

The State Second Pension will be abolished from 6 April 2016. From this date, all pension plans that still contract-out of the State Second Pension will cease to do so. As a consequence, sponsoring employers and active members of these pension plans will see their lower, contracted-out National Insurance contribution rates end. Employer and active member NI contributions will increase to the standard rate.

Regulations<sup>1</sup> are now in force which will allow a private sector pension plan to be amended by its sponsoring employer, so as to offset the effects of the end of lower employer NI contributions from 6 April 2016. This statutory amendment power lies with the employer alone, will not require the consent of trustees or members, and can be exercised regardless of any restrictions in the pension plan rules. Amendments can be made at any time from now until 5 April 2021 but will only be able to operate on or after 6 April 2016.

Employers who wish to amend their pension plan from the earliest possible effective date are advised to start acting well in advance of their target implementation date due to the process that has to be completed. Our process map overleaf highlights the key stages and actions for employers.

### What Can an Employer Do Where Its Pension Plan Benefits Will Continue to Accrue After 5 April 2016?

Using the statutory amendment power, employers can increase member contributions or decrease future benefits (or a combination of both). These changes can only take effect from 6 April 2016, or a later date if the employer chooses. The employer must first obtain an actuarial certificate, to indicate these changes do not result in cost savings in excess of the amount required to offset the annual increase in the employer's NI contributions.

The employer will need to appoint an actuary to carry out the calculations and provide the certification – this is unlikely to be the pension plan's appointed actuary due to potential conflict issues with his role in advising the trustees.

### What Employers Cannot Do

Employers cannot use the statutory amendment power to:

- decrease their own contributions to the pension plan;
- make changes for employees who have 'protected person' status (this is set out in the regulations and applies to certain previous employees of some former nationalised industries); or
- alter the pension plan in a way that would change the balance of powers in that pension plan.

### The Employer's Interaction With Its Actuary

The employer will need to enter into discussions with its actuary to establish what it wants to achieve within the boundaries set out in the regulations. The actuary will also advise on the data that he needs to undertake the necessary actuarial calculations, which will include employee earnings information and potentially some data that is held by the pension plan trustees.

When carrying out his calculations, the actuary will use the methods and assumptions already used to calculate the plan's technical provisions – updated as necessary to reflect market conditions between the date of the last valuation and the chosen calculation date. The employer will choose the calculation date, which can be any date after 31 December 2011, and can request that actuarial assumptions are adjusted to a best estimate basis by removing margins for prudence. The actuary can also use employee earnings data from the three year period (rather than one year) leading up to the calculation date if the earnings data from the one year period is "significantly abnormal".

In practical terms, the employer may want to engage with the actuary to understand the effects of setting different calculation dates, varying the assumptions and/or using different employee earnings data (and the extent to which such variations are material in terms of the precise amendment that the employer would like to make). Although the employer is responsible for setting the calculation date it will require help and advice to establish which date best reflects its objectives. Changing the calculation date may produce a significantly different result in terms of the amendment that is possible using the statutory amendment power. Employers will have different views on how important it is for them to investigate these issues fully.



<sup>1</sup> The Occupational Pension Schemes (Power to Amend Schemes to Reflect Abolition of Contracting-out) Regulations 2015.

## Employer's Process Map

We set out below our suggested overview of the amendment process. Employers may wish to use this map to formulate their own project plan. We have flagged areas where we foresee the potential for stages in the process to take time to complete, and where the employer may wish to build in extra practical steps.



## Consultation With Employees

Where changes are proposed to pension plan rules, the existing employee consultation requirements will apply. The consultation must be carried out by the employer and:

- must involve all affected employees – this includes prospective members of the pension plan (for example, employees that can join the plan in the future at their own option, at the expiry of a waiting period or with employer consent);
- must run for a minimum of 60 days;
- should clearly communicate the amendments that the employer is proposing to make and how this will impact on affected employees;
- should be a genuine consultation, and not pre-judge the outcome.

Further to this, in its response to consultation, the DWP stated that it is “critical” that employer proposals are transparent, and also that the proposals should be equitable across different groups of pension plan members.

## Practical Issues

Employers may need to request information from the trustees in connection with the proposed amendment of the pension plan.

The amendment power can be exercised more than once in relation to the same members – so if an employer does not wish to recoup the full cost of its NI increase when it first acts on this issue, it can make further amendments at any point before 6 April 2021. However, the original calculation date must be used in relation to subsequent amendments.

Employers should not overlook obligations owed to employees outside of the pension plan rules, which could impact on their ability to make changes to the pension plan, for example, any pension rights granted under contracts of employment. Employment law advice may be required.

## Use of the Pension Plan’s Own Amendment Power

Although employers have a statutory power to amend the pension plan to recoup their increased NI costs, there is nothing in legislation to prevent employers from using the amendment power contained in the pension plan rules for the same purpose (although the terms of the amendment power and any consultation obligations must be observed). A rule amendment may well be needed where an employer wishes to make more extensive changes than those which would just offset the increase in its NI contributions. Where the rules require trustees to agree to rule amendments, employers would need to work with the trustees to obtain their agreement, alongside any wider discussions about employer support of the pension plan.

## Multi-employer Pension Plans

If a pension plan has more than one employer (or if a sectionalised pension plan has more than one employer in relation to each section), it is the “principal employer” who may exercise the statutory amendment power. The “principal employer” is defined in the regulations as the employer who is nominated to act on behalf of the other employers on matters relating to scheme funding or, if there is no such nominee, the employer who is specifically nominated to act on behalf of the other employers for the purpose of exercising the statutory amendment power. If nomination of a principal employer is necessary then the participating employers will need to reach agreement on the nomination process for their own pension plan. Participating employers will also need to address concerns that may arise in sharing data with the nominated principal employer (from a data protection perspective and/or a commercial sensitivity perspective).

### A Few Extra Notes for Trustees ...

1. The trustees must provide any information that is reasonably requested by the employer in connection with the exercise of the statutory power and they need to agree a reasonable period in which the information will be provided. Penalties apply to trustees who do not take all reasonable steps to comply. Trustees should take legal advice if they have any concerns regarding data protection issues when providing information to the employer.
2. Before giving their agreement to any use of the pension plan’s amendment power, trustees should be mindful of the fact that the employer would still be able to make use of the statutory override power at a later date, to make further amendments without their agreement. Taken together, this could result in overall cost savings exceeding the amount required to offset the increase in the employer’s NI contributions. Trustees should seek legal advice before giving their agreement to any use of the pension plan’s amendment power.
3. Depending on the amendment that is made, trustees may need to review the scheme funding documents, including the schedule of contributions.
4. Trustees may wish to seek advice from their own professional advisers in order to verify that the amendment meets the statutory requirements, and to consider appropriate action if not.

## A Collaborative Approach

This is the first time that employers have been given a unilateral statutory power to amend their pension plan. Although there is no requirement for trustee approval or consent to the use of the statutory amendment power we would encourage good lines of communication between employers and trustees. Once the amendment is made, trustees will be required to implement it, including the usual processes of: liaising with advisers; ensuring that the pension plan is correctly administered on the amended basis; updating member communications; dealing with questions or complaints; and ensuring that the pension plan documentation is in order. Trustees can only carry out these duties if the amendment is clear and accurately documented. They may wish to seek advice from their own professional advisers in order to establish this. *It is in the best interests of all parties that time is taken in the amendment process to allow the trustees and employer to each be content that any changes will work and be implemented effectively.*

## Further Information

For further information please contact any of the partners listed, or your usual contact in the Squire Patton Boggs pensions team.

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