

# What the Regulator expects...

a field guide for trustees



# Contents

Setting the scene.....	1
Whistleblowing .....	2
Notifiable events.....	3
Internal controls.....	4
Conflicts of interest and duty .....	5
Trustee knowledge and understanding.....	6
Member-nominated trustees (MNTs).....	7
Internal dispute resolution (IDR) .....	8
Early leavers.....	9
Amending the scheme .....	10
Funding (only relevant to defined benefit trustees).....	11
Corporate activity (moral hazard powers and clearance).....	12
Cross-border schemes.....	14
Scheme abandonment.....	15
Late payment of contributions in defined contribution schemes .....	16
Communications with members of defined contribution schemes .....	17
Want more information? .....	18



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# Setting the scene

The Pensions Regulator has high expectations of you as a trustee and has published many hundreds of pages of information detailing them. This Guide highlights the key aspects of the Regulator's publications and will help you to build up a working understanding of what the Regulator expects of you.

Each section contains the key points from the Regulator's guidance, references to relevant Regulator publications and other useful information. If you want to learn more, a section at the back of this Guide points you in the right direction.

This Guide is a summary of what the Regulator has published to date and is not of course a substitute for professional advice about any specific situation.

## Role of the Pensions Regulator

Since 2005, the Regulator has been responsible for ensuring that occupational pension scheme trustees comply with their numerous statutory duties. The Regulator's statutory objectives also include:

- ✔ protecting members' benefits
- ✔ reducing the chance of claims being made on the Pension Protection Fund (PPF)
- ✔ promoting better scheme administration.

## Regulator publications

The Regulator has published a large volume of material aimed at meeting its objectives. It has a clear expectation that trustees will be aware of and act on their content. The different types of publication issued by the Regulator are:

- ✔ **Codes of Practice:** contain practical guidance in relation to compliance with legislation. They are not statements of the law and there is no penalty for failing to comply with them. The Regulator says that it is not necessary for all the provisions of a code to be followed in every circumstance. However, when determining whether legal requirements have been met, a court or tribunal must take any relevant codes of practice into account.
- ✔ **Guidance:** aims to share good practice and provide practical support. Again, there is no legal obligation to follow it, but trustees should expect that the Regulator will want them to have acted in accordance with its guidance and may seek to use its powers where they have not.
- ✔ **Other:** there is a variety of other publications issued by the Regulator aimed at educating trustees including updates and consultation papers. Trustees need to be aware of these as well.

## Regulator's powers

The Regulator has extensive powers of intervention and sanction, which include:

- ✔ **finances** – for non-compliance with legislative requirements of up to £50,000 for trustee companies or £5,000 for each individual trustee. Fines cannot be paid out of scheme assets. Fines can also be imposed directly on directors of corporate trustees where a director was responsible for the non-compliance.
- ✔ **criminal sanctions** – a few statutory requirements attract criminal penalties for non-compliance. These include breach of the restrictions on employer related investments.
- ✔ **appointment and removal of trustees** - can be done for various reasons, all aimed at improving management of the scheme.
- ✔ **improvement notices** – directions to take specific actions or to stop doing particular things.
- ✔ **winding-up the scheme** - where it is in the interests of the scheme members to do so.

# Whistleblowing

## Overview

The Regulator often becomes aware that a scheme has not been run in accordance with legal requirements by reports from “whistleblowers”. As a trustee, you have to report to the Regulator where you have “reasonable cause to believe that... a duty ... imposed by... law, has not been... complied with, and... the failure to comply is likely to be of material significance to the Regulator in the exercise of any of its functions”.

## Key points

- applies to trustees (but not each director of a corporate trustee, although they do each have a duty to ensure that the trustee company complies with the whistleblowing requirements)
- also applies to advisers (except generally legal advisers), administrators and employers
- overrides any duty of confidentiality (except legal privilege)
- always report a breach caused by dishonesty, poor governance, poor advice or deliberate contravention of the law
- an isolated incident which has been corrected will not usually give rise to a duty to report
- a report should be made as soon as reasonably practicable. This depends on circumstances but will usually mean days rather than weeks
- you should have a reporting procedure in place – if you are not sure, check
- reports must be in writing through the Exchange system which you can access on the Regulator’s website
- failure to report without “reasonable excuse” is a civil offence
- if in doubt, seek legal advice

## Examples from Regulator of how to treat different breaches

Green breaches – need not be reported	Amber breaches – depends on the circumstances	Red breaches – must be reported
Occasional administrative lapses in a well run scheme where action taken to put matters right and prevent recurrence	Several “green” breaches within a short period – consider underlying cause and how it has been dealt with	Where there is a criminal penalty eg employer-related investment or acting as a trustee whilst disqualified
Failure to follow detail of the legislation where breach is unlikely to result in an error or misunderstanding	Auditor discovers benefits for some members have been wrongly calculated – consider how many are affected and why did it happen	Matters indicating possible dishonesty or misuse of assets or contributions
Breaches arising from trustees’ inaction where doing nothing is a temporary and practical response to circumstances outside their control	Failure to follow the requirements of the Scheme Rules – consider why and what the impact is on members	Failure of the trustees to review investment policy in light of significant changes to circumstances
	Failure to obtain an actuarial report on time – consider whose fault was the delay and how long is it	Trustees revise a statement of investment principles without consulting the employer
		Persistent failure to obtain auditors’ statements on contributions or audited accounts
		Trustees taking decisions on matters which require professional advice without obtaining it

## For more information...

- Regulator’s Code of Practice No. 1 – Reporting breaches of the law
- Regulator’s Guidance on reporting breaches

# Notifiable events

## Overview

One of the Regulator's objectives is to minimise the possibility of schemes claiming on the Pension Protection Fund (PPF). Trustees of defined benefit schemes are therefore required to notify the Regulator of certain events which might make a claim on the PPF more likely. The intention is that notifiable events will provide an early warning of possible insolvency or underfunding giving the Regulator the opportunity to assist, or to intervene, before a call is made.

