EXPLANATORY MEMORANDUM TO

THE OCCUPATIONAL PENSION SCHEMES (PRESERVATION OF BENEFIT AND CHARGES AND GOVERNANCE) (AMENDMENT) REGULATIONS (NORTHERN IRELAND) 2018

S.R. 2018 No. 54

1. Introduction

1.1 This Explanatory Memorandum has been prepared by the Department for Communities to accompany the Statutory Rule (details above) which is laid before the Northern Ireland Assembly.

1.2 The Statutory Rule is made under sections 69(2)(b) and (4)(b) and 177(2) to (4) of the Pension Schemes (Northern Ireland) Act 1993 and sections 42 and 51(6) of, and paragraphs 1(1)(a) and 7 of Schedule 18 to, the Pensions Act (Northern Ireland) 2015 and is subject to the negative resolution procedure.

2. Purpose

2.1 These Regulations make technical amendments to existing Regulations to simplify the conditions which must be satisfied for trustees or managers of pension schemes, or other parties who hold the right, to transfer groups of certain pension scheme members from one scheme to another without having to seek the explicit permission of individual members in advance. They also maintain the protection offered by the cap on member-borne charges in pension schemes used for automatic enrolment into workplace pensions, when members are moved between or within schemes without their active consent.

3. Background

3.1 Section 69 (form of short service benefit and its alternatives) of the Pension Schemes (Northern Ireland) Act 1993 permits alternatives to short service benefit (pension benefit that must be provided for a member who leaves the scheme before retirement and does not receive a pension immediately), including transfers without consent as prescribed in regulations.

3.2 It is accepted that small pension schemes can represent poorer value for money for their members, for example, with the absence of economies of scale, smaller schemes can pay significantly more in charges, be less able to negotiate effectively with service providers to deliver good member outcomes and be less able to invest in asset classes.

3.3 The current process for scheme consolidation is very burdensome. Schemes can seek consent to consolidate from every individual member – but this is time consuming and difficult, with low response rates even after concerted efforts. A ‘without consent’ approach is available but is difficult to apply or serves no useful purpose when used for many defined contribution schemes having originally been designed for defined benefit schemes.

3.4 Regulation 12 of the Occupational Pension Schemes (Preservation of Benefit) Regulations (Northern Ireland) 1991 sets out the current conditions under which a member's accrued rights (pension pot) may be transferred from one occupational scheme to another. This requires a relationship between the ceding and receiving schemes (regulation 12(2)) and certification by an actuary (regulation 12(3)).

3.5 These Regulations provide for an alternative process for the bulk transfer of pension scheme members' money purchase benefits where they do not have any underlying guarantees. In broad terms, a money purchase benefit is a 'cash pot' which is attributable to the member. Typical guarantees include those about the rate of growth of the pot or the rate at which the final pot can be converted into a retirement income. Non-money purchase benefits and money purchase benefits with guarantees will continue to be subject to the two current requirements for bulk transfers without member consent – an actuarial certificate and meeting the 'scheme relationship condition'.

3.6 Trustees of all pension schemes have a fiduciary duty of undivided loyalty to act in the best interests of their beneficiaries, usually known as members, and this fiduciary duty will continue to be the underpinning principle when considering a transfer of members without their consent.

3.7 These Regulations impose a new procedure for the transfer of money purchase benefits without any guarantee or promise. It removes the requirement for an actuarial certificate and the scheme relationship condition, and instead requires the ceding scheme (or employer where they make the decision) to seek advice from an independent adviser prior to the transfer. This requirement applies to all money purchase benefits without a guarantee unless the transfer is to a connected scheme (where the sponsoring employers are connected through a common ownership structure and have a controlling position in their respective schemes) or a master trust (a multi-employer scheme) authorised under the Pension Schemes Act 2017 or any corresponding Northern Ireland legislation.

3.8 These Regulations also change the cap on pension scheme charges introduced by the Occupational Pension Schemes (Charges and Governance) Regulations (Northern Ireland) 2015. The charge cap is applicable to any member invested in the default investment option or 'arrangement' of a scheme used for automatic enrolment – so that, broadly, members who did not choose their arrangement should be protected by the cap.

