In each of these cases the Pensions Ombudsman examined in great detail whether the member had a right to the transfer requested, either in statute or under the transferring pension plan's own provisions. Trustees and pension providers face an onerous task if they aim to apply a similar level of scrutiny as the Pensions Ombudsman when evaluating transfer requests.

To assist trustees and pension providers an industry group has produced a Code of Practice "Combating Pension Scams". Compliance with the Code is voluntary. However, the Code sets out an industry standard due diligence process for trustees to follow when considering a transfer request, together with information on matters such as raising member awareness of pension scams and how to report suspicious cases. The Code also includes example correspondence and forms, although any documentation must be carefully tailored to the pension plan and the circumstances in question, and should be reviewed by the pension plan's legal advisers. We particularly recommend that trustees undertake a rigorous review of discharge forms that members are expected to sign before proceeding with a transfer. In the current environment these forms may play a crucial role in protecting trustees from member complaints regarding a transfer once it has been made.

The Pensions Regulator materials, Pensions Ombudsman determinations as well as the Code of Practice make it clear that trustees have a critical role to play in increasing member awareness of the risks posed by pension scams. Trustees should review how their member communications and transfer processes address this.

We also recommend that trustees of all types of pension plan familiarise themselves with the latest pension scam developments, including the materials published by the Pensions Regulator and the new Code of Practice, and examine their processes for identifying, assessing and dealing with suspicious transfer requests.

4 Zurich Personal Pension Plan (PO-1837), AVIVA Personal Pension Scheme (PO-3809), Standard Life Self Invested Personal Pension Scheme (PO-3105) and Prudential Personal Pension Scheme (PO-3184).

Suggested trustee actions

- Identify the different categories of benefits within the pension plan to understand members' statutory transfer rights
- Ensure trustees are familiar with the following
  - The Code of Practice "Combating Pension Scams"
  - The Pensions Regulator's Guidance "DB to DC transfers and conversions"
  - The latest materials published by the Pensions Regulator on pension scams
- Review transfer processes, including the following considerations
  - Check whether the expectations of the Pensions Regulator regarding DB to DC transfers and conversions are met
  - Do the transfer processes accommodate the new statutory transfer rights?
  - Have transfer processes been updated to incorporate the requirement that a member obtains "appropriate independent advice" before transferring safeguarded benefits?
  - Ensure there are adequate measures in place to identify pension scams and deal with suspicious transfer requests
  - Review how cash equivalent transfers are calculated and, if the scheme is underfunded, consider whether transfer values should be reduced
  - Are procedures in place to monitor demand for transfers and the impact of transfers on pension plan funding and investments?
- Review transfer provisions in the pension plan rules
  - Should the rules be updated to reflect the new statutory transfer rights?
  - Consider the use of the new trustee resolution amendment power
- Review and update member communications and transfer documentation, particularly discharge forms
- Consider trustee training to assist trustees with understanding the relevant legislative requirements, changes to industry practice and the impact on the pension plan

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