## Key points

- ✔ applies to each trustee (but not each director of a corporate trustee, although they do each have a duty to ensure that the trustee company complies with these requirements)
- ✔ overrides any duty of confidentiality (except legal privilege)
- ✔ notify as soon as reasonably practicable - this depends on circumstances but implies urgency (eg next day)
- ✔ made in writing – there is a form on the Regulator's website
- ✔ you should have a procedure in place to ensure notifiable events are reported – check if not sure
- ✔ the Regulator has a range of actions it can take for non-compliance including civil penalties
- ✔ employers have similar duties to notify specified events relating to them

## Notifiable events

Event	Does it always need to be notified?
Transfer payments in or out of more than either 5% of scheme assets or £1.5million	Not if funding is above the level where the scheme would potentially be eligible to enter the PPF and trustees have not needed to report any non-payment under schedule of contributions in last 12 months
Trustee decision to grant benefits to a single member worth more than either £1.5million or 5% of scheme assets	Not if funding is above the level where the scheme would potentially be eligible to enter the PPF and the trustees have not needed to report any non-payment under schedule of contributions in last 12 months
Trustee decision resulting in non-payment of an employer debt to the scheme	Not if the uncollected debt is less than 0.5% of scheme assets, funding is above the level where the scheme would potentially be eligible to enter the PPF and the trustees have not needed to report any non-payment under schedule of contributions in last 12 months
Augmenting member benefits without either seeking actuarial advice or securing additional funding advised by the actuary	Always

## For more information...

- ✔ Regulator's Code of Practice No. 2 – Notifiable Events
- ✔ Regulator's Guidance on Notifiable Events
- ✔ Regulator's Summary of conditions which apply

# Internal controls

## Overview

Trustees of an occupational pension scheme must “*establish and operate internal controls which are adequate for the purpose of securing that the scheme is administered and managed in accordance with the scheme rules, and...the requirements of the law*” (Pensions Act 2004).

## Key points

- you must decide what internal controls are needed to make sure your scheme is well managed in accordance with the law and scheme rules
- internal controls are administrative procedures, systems for monitoring administration and management and procedures to ensure the safe custody and security of scheme assets
- internal controls should be appropriate to the nature and size of the scheme. Smaller schemes may require less formalised controls than larger schemes
- internal controls should be reviewed at least annually or sooner if substantial changes take place, such as a deterioration in funding, or where an existing control has been found to be inadequate
- if inadequate internal controls are in place, there are no specific statutory penalties, but trustees will need to consider whether they will need to whistleblow on themselves to the Regulator

## Examples of risks and appropriate controls

Risk	Possible types of control (where appropriate)
Fraud (misappropriation of assets and fraudulent financial reporting)	Segregation of duties; frequent reconciliation procedures for cash and investment balances
Corporate risk (risk of deterioration in employer covenant and ongoing funding)	Monitor strength of covenant, put procedures in place to detect corporate transactions in the public domain and assess impact on the scheme
Funding/investment (inappropriate investment strategies)	Reconciliation procedures; review of investment strategies; independent review of funding advice
Compliance/regulatory risk	Compliance audits; stewardship and compliance reports from third parties
Non-compliance or maladministration by administration team or third party advisers	Review of key controls by administration team; authorisation procedures; periodic meetings between trustees and provider; service level agreement reviews; performance appraisal of providers; internal review procedures by administrators.
Computer system and database failures	System recovery plans; data back-up procedures; password controls
Poor scheme management	Regular trustee meetings; decisions taken within those meetings; minutes prepared for all meetings; sub-committees; manage conflicts of interest
Existing controls are not operating effectively	Periodic review of controls with changes made on a timely basis

## For more information...

- Regulator’s Code of Practice No.9: Internal Controls
- Regulator’s Guidance on Internal Controls

**Note:** The Regulator has published revised draft guidance on internal controls which is currently open for consultation. The new draft contains considerably more detail on what appropriate internal controls are so trustees revising internal controls need to check which version of the guidance is currently in force.

# Conflicts of interest and duty

## Overview

Trustees have a trust law duty to avoid situations where they have an actual or potential conflict between (i) their personal interests and the interests of scheme beneficiaries or (ii) the duties they owe to a third party (such as their employer) and those they owe as a trustee.

## Key points

- you should understand the law relating to conflicts
- there should be a register of existing or potential trustee conflicts (this would include membership of the scheme or holding office with the employer)
- you should have a procedure to identify and deal with conflicts and all of the trustees should be familiar with this procedure
- a trustee should operate on the assumption that they are under an obligation to disclose all relevant information they hold (in any capacity) to other trustees. This can give rise to conflicts for trustees who are likely to be in receipt of sensitive information about the employer and such potential conflicts should be managed through the agreement of all of those involved
- some of the duties on conflicts and disclosure may be displaced by provisions in the scheme rules and you should be aware of the relevant provisions
- it is good practice for the first matter on the agenda at each trustees' meeting to be conflicts, even if it is to disclose that there is none. This should be recorded in the minutes of the meeting

## Additional issues for corporate trustees

- the position is more complex where you are a director of a trustee company as there are also provisions in the Companies Act 2006 dealing with conflicts of interest and duty
- as well as looking at any provisions in your trust deed on conflicts, you will also need to consider the trustee company's articles of association. The articles may allow you to continue to act if you have a conflict of interest or duty providing you declare it to the other trustees. However, they may contain restrictions on when and how you can continue to act and you need to be aware of these
- if there is nothing in the trustee company's articles of association dealing with conflicts of interest, then you may need to consider amending them

## For more information...

- Conflicts of interest – Regulator's summary guidance
- Conflicts of interest – Regulator's full guidance

# Trustee knowledge and understanding

## Overview

Legislation requires trustees to be conversant with the scheme documents and to have knowledge and understanding of the law relating to pensions and trusts and the principles of scheme investment and funding.