3.9 These Regulations provide that the cap will continue to apply when members are moved without consent to a different scheme not used for automatic enrolment. In addition, they modify the application of existing regulations so that members who originally did make an investment choice and are moved without consent will not be placed into a default arrangement, if that original choice was made in the previous 5 years.

4. Consultation

4.1 There is no requirement to consult on these Regulations. They make in relation to Northern Ireland only provision corresponding to provision contained in regulations made by the Secretary of State for Work and Pensions in relation to Great Britain.

5. Equality Impact

5.1 Proposals for the Pensions Act (Northern Ireland) 2015 were subject to a full Equality Impact Assessment. In accordance with its duty under section 75 of the Northern Ireland Act 1998, the Department has conducted a screening exercise on the legislative proposals for these Regulations and, as they make mainly technical amendments, the Department has concluded that they would not have significant implications for equality of opportunity and considers that an Equality Impact Assessment is not necessary.

6. Regulatory Impact

6.1 A Regulatory Impact Assessment is attached as an Annex to this Explanatory Memorandum.

7. Financial Implications

7.1 None for the Department.

8. Section 24 of the Northern Ireland Act 1998

8.1 The Department has considered section 24 of the Northern Ireland Act 1998 and is satisfied that these Regulations –

(a) are not incompatible with any of the Convention rights,

(b) are not incompatible with Community law,

(c) do not discriminate against a person or class of person on the ground of religious belief or political opinion, and

(d) do not modify an enactment in breach of section 7 of the Northern Ireland Act 1998.

9. EU Implications

9.1 Not applicable.

10. Parity or Replicatory Measure

10.1 The corresponding Great Britain Regulations are the Occupational Pension Schemes (Preservation of Benefit and Charges and Governance) (Amendment) Regulations 2018 (S.I. 2018/240) which come into force on 6th April 2018 and 1st October 2019. Parity of timing and substance is an integral part of the maintenance of single systems of social security, child support and pensions in line with section 87 of the Northern Ireland Act 1998. The Regulations are necessary to safeguard members' interests, and to ensure pension schemes can continue to function on a UK-wide basis. It was, therefore necessary to make the Regulations during the period of interregnum.

ANNEX

REGULATORY IMPACT ASSESSMENT

THE OCCUPATIONAL PENSION SCHEMES (PRESERVATION OF BENEFIT AND CHARGES AND GOVERNANCE) (AMENDMENT) REGULATIONS (NORTHERN IRELAND) 2018

The costs and savings outlined in this Regulatory Impact Assessment are calculated on a United Kingdom-wide basis.

Rationale for intervention and intended effects

1. Automatic Enrolment is reshaping the Defined Contribution (DC) pensions market. The market has been changing from one where members' assets are overseen by trustees of many small schemes, towards one with fewer larger schemes, including Master Trusts. As shown by the Charges Survey[1], studies carried out by The Pensions Regulator on scheme governance[2], common and conditional data[3] and transfer times[4], and The Regulator's 21st Century Trustee strand[5], larger schemes tend to deliver better administration and better value for members. Nevertheless some 1,750 schemes[6] with between 12 and 1,000 members[7] remain. To allow the shift towards better member outcomes to continue, removal of barriers to consolidation of these smaller schemes is desirable. Recent reports by the Financial Conduct Authority[8] and the Law Commission[9] have pressed for an easement of the process for moving groups of members into schemes they consider to be better value.

2. It is believed that bulk transfers of pension scheme members have become more common, particularly since the advent of Master Trusts, and can take place as a result of mergers and acquisitions activity, or scheme trustees wishing to move members to access better value for money, or improved member benefits. Rather than schemes having to contact each individual member for consent, which can be time-consuming and sometimes impractical – for example, when members cannot be traced - regulations[10] exist which allow schemes to bulk transfer members without their consent, under certain conditions outlined below.

3. Currently, legislation requires the following conditions to be met in order for a bulk transfer without member consent to take place:

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1 https://www.gov.uk/government/publications/pension-charges-survey-2015-charges-in-defined-contribution-pension-schemes
2 DC trust-based pension schemes research, http://www.thepensionsregulator.gov.uk/docs/dc-research-technical-report-2016.pdf
3 Researching record-keeping and administration in trust-based pension schemes: Findings from The Pensions Regulator's 2016 quantitative survey (http://www.thepensionsregulator.gov.uk/docs/record-keeping-survey-2016.pdf) and 2015 qualitative research (http://www.thepensionsregulator.gov.uk/docs/trustee-landscape-quantitative-research-2015.pdf)
4 Survey on flexible pension access: report of findings on the 2015 research survey
5 21st century trusteeship and governance: response to discussion paper, 2016, http://www.thepensionsregulator.gov.uk/docs/21st-century-trusteeship-governance-discussion-response-2016.pdf
6 http://www.thepensionsregulator.gov.uk/doc-library/dc-trust-presentation-of-scheme-return-data-2018.aspx
7 There are an additional 32,000 schemes with 11 or fewer members. The vast majority of these are schemes where the members are also the trustees, or are current or former directors of the sponsoring employer, who acts as trustee. These schemes are discounted from all the other figures in this note
8 Asset management market study: final report, June 2017, https://www.fca.org.uk/publication/market-studies/ms15-2-3.pdf
9 Pension Funds and Social Investment, June 2017, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/625846/6.3496_LC_DRAFT_190617_TT_20_06_17__PRINT_-_final_.pdf
10 http://www.legislation.gov.uk/nisr/1991/37/contents/made

- the transfer must be made to another occupational pension scheme;
- the trustees must obtain a certificate signed by an actuary, stating that the benefits offered by the receiving scheme are ‘broadly no less favourable’ for members than the current scheme;
- the transferring scheme and the receiving scheme must be connected to each other in a way specified in regulations (the scheme relationship condition); and
- the members must be given information about the proposed transfer and the value of the rights to be transferred at least one month before the transfer.

4. Some of the above conditions, while still relevant in cases of transfers of Defined Benefit (DB) schemes are harder to apply to transfers of DC to DC schemes. In many cases, schemes will have to specially appoint an actuary to produce the certificate, adding to the costs and time taken for the transfer.

5. Whilst actuaries are able to make a considered judgement of outputs in DB transfer cases, DC schemes can be more difficult to compare as they are based on investment strategies, and other elements of the DC packages will be harder to quantify on a strictly financial basis. This has led to a variation in interpretation, with actuaries taking different risk approaches and sometimes being unwilling to provide certificates. This results in a non-standard approach which depends to a large extent on the factors taken into account by the actuary. Equally, the scheme relationship condition can be difficult to meet in some DC cases, leading to some technical workarounds being created, which can add administrative time to the process, with no member benefit.

6. There is some evidence that transfers which could be in the best interest of members are not happening as a result of the costs and complexities involved in satisfying the current conditions.

Viable policy options (including alternatives to regulation)

7. Option 1: Do nothing - a non-legislative measure would not be suitable due to increasing pressure to increase scheme consolidation and aid effective transfers. Without regulatory change, pension schemes will remain required to obtain the actuarial certificate and meet the scheme relationship condition to carry out the transfer.

8. Option 2: This is the preferred option. In respect of money purchase benefits without guarantees:
    - Measure 1- Remove the requirement for an actuarial certificate in cases of transfers to authorised Master Trusts, other schemes authorised under the Pension Schemes Act 2017 or any corresponding Northern Ireland legislation and transfers to ‘connected’ schemes, and in the case of transfers to schemes not authorised under that legislation or to unconnected schemes require trustees to seek advice from an independent appropriate adviser.
    - Measure 2 - Remove the scheme relationship condition from the process.

- Measure 3 – (1) Ensuring capped deferred members, moved without consent to a scheme not being used for AE, continue to benefit from the cap in the new scheme. (2) Ensuring members who recently chose non-default arrangements are not forced into capped arrangements on transfer.