## Key points

- you must know enough to appreciate when to seek professional advice and to understand that advice
- new trustees have up to 6 months to get up to speed but if in that time you have a decision to make, you must know enough to make the decision properly. You can start learning before you are appointed
- trustees in specific roles (eg on an investment committee) are expected to have higher levels of relevant knowledge than other trustees
- the chair of trustees or a sub-committee may need to have more knowledge as other trustees may rely upon him for help and support and a chair should be able to carry out these responsibilities from the date of appointment
- you need to be conversant with the trust deed and rules, member booklets, agreements with advisers, statements of investment and funding principles and any other documents dealing with the running of the scheme. Keep a file of relevant documents (either in hard or soft copy)
- you are responsible for keeping your knowledge up to date and should keep a record of how you have done this.
- read the relevant "Scope" document which explains the extent of the knowledge the Regulator expects trustees to have. Use it as a checklist to identify gaps in your knowledge
- the trustees as a whole should discuss how they are complying with these requirements

## Some of the specific things you need to know

DB and DC	DB only	DC only*
Basic trust law requirements: trustee duties and powers, balance of power, conflicts of interest, role of advisers, taking and leaving office, protection of trustees, responsibility for scheme governance	Role of advisers in restructuring or where threat to employer covenant	How DC arrangements work, their administration and investment risk is borne by members
Key provisions of pensions and other relevant legislation, the tax regime, relationship between state and occupational pensions and provisions in relation to qualifying schemes which apply from 2012	PPF guidance, regulator's powers in relation to sponsoring employers. How scheme funding works and how assets and liabilities are valued	The provisions of the Finance Act which allow a cap to be put on contributions.
Major asset classes, risk v reward, existence of specialised asset classes, implications of overseas investment	How asset liability matching works, principles of strategic asset allocation	Default funds and lifestyling arrangements, matching assets to expectations
Principles of fund management, how performance can be measured and selection of fund managers	Process for determining contributions and relationship between trustees and employer	Where investment choices are offered to members, how those choices work

*\*if you are a trustee of a fully insured defined contribution arrangement with fewer than 100 members, the scope of knowledge that you are required to have is lower and is set out in a separate scope document*

## For more information...

- Regulator's Code of Practice No. 7 - Trustee Knowledge and Understanding
- Regulator's Scope document for DB schemes (with associated DC element)
- Regulator's Scope document for DC schemes
- Regulator's Scope document for small fully insured DC scheme

# Member-nominated trustees (MNTs)

## Overview

Almost all schemes must ensure that at least one third of the trustees (or directors of the trustee company) are member-nominated.

## Key points

- decide on the appropriate number of MNTs for your scheme. For example, if there are 10 trustees, there will need to be at least 4 MNTs
- the MNT requirements do not apply where all of the trustees are independent (as defined in the legislation)
- the requirements are broadly the same whether the scheme has individual trustees or a corporate trustee. In the case of a corporate trustee, the requirements apply to its directors
- you must have procedures for the nomination and selection of MNTs. When designing procedures you must have regard to the principles of proportionality, transparency and fairness
- the nomination process must be open to all of the active and pensioner members (or organisations representing them). You have discretion whether to include deferred members. It may be possible to have different MNTs appointed by different classes of member
- the selection process must involve “some or all” of the members. This means that it must involve a minimum of 2 members (they may also be existing trustees). The process can be whatever you think is appropriate, including ballots and selection panels
- whatever process is adopted, you will need to communicate with the members (to invite nominations and possibly as part of the selection process)
- consider issues such as the term of office and whether an MNT should leave office if they cease to be an employee or an active member
- keep a record of all of the steps taken to comply with the MNT requirements
- if insufficient MNTs are appointed, the process for nomination and selection should usually be run again within 3 years
- procedures must usually be reviewed every 3-5 years

## For more information...

- Regulator’s Code of Practice No 8: MNTs/MNDs – Putting arrangements in place
- Regulator’s Guidance: Member-nominated trustees and member-nominated directors

# Internal dispute resolution (IDR)

## Overview

Since 1997 schemes have had to have an internal dispute resolution procedure to deal with disputes between beneficiaries and trustees. Originally it had to be a two stage procedure with strict time limits. However, this has been simplified and trustees can now choose to have a one or two stage procedure and the time limits are set out in a Code of Practice issued by the Regulator.

## Key points

- if you opt for a one stage IDR process, a trustee board decision about the dispute is required
- if you opt for two stages, the first stage decision is made by a named decision-maker (eg the pensions manager, secretary to the trustees or a particular trustee) with the trustees reviewing that decision as stage two if the beneficiary does not accept the stage one decision
- generally, a complaint should be brought within 6 months of a person ceasing to have an interest in the scheme (although trustees may accept complaints brought outside this period)
- a decision on a complaint must usually be given within 4 months. Where the IDR procedure is in two stages, the 4 month time limit applies to each stage
- decisions should be notified to complainants within 15 working days
- these time limits may be varied depending on the circumstances
- if you currently have a two stage procedure and decide to move to a single stage procedure, members will need to be notified of the change. This can be done in the next communication you would normally send to members

## Information complainants must be given

Event	What information	When
Complaint received	That the Pensions Advisory Service (TPAS) is available to assist them and what its contact details are	As soon as reasonably practical after receiving the complaint
Stage 1 decision (if scheme has two stage process)	The decision from stage 1 and statement that the complainant can progress to stage 2	Within 4 months of receiving the complaint and within 15 working days of making the decision
Stage 2 decision or decision by trustees if single stage process	The trustees' decision and the contact details for the Pensions Ombudsman together with a statement of what he does	Within 4 months of the complaint being referred to the trustees and within 15 working days of making the decision

## For more information...

- Regulator's Code of Practice No. 11: Dispute Resolution – Reasonable Periods
- the information requirements are set out in The Occupational Pension Schemes (Internal Dispute Resolution Procedures Consequential and Miscellaneous Amendments) Regulations 2008

# Early leavers

## Overview

Members who leave pensionable service after less than 2 years do not usually have to be given pension benefits in the scheme. However, members with at least 3 months service have a right to a refund of their own contributions or a transfer payment. Those with at least 2 years service also have a right to a transfer payment. Members with less than 3 months service do not need to be offered any benefits but it is common to offer a refund of their contributions.

## Key points

### Where member leaves pensionable service with between 3 months and 2 years service:

- You normally have 3 months to give members a statement explaining that they have a right to either a refund of their own contributions or to take a transfer and how much each is worth
- If you know you cannot make this notification within 3 months, you should tell the member and keep them updated
- The statement must include the last possible date for the member to reply to the trustees. 3 months is a reasonable period and if the member asks for longer, you may agree but are not obliged to do so
- Members should also be told how to communicate their decision to the trustees
- Once the member has told you what they want done, you must normally act within 3 months, but may take longer if circumstances justify it
- If a member does not reply within the specified time limit, you may pay a refund of contributions but you should wait at least 1 month from the end of the reply period before doing so
- If the member was in contracted-out service in the scheme and there is a possibility of buying them back into the state scheme, the total time periods for all stages should not be longer than 6 months

### Transfer payments

- Members are entitled to request a transfer payment. This should reflect the cash value of their benefits within your scheme and is usually referred to as a “*cash equivalent transfer value*” (CETV)
- The manner in which the CETV is calculated must be decided by you:
  - although your responsibility, in reality you are likely to follow actuarial advice
  - you need to make decisions on how you are going to treat discretionary benefits and the extent to which you will assume that members exercise options at retirement (although taking options into account cannot reduce a CETV)
  - you should have regard to your investment strategy and likely investment returns when choosing appropriate assumptions
  - you may reduce CETVs where the scheme is underfunded but it will not normally be appropriate to do so if the employer covenant is strong and the deficit is likely to be made up
  - you should review the basis of calculation from time to time (the Regulator suggests at the same time as the triennial actuarial valuation or sooner if there is a reason why the existing basis is no longer appropriate)
  - the same basis should normally be used for all transfer payments (whether the member has 2 years service or not)

- if the scheme is in wind-up or a PPF assessment period, additional issues need to be considered.

## For more information...

- Regulator’s Code of Practice No.4: Early Leavers
- Regulator’s Guidance on Transfer Values

# Amending the scheme

## Overview

To protect the interests of scheme members, there are restrictions on the ways in which schemes can be amended. There are also requirements to tell members about certain proposed changes and allow them to comment on them. Some of these statutory requirements are the responsibility of the trustees.

## Key points

- ✔ trustee consent to amendments is nearly always required
- ✔ amendments are legally complex and you should seek advice before making any
- ✔ you must ensure that you have complied with the requirements of the trust deed (some contain important restrictions on amendments)
- ✔ if an amendment might affect rights already built up in the scheme, you must explain to members the likely impact of the change
- ✔ if an amendment might affect rights already built up in the scheme, you can amend (subject to any trust deed restrictions) if the total overall value of the member's earned rights will not be reduced (ie if the change is "actuarially equivalent") or if the member consents

### **If going down the actuarial equivalence route you should:**

- explain to members how the actuarial value of their overall benefits is still the same
- give members at least 4 weeks to make representations to you about the proposed change
- consider giving members a specific person to contact with queries
- allow time to consider any representations from members
- obtain an actuarial statement within 1 month after the change confirming actuarial equivalence

- ✔ once an amendment decision has been made, tell members within 1 month (and before it takes effect)
- ✔ if members consented to the amendment, implement it within 7 months of consent
- ✔ if the amendment affects benefits to be earned in the future, the employer may well need to comply with statutory consultation requirements and you should ask them if they have done so. The Regulator may waive such requirements eg if there is an immediate threat to the scheme or jobs
- ✔ if an amendment is not properly made it can be treated as never having had any effect

## For more information...

- ✔ Regulator Code of Practice No 10. - Modification of Subsisting Rights. This contains useful flow charts for the consent route and the actuarial equivalence route
- ✔ Regulator Statement on employer duty to consult

# Funding (only relevant to defined benefit scheme trustees)

## Overview

The Pensions Act 2004 introduced the “scheme specific funding” regime for defined benefit schemes. It is the trustees’ responsibility to implement these requirements, although for many aspects employer consent may be required.

## Key points

- ✔ work out if employer consent is required to the various elements of the funding process. This depends on the scheme rules. Where employer consent is not required, they must still be consulted and given time to consider documents and take advice
- ✔ if the scheme actuary has contribution setting powers in the rules he may be required to certify whether he agrees with any funding decisions
- ✔ where trustees and employers need to agree on relevant funding matters, failure to do so must be reported to the Regulator within 10 working days of when agreement should have been reached
- ✔ actuarial assumptions should be prudent with regard to the nature of the scheme’s liabilities
- ✔ the aim is always to ensure that there are sufficient assets in the scheme to meet its liabilities. However, the legislation does not require you to value scheme liabilities based on their full “buy-out” cost
- ✔ a schedule of contributions will be prepared and you should have procedures in place to monitor payment in accordance with the schedule and investigate non-payment
- ✔ the Regulator has acknowledged that in the current economic crisis, trustees may need to review the length of existing deficit recovery plans, although they should remain as short as reasonably possible