Supporting evidence

9. The current legislation covering bulk transfers without member consent requires that for these types of transfers to be carried out, trustees must meet certain conditions. These include:
    - Obtaining a certificate from an actuary, stating that they have reviewed the receiving scheme, and consider the proposed benefits in the receiving scheme to be 'broadly no less favourable' for members than the ceding scheme
    - The need for an existing link between the two schemes (also known as the 'scheme relationship condition').

10. These requirements were drafted in a climate of mainly Defined Benefit (DB) pension schemes, and reflected conditions at the time. The actuarial certificate requirement works well in DB schemes, where there is a guaranteed member outcome that actuaries can compare. This doesn't exist in Defined Contribution (DC) schemes, where outputs are dependent on investment strategies, which actuaries find difficult to assess. The scheme relationship is also less meaningful for DC schemes, as there is no covenant between employer and trustee, and has led to workarounds being introduced as a technicality to satisfy this condition.

11. In December 2016, a Call for Evidence sought industry views on the current legislation, and how well it was working for DC to DC bulk transfers without consent[11]. 45 responses were received from a range of firms and individuals and found overwhelming support for a change in legislation to facilitate transfers, with broad support for removing the need for an actuarial certificate, and removal of the scheme relationship condition.

12. The measures for change are:
    - The removal of the requirement to obtain an actuarial certificate for certain DC-DC transfers (that is transfers where there are no potentially valuable guarantees or options to be assessed) and the requirement to seek advice from an independent adviser where the receiving scheme is not authorised under the Pension Schemes Act 2017 or any corresponding Northern Ireland legislation.
    - The removal of the scheme relationship condition for pure DC-DC transfers.
    - Maintaining, and amending the scope of, the protections provided by the charge cap.

13. These measures and their expected impacts are summarised below:

11 https://www.gov.uk/government/consultations/bulk-transfers-of-defined-contribution-pensions-without-member-consent

Measure 1: Removal of the Actuarial Certificate for DC-DC transfers.

14. Historically, the occupational pension DC scheme market has been dominated by a large number of small schemes, from 4,170 schemes with 12 to 999 members in 2009 to 1,750 schemes in 2017. This has had an impact on scheme governance, efficiency and regulatory oversight. The DC landscape has been changing since 2009 and the increasing popularity of Master Trusts in recent years will continue to affect the landscape. Typically schemes will transfer most or all members to another scheme before they begin the process of wind up and close their scheme down. This means members do not pay the cost of wind-up. Removing the barriers to consolidation for these smaller schemes is desirable, as it will allow trustees of schemes who are aware that they do not offer best value for members to transfer members more easily. This will allow continued improvement in governance standards and efficiency.

15. In addition to legislation, trustees of DC schemes are covered by the DC Code[12], produced by The Pensions Regulator, which sets out expectations on trustees, including their obligation to consider 'value for members' when running a pension scheme.

16. Currently, legislation requires trustees to obtain an actuarial certificate before performing a bulk transfer without member consent. In order to demonstrate that consideration has been given to the benefits offered by the receiving scheme, an actuary must certify the receiving scheme benefits are 'broadly no less favourable' than those in the ceding scheme. This condition works well for DB schemes, where there are tangible outputs which can be compared, but not so well for DC schemes, where outputs are dictated by investment strategies. In order to obtain an actuarial certificate, a scheme actuary often needs to be appointed.

17. However, this process adds considerably to the time taken to process transfers, and the costs of the transfer. Responses to the Call for Evidence showed that within the industry there was strong evidence that this condition is acting as a barrier to efficient transfers. Some responses indicated that they were not transferring members as the cost of carrying out the transfer was prohibitive. This means that the member is not gaining access to the best value pensions possible.

18. From one response to the call for evidence, a large administrator estimated that the actuarial certificate is currently a problem, by delaying or blocking, during roughly 20% of bulk transfers without member consent, and tended to discourage DC schemes from carrying out bulk transfers.

19. The intention is to amend this condition, as detailed below, in order to reduce the regulatory burden on the industry and to aid efficient bulk transfers and scheme consolidation.