## Required funding documents

Document name	Content	Timings
<b>Actuarial valuation</b>	Values the scheme’s assets and liabilities on the basis of assumptions chosen by trustees (with employer agreement or consultation) and actuarial advice.	Every 3 years or sooner if circumstances suggest one is needed. Must be completed within 15 months of ‘as at’ date.
<b>Statement of funding principles</b>	Records all of the assumptions used and decisions about the manner and period within which to eliminate any deficit.	Produce within 15 months after the effective date of the valuation and at any other time if necessary.
<b>Schedule of contributions</b>	Sets out the rates of the contributions payable and their due dates. It must be certified by the scheme actuary.	Lasts 5 years from the date of certification (or the length of recovery period if longer).
<b>Recovery plan</b>	Sets out how any shortfall will be made up and over what period. Prepared by the trustees (with employer agreement or consultation).	Typically lasts for several years but should be as short as reasonably possible.
<b>Actuarial interim report</b>	An update of the funding position from the date of the last valuation.	Where no valuation is obtained, produce within 12 months of the last valuation or interim report.
<b>Summary funding statement</b>	Issued to all scheme beneficiaries summarising the funding position of the scheme and an explanation of any changes in the funding position. It should be in member friendly language.	Sent out within 3 months of the date each actuarial valuation or report should have been obtained by.

## For more information...

- ✔ Regulator’s Code of Practice No. 3 – Funding Defined Benefits
- ✔ Regulator’s sample funding documents and Guidance and Statements on trends in recovery plans and funding

# Corporate activity (moral hazard powers and clearance)

## Overview

The Regulator has powers to ensure that employers with occupational pension schemes do not attempt to avoid their funding obligations, for example by manipulating group structures. The Regulator has power in certain circumstances to look around a corporate group, including companies which have no direct responsibility for funding the pension scheme, and require them to fund a scheme deficit or provide another form of financial support to the scheme. Corporate groups concerned that a transaction may trigger the use of these powers can seek “clearance” from the Regulator.

## Key points

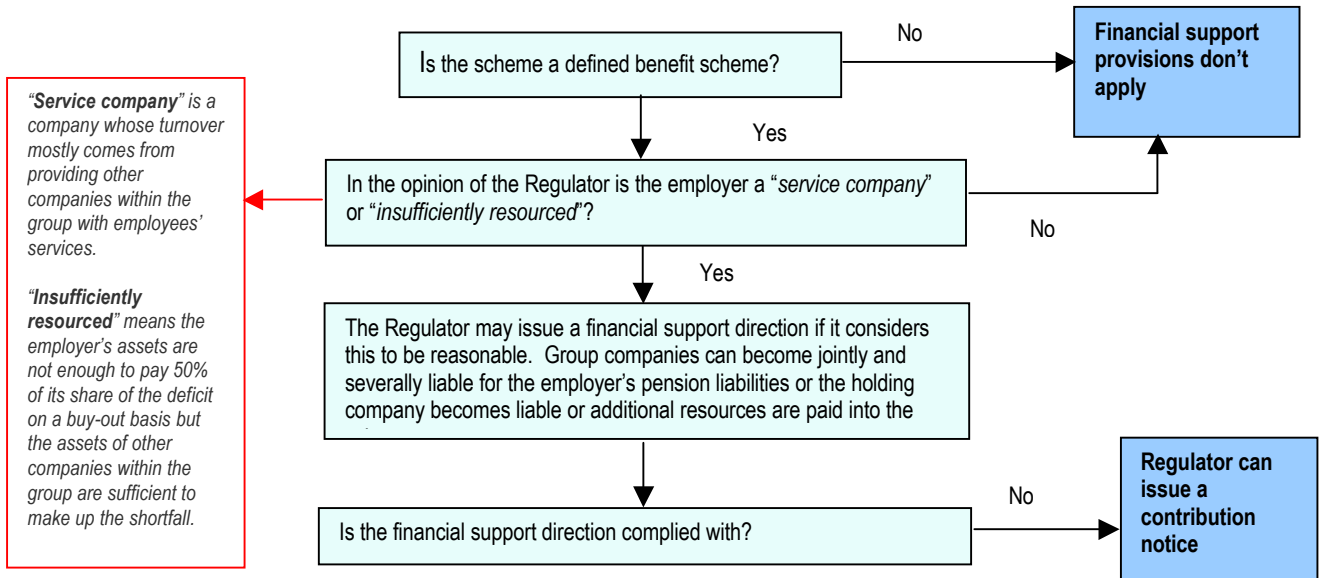
- the Regulator’s “moral hazard” powers enable it to issue financial support directions (requiring financial backing for the employers’ obligations to fund the scheme) and contribution notices (requiring third parties to contribute to the funding of the scheme). When it can do so is set out on the next page
- because a wide range of normal corporate activities could potentially trigger the exercise of the Regulator’s moral hazard powers, the Regulator has a process which enables parties to seek confirmation that a particular transaction will not trigger the use of its powers. This is referred to as clearance
- clearance is always voluntary, although the Regulator’s guidance sets out when it expects clearance to be requested
- applications for clearance are generally made by employers, but trustees should normally be involved in the process. The Regulator will usually ask for your views concerning the application
- the Regulator expects applications for clearance to be considered where an event will result in a significant weakening of the employer covenant or make the recovery of any scheme deficit less likely
- the need for clearance of employer events typically depends on the strength of the employer covenant before and after event and whether the scheme is in deficit. The clearance guidance has an appendix setting out the kind of things you should take into account when assessing the strength of the employer covenant
- if an event may require clearance, employers and trustees should consider how the event’s impact on the scheme can be mitigated. Mitigation could be the payment of additional cash into the scheme or providing additional security
- you should be prepared to negotiate with employers to protect the interests of scheme members
- the Regulator has so far only exercised its moral hazard powers on one occasion although the threat of such powers has often influenced behaviour towards schemes in a positive way