12 http://www.thepensionsregulator.gov.uk/codes/code-governance-administration-occupational-dc-trust-based-schemes.aspx#s22009

20. The proposals are:
   - The need to obtain a certificate should be removed for 'pure' DC-DC transfers where there are no potentially valuable guarantees[13] or options to be assessed.
   - Where the transfer is to a Master Trust or other scheme which has been authorised to operate by The Pensions Regulator, or to a 'connected scheme', no further scheme quality test will need to take place. Trustees will still have a fiduciary duty of undivided loyalty to the best interests of members. Further guidance will be developed in order to assist trustees in this.
   - Where the transfer is **not** into an authorised or connected scheme, the trustees of the ceding scheme will be required to carry out a full review of the receiving scheme, again under their responsibilities in trust law, with appropriate guidance, for example, from the Regulator. Additionally, trustees should take steps to consult with an appropriate advisor who they have verified to be independent from the scheme under consideration.

21. The removal of the independent advice requirement for connected schemes stems from the conclusion that where schemes are 'connected' – that if the sponsoring employers of the connected and ceding schemes are connected firms and they have a controlling position in the two schemes – the risk of an adviser to the scheme holding significant conflicts of interest is much more limited, and therefore the independence test for advice to the trustees is unnecessary.

<u>Measure 2: Removal of the Scheme Relationship condition</u>

22. Currently, legislation requires the ceding scheme and the receiving schemes to be connected to each other in a way specified in regulations[14] (the scheme relationship condition). Where this condition is not met, it typically requires the ceding scheme to set up a transfer of one member to create a 'relationship' with the receiving scheme before being able to process a bulk transfer. This adds additional cost and time to the process.

23. In relation to DB to DB scheme transfers, the scheme relationship condition serves a useful purpose. It limits bulk transfers without member consent to scheme reconstructions within a corporate group, and to sale and purchase situations involving different corporate groups. However, the condition serves no useful purpose in the DC market and is hindering transfers from taking place.

24. Respondents to the Call for Evidence stated that having to meet this condition could be a barrier to transfers to outsourced schemes such as Master Trusts, which could be beneficial in reducing the ongoing costs to employers. The condition restricts the options available to the trustees or managers of the scheme considering a bulk transfer, by limiting the choice of available schemes to those with whom the employers have an existing relationship.

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13 Potentially valuable guarantees typically include Guarantees about the rate at which a pension pot might increase (Guaranteed Investment Returns), or a Guarantee about the rate at which the pension pot can be converted into income via an annuity (Guaranteed Annuity Rate). These might be money purchase or non-money purchase guarantees depending on whether the funding risk for the guarantee is borne by an insurer to the scheme, or the scheme itself

14 http://www.legislation.gov.uk/ nisr/1991/37/contents/made

25. Respondents also stated that they felt the condition seems to be at odds with the trustee obligation to seek better value if they believe that inferior value is provided through their own scheme. Respondents also stated that employers were circumventing this condition. Employers can potentially become participating employers in a master trust arrangement to meet the condition - but if there are no further contributions being paid by the employer this can often be seen as an unnecessary requirement. In practice this serves no useful purpose as the employer could withdraw from being a participating employer soon after the transfer takes place.

26. From one response to the call for evidence, a large administrator estimated that the scheme relationship condition is only currently a problem during roughly 3% of bulk transfers without member consent. However, schemes routinely need to carry out a small amount of additional work to meet the requirement (which does not add any member value). The responses from the call for evidence also suggested that this condition is not currently causing costs in transfers performed by smaller schemes, providers and administrators, as they may not perform transfers where this condition is currently a barrier. Due to the small amount of transfers per year this affects and due to the workaround, this is less of a barrier than the actuarial certificate.

27. This condition is being removed as it serves no useful purpose in transfers between DC schemes, and does not add value for members. The condition continues to serve a useful purpose in DB schemes, where the ongoing commitment of a sponsoring employer is needed to make up shortfalls in scheme funding.

28. To protect members, however, trustees should of course consider appropriate due diligence on the receiving scheme where they have no prior relationship with the transferring scheme, as set out in the DC code produced by The Pensions Regulator.

<u>Measure 3: Maintenance and extension of charge cap protection.</u>

29. Currently regulations 3 and 4 of the Occupational Pension Schemes (Charges and Governance) Regulations (Northern Ireland) 2015[15] require that a member is protected by the charge cap[16]:
    - When the scheme of which they are a member is or has been used for automatic enrolment by their current or former employer, and
    - They have not made an active choice about the investment option to which their contributions are allocated.

30. This left two issues in relation to transfers without member consent.

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15 http://www.legislation.gov.uk/nisr/2015/309/regulation/3/made and http://www.legislation.gov.uk/nisr/2015/309/regulation/4/made

16 With effect from April 2015, members of schemes used for AE by their current or former employers, and invested in the default arrangement of the scheme are protected by the charge cap, set at 0.75% per year of the funds in their default arrangement, or an equivalent combination charge. However, they are not protected if they are transferred without consent to another scheme which is not used for automatic enrolment by their employer.

31. The first relates to ensuring protection is maintained. Currently, where a capped member has accumulated pension savings in a scheme used for automatic enrolment by their employer, but is subsequently transferred without consent to a scheme which is *not* being used for automatic enrolment by their employer, the tests for charge cap protection are no longer met. This means that the member can then be charged in excess of 0.75%, despite having made no choice about where their contributions are invested.

32. The second relates to where the member originally made an active choice of investment option (and is therefore in an uncapped arrangement), but is subsequently moved without consent to another arrangement in the same scheme, or in a different scheme that is being used for automatic enrolment. Current regulations provide that the charge cap should then apply to this member.

33. It is considered that where the member has made an active investment choice in the past 5 years leading up to the transfer date, then they could be transferred without consent to an investment option which was not charge capped. Where choices were made more than 5 years ago, it is considered reasonable for trustees to be required to move the member to a default fund in the receiving scheme.

<u>Estimated impacts</u>

34. The measures are expected to be deregulatory and reduce cost to industry. The costs and benefits are set out below:

Volumes of bulk transfers carried out each year.

35. At present, there is no one central body that collects data for the volume of bulk transfers without member consent carried out each year. Using information provided by a large administrator in the call for evidence on the number of bulk transfers they administer each year, and multiplying this figure by their total market share (using data supplied by TPR[17]), it is estimated that around 63 bulk transfers without member consent take place each year.

36. This assumption is limited as it is based upon one administrator's evidence, and they may not be fully representative of the market. However, they represent a large proportion of the market, with transfers ranging in size, and transfers into both DC single employer schemes and Master Trusts. Therefore, there is confidence in using this data to inform the assumptions as they represent a wide range of transfers.

37. TPR provided further information from their yearly scheme return, that 35 occupational pension schemes reported performing a bulk transfer without member consent last year. However, it is not compulsory for schemes to provide this information, therefore not all transfers will have been recorded. Schemes

17 This information is not published due to commercial sensitivities.

may also have performed more than one transfer, as the numbers of bulk transfers is not asked in the scheme return.

38. Overall, the figures provided by TPR are likely to be an underestimate of the total number of bulk transfers that take place each year, however do not contradict the assumption that 63 transfers take place per year.

Measure 1: Removal of the Actuarial Certificate of DC-DC transfers

Savings to business

39. The weighted average cost of an actuarial certificate, based on the responses to the call for evidence, is £15,417. This is based on 7 responses, indicating the most common costs of £5,000 and £20,000 per transfer, and then weighting the costs by the frequency of which they occur. However, there is a large range around this estimate, with costs ranging from £1,500 to £150,000[18]. Responses to the call for evidence suggest that the cost is defined by the complexity of the transfer, not the size; therefore it is difficult to obtain a specific cost for the actuarial certificate.

40. With the removal of the actuarial certificate, the **saving to business would be £971,271 per year**[19].

41. Based on internal analysis performed by The Pensions Regulator, in 2016/17, 54% of all transfers into DC trust schemes went into Master Trusts. However, as this includes all transfers, including member initiated transfers and not just bulk transfers without member consent, it can only be used as a platform for making an assumption on bulk transfers. This is an increase from 35% in 2015/16.