## For more information...

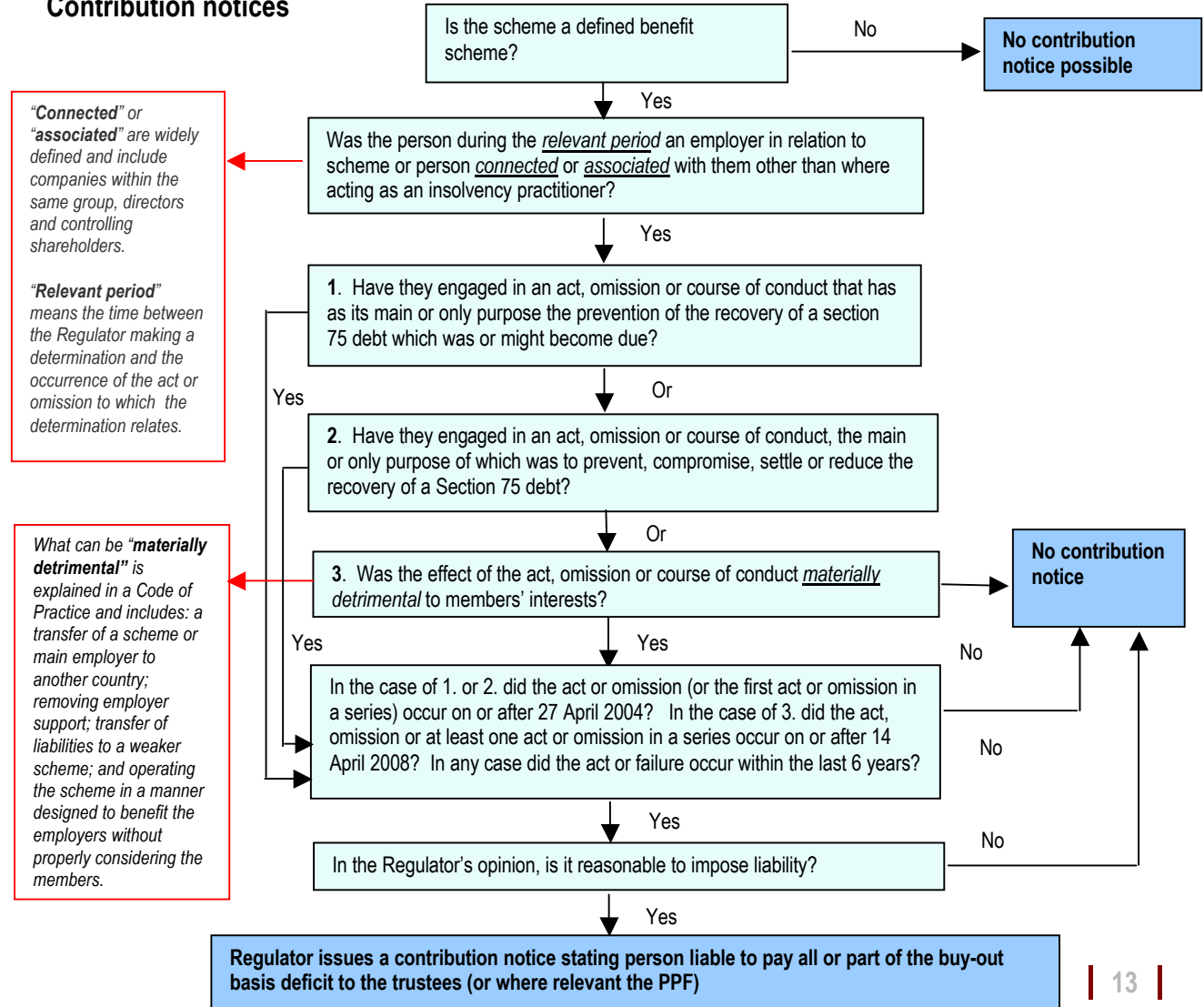
- Regulator’s Code of Practice No 12: Circumstances in relation to the material detriment test
- Regulator’s Clearance Guidance – June 2009

## How the Regulator's moral hazard powers work

### Financial support directions



### Contribution notices



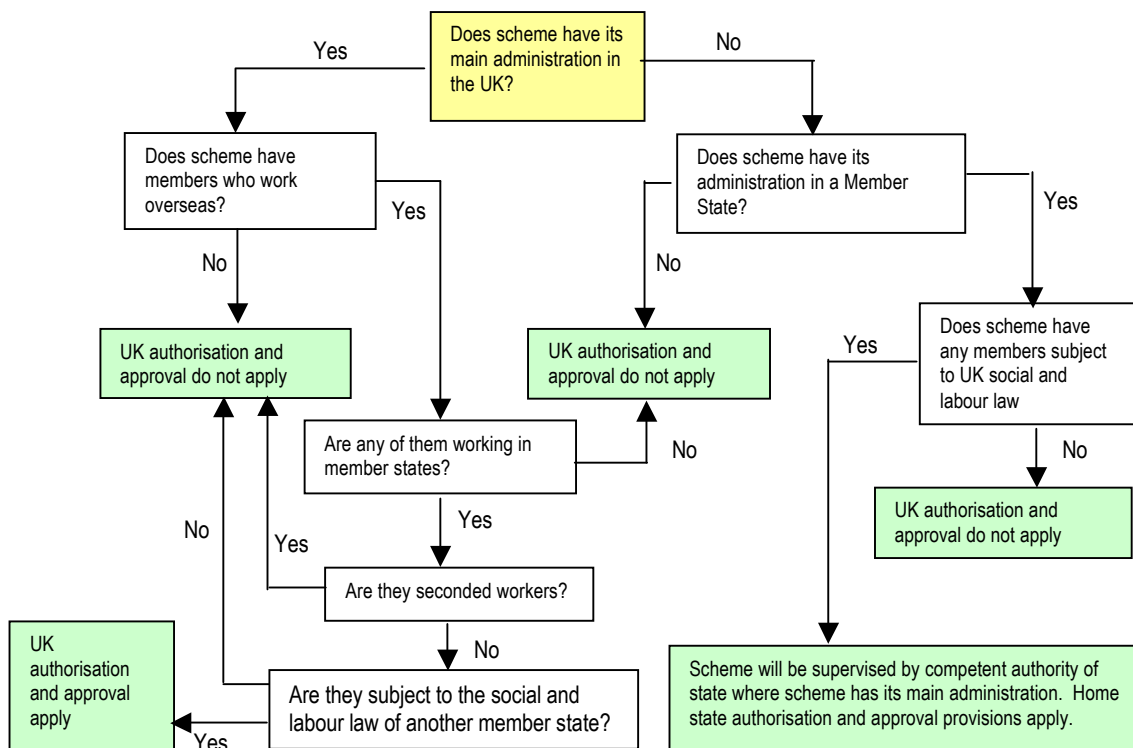
# Cross-border schemes

## Overview

From December 2005, pension schemes located in one state in the European Economic Area (EEA<sup>1</sup>) need to apply for authorisation and approval to accept contributions from employers employing members who are subject to the social and labour laws of another EEA state. There are also obligations for such schemes to be fully funded on their ongoing basis and to comply with the social and labour laws of the applicable EEA state(s). As these are onerous consequences, it is important to avoid unintentionally falling within the cross-border regime.

## Key points

- This diagram is based on one prepared by the Regulator to help trustees understand how the cross-border regime works.



- if employees are seconded to another EEA state, they may be able to remain an active member of the scheme without triggering the cross-border requirements. The employer should check the terms of any secondment to ensure it meets all the requirements for this to happen.
- if an active member is working outside of EEA, the cross-border regime does not apply
- if in any doubt about the applicability of the cross-border requirements to your scheme, seek legal advice
- where UK authorisation and approval is required, forms and guidance on the process are available on the Regulator's website

## For more information...

- Regulator's Guidance on EU Cross-border Schemes
- Regulator's summary and overview of pensions and employment law relevant to pensions in the UK.

# Scheme abandonment

## Overview

Most defined benefit schemes rely on the continued financial support of an employer to be able to pay member benefits in full. Trustees should consider any potential “abandonment” of their scheme by a sponsoring employer with great care.

## Key points

- any arrangement that will result in breaking the link between the scheme (or a significant proportion of members) and the current employer or the employer’s business must be considered carefully by the trustees as it may not be in the members’ best interests
- you must consider transactions or restructurings which would result in scheme liabilities being transferred from one employer to another or the covenant of a major participating employer becoming much weaker, to determine whether it could amount to “abandonment”
- where an event might be “abandonment” you should try to ensure that the full amount necessary to insure members’ benefits with a regulated insurer is paid or the scheme remains supported by an employer of substance and is suitably compensated for any change in the employer’s covenant
- where the scheme rules give trustees power in relation to such transactions (eg agreeing to participation by a new employer), the trustees should seek professional advice and this should usually be paid for by the employers
- you should seek “mitigation” (compensation for the scheme) to make up for any loss in strength of employer covenant
- you should consider whether you have any duties to report the proposed arrangements to the Regulator under either the whistleblowing or the notifiable events regimes (see relevant sections of this Guide)

## Issues for trustees to consider

### Some issues to consider when there is a potential abandonment:

- Will a section 75 debt be triggered? If so, the trustees’ scope for claiming payments to scheme or securing other protections may be strengthened.
- If trustees are asked to agree to the apportionment of a debt between employers, you should consider why and what the impact is. If there is a compromise of any section 75 debt, what effect will this have on potential entry into the PPF?
- Consider the scheme rules to determine what powers the trustees have in relation to the proposed transaction.
- What is the strength of the employers’ covenant to the scheme before the transaction takes place?
- What is the nature and strength of the employers’ group; is there any additional security which could be obtained?
- What is the strength of the covenant of any proposed replacement employer? What is its legal structure, where is it based and who are the ultimate owners?
- Is there a potential advantage to the proposed transaction?
- Will the transaction have an impact on the scheme’s investment strategy (if there is no longer anyone underwriting risk)?
- Are there any alternatives such as restricting future benefits in the scheme?

## For more information...

- Regulator’s Guidance on Abandonment

# Late payment of contributions in defined contribution schemes

## Overview

Trustees of defined contribution schemes (i.e. which have no defined benefit element) are only required to report to the Regulator the late payment of contributions where it is likely to be of material significance to the Regulator, whose Code of Practice provides examples of when this will be the case.