42. The opinion of one large administrator within the industry is that around 64% of bulk transfers without member consent that they administer currently go into a Master Trust; however this is increasing year on year, and they expect this to continue in the future. This is in a similar ballpark to the figures for all transfers from TPR and the increase in the percentage to master trusts can also be seen in the TPR data.

43. Given that the number of transfers per year is increasing, and there are an increasing volume of people transferring into Master Trusts, the figure is expected to be higher after the regulation change. However, there is no top estimate for what this would be. Given the evidence available, the assumption is that 64% of bulk transfers without member consent go into Master Trusts in the cost impacts.

44. Where a transfer is into an authorised Master Trust, no additional steps are required. However, it is advised that a scheme trustee takes continued care when processing transfers to ensure the best outcome for members, especially with the

18 The £150,000 cost was the total cost of the transfer, not specifically the cost of the actuarial certificate. Therefore it has limited use in informing assumptions.
19 Calculated by the number of bulk transfer per year*cost of an actuarial certificate. (63*£15,417.)

removal of conditions that currently safeguard member benefits. As scheme trustees should already be doing this under their fiduciary duty, it is assumed there will be **no additional cost to the industry**.

45. An indirect cost is if a scheme trustee wanted to apply additional due diligence (above and beyond that which they are already required to perform as trustees). It is estimated that this would be a reasonably small amount of time and therefore cost. As an example, suppose they spent around 2 hours on additional due diligence. Using the wage estimate of £25.08 an hour (based on a professional's wage from ASHE 2016, Table 2.5[20], uplifted for overheads by 27%, in line with the Green Book guidance) multiplied by the expected number of bulk transfers per year, a yearly cost to the industry of £3,160 is estimated[21]. This is an indirect cost of the measure, as no additional due diligence is required as directly from the measure; it is at trustee's discretion whether they feel extra due diligence is needed.

46. Where transferring into a scheme which is not an authorised Master Trust or a connected scheme, trustees are required to obtain and consider the advice of a suitably competent professional who the trustees have verified to be independent from the receiving scheme. The average cost of using an independent professional is unknown. From consultation with stakeholders and responses to the online consultation, it is estimated that it is highly unlikely to cost more than an actuary and that if the process is to become less complicated this should reduce the cost. However, there is no evidence base to support the cost being lower, so the assumption is that there would be no difference in the cost of obtaining the advice from an independent professional than from an actuary; therefore assuming a cost of £15,417. Based on this assumption, the **cost to business** of transferring into a non-authorised Master Trust and gaining advice from an independent professional would be **£349,658**. (Calculated 63*36%*£15,417).

47. Schemes wanting to perform a bulk transfer without member consent would need to familiarise themselves with the new regulations. It is assumed that scheme trustees would only need to familiarise themselves with these regulations if they intend to perform a bulk transfer, and that they would only need to do so once (the first time). Only those who have already performed a bulk transfer under the current regulations would have to familiarise themselves with the new rules, since those who have not performed one would familiarise themselves with the new set of rules rather than the previous set of rules and therefore would be no cost over and above the baseline. Given the pent up demand within the industry to perform bulk transfers without member consent, it is assumed that all schemes expecting to perform a bulk transfer in the first year would need to familiarise themselves with the new regulations. It is not known how many schemes contribute to the 63 transfers per year, therefore it is assumed that each transfer is by a different scheme and therefore will affect 63 schemes.

20 https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/occupation2digitsocashetable2
21 Calculation based on number of transfers*2 hours*hourly wage of trustee. (63*2*25.08).

48. It is estimated it would take a scheme trustee around 47 minutes to read and understand the new regulations - approximately 17 minutes to read (based on an average reading time of 300 words per minute, 500 words per page and expected 10 sides to read), plus an additional 30 minutes to digest the information. This assumption is consistent with the Simplifying of advice requirements impact assessment[22].