## Key points

- you should have procedures in place to identify late or incorrect payment of contributions
- where you identify a late payment, you should take action to obtain any contributions that are still outstanding and consider whether to make a report to the Regulator
- you should normally make a report to the Regulator within 10 working days of becoming aware that one is needed
- if you make a report to the Regulator, you must also notify members and you must generally do this within 30 days of when the need to make a report to the Regulator arose

### Trustees should report late payments to the Regulator where:

- contributions have been outstanding for more than 90 days (unless it was as a result of an error which was discovered outside the 90 days and has been rectified)
- the late payment involves fraud or dishonesty
- the failure carries a criminal sanction because the employers have been “knowingly concerned in the fraudulent evasion of the obligation to pay member contributions”
- where the trustees are aware that the employer does not have adequate procedures in place to ensure contributions are paid on time
- where there is no prospect of the employer paying overdue contributions

- even if no obligation arises to report to the Regulator, any late payment of contributions can lead to member complaints and possible member loss and so efficient receipt and investment of contributions is very important

## For more information...

- Regulator's Code of Practice No.5: Reporting late payment of contributions to occupational defined contribution schemes

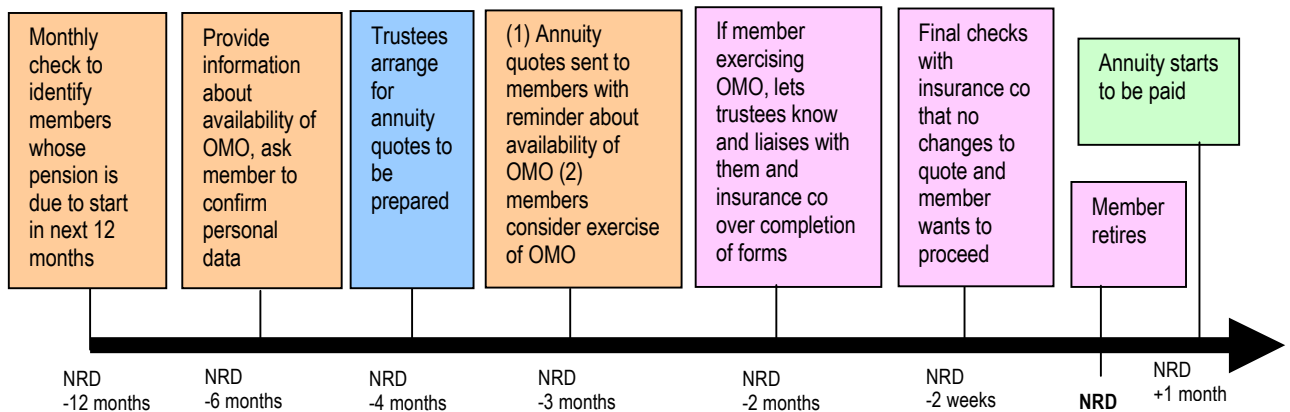
# Communications with members of defined contribution schemes

## Overview

The Regulator believes that the greatest risks for defined contribution scheme members arise from lack of member understanding; poor administrative and investment practices; unduly high charges; and poor decisions on retirement choice. It is therefore particularly concerned with ensuring good standards of communications in such schemes.

## Key points

- members approaching retirement must be aware of all of their options so they can make the right decisions. In particular, they must be aware of the “open market option”, i.e. where they can choose their own annuity provider.
- when drafting member communications, you should:
  - identify objectives, and have a clear communications plan
  - identify the best ways to communicate and what form communications should take
  - tailor communications to the audience and remember the needs of all groups, not just active members
  - be open and honest
  - avoid jargon
  - choose a good time and try to get members to engage
- the Regulator has drafted several booklets which are aimed at members and which trustees could consider giving to members. One explains different types of investments to members to assist them with investment options and another explains different types of annuities and other alternatives which might be available on retirement.
- when members come up to retirement, it is important to have an effective process to convert their defined contribution accounts into retirement income. Trustees need to consider how benefits are to be secured and what choices members have. This diagram is based on one prepared by the Regulator and illustrates what the Regulator considers might be an effective process:



## For more information...

- Regulator’s Guidance: Our approach to DC regulation.
- Regulator’s Guidance: Effective member communication
- Regulator’s Guidance: Member retirement options
- Engaged employers and informed retirement choices – key to good outcomes for members of DC pensions
- Making your retirement choices and making pension fund choices – think before you choose (for members)

**OMO** – “open market option”  
**NRD** – “normal retirement date”

## Want more information?

The Pensions Regulator has published many hundreds of pages of information and this Guide seeks to draw out the key points. Because there is a lot more to be said on each topic we will be putting more detailed guidance on each area on our website at: <http://www.cms-cmck.com/Employment-Pensions/Pensions>

In addition:

- If you would like more general guidance as to what the Regulator thinks a trustee's role is, it has published a basic guide which can be found at: <http://www.pensionsregulator.gov.uk/trustees/guidance/index.aspx>
- On each page we have highlighted the Regulator's publications which contain more information about that particular subject. In addition to the subjects dealt with in this Guide, the Regulator has also published guidance on multi-employer schemes and withdrawal arrangements; winding-up; offering inducements to members; and life cover only arrangements. All of the Regulator's publications are available at: <http://www.pensionsregulator.gov.uk/>
- The Regulator also has an on-line trustee training course, the "trustee toolkit" which can be completed over any length of time and which contains a lot of information dealing with what the Regulator expects from trustees and examples of practical situations. The Regulator has said that this is required study for new trustees unless they can find an alternative learning programme which covers all the items they are required to know as part of their knowledge and understanding duties. The trustee toolkit is at: <http://www.trusteetoolkit.com/arena/index.cfm>
- In places we have referred to the Pension Protection Fund because part of the Regulator's remit is to reduce potential claims on the PPF. If you would like to understand more about the PPF, it has a guidance page for scheme trustees at: <http://www.pensionprotectionfund.org.uk/Pages/SchemeTrustee.aspx>
- If you have specific concerns, your professional advisers are there to help you with these. The Regulator has also published a guide on getting the best from your professional advisers which is available at: <http://www.pensionsregulator.gov.uk/trustees/relationsWithAdvisers/index.aspx>

### Need legal advice?

The pensions team at CMS Cameron McKenna is available to advise on all aspects of pensions law, including the responsibilities of trustees. If you are not already a client and are interested to know more about our services, please contact **Mark Grant** (partner) – **E:** [mark.grant@cms-cmck.com](mailto:mark.grant@cms-cmck.com) **T:** +44 (0)20 7367 2325.

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