49. Based on an estimated wage cost of £25.08 an hour- based on a professional's wage from ASHE 2016, Table 2.53 , uplifted for overheads by 27%, in line with the Green Book guidance, it would therefore cost a scheme trustee £19.65 to familiarise themselves with these rules. Therefore, multiplying this by the expected number of transfers per year, the estimate is a **one off cost to the industry of £1,238 in year one**.

50. There is a degree of uncertainty around the figures used, as there is limited evidence to inform assumptions.

51. The earliest date expected for the first Master Trusts to become authorised is April 2019. Therefore, between April 2018 and April 2019 when the first Master Trusts will become authorised, all bulk transfers without member consent will be transferred into non authorised Master Trusts (assuming 100% of transfers into non authorised Master Trusts instead of 46%). Therefore, based on the assumptions used above for transferring into non authorised Master Trusts, and assuming all 63 bulk transfers expected to be performed per year will be through this method, the cost of transferring into non authorised Master Trusts in the first year will be **£972,509**.

52. This is calculated from the cost of consulting an independent professional (£971,217=63*15,714), plus familiarisation costs (£1,238, as above.) The total cost in year 1 would therefore be £972,509 minus the saving of £971,271 for no longer requiring the actuarial certificate. Therefore it is estimated there will be a total cost to industry in year 1 of **£1,238**.

53. Based on the above assumptions, the expectation is a **total cost to business in year one of £1,238 and a total yearly saving to business of £621,613 in all subsequent years**.

54. This cost in year 1 is due to the percentage of transfers into authorised Master Trusts being zero (as there won't yet be any authorised Master Trusts). Once the first Master Trusts have been authorised (April 2019), the assumption is that 64% of transfers will be into authorised Master Trusts, and this assumption will be used in all subsequent years.

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22 https://www.communities-ni.gov.uk/publications/pension-schemes-act-2015-transitional-provisions-and-appropriate-independent-advice-amendment

Wider Considerations

55. There are wider considerations of the measure, which may occur as an indirect result and therefore are not included in the impact to business.

56. It is expected, as a result of the measure, that there will be an increase in the volume of bulk transfers that take place each year. This is due to the reduced financial burden of transferring into an authorised Master Trust, and the reduced complication of transferring into schemes which are not authorised Master Trusts. However, there is no estimate for how many this may be. These are not counted in the direct costs and benefits as the measure does not force an increase in bulk transfers, but by easing the process an increase is expected.

57. It is also expected that there will be an increased consolidation of schemes as a result, in particular with schemes transferring into an authorised Master Trusts. There may also be the development of industry-led aggregators for deferred members' pension pots. These are schemes which specialise in receiving deferred members' pension pots from multiple other schemes in such a way that whilst individually uneconomic for each of the ceding schemes they are collectively profitable for the receiving scheme. Such a development will reduce the costs to trustees associated with maintenance of multiple small pots.

58. There may be an indirect cost to the actuarial professional of new regulations. As providers will no longer require an actuarial certificate, it can be assumed that actuaries will lose this business. However, some providers may still choose to use an actuary when seeking advice from a financial professional. It can also be assumed, that this loss of business to actuaries will be directly transferred to financial professionals, often from the same firms.

59. There may be indirect benefits to employers. In single employer DC schemes, the sponsoring employer often takes responsibility for some costs, such as scheme governance and administration. Transferring some or all DC scheme members to more efficiently administered master trusts will tend to reduce employer burdens overall.

60. Under the new regulations, it is expected that the time taken for a bulk transfer without member consent will be reduced. This can be assumed for all transfers into an authorised Master Trust or to a 'connected scheme', as no additional process on top of trustees' due diligence is required. Where transferring into another scheme, it is estimated that it would not significantly increase the time of the transfer, if it increased at all, as the process is similar however advice is given by a more suitable professional.

Benefits to Members

61. Under the new regulations, members are expected to benefit. Given the additional diligence and professionalisation offered by dedicated trustees and more relevant advice from the financial professional whose skills and knowledge are more relevant for the comparison of DC pension schemes, it is assumed that

more members will be transferred into better governed schemes, offering better value for money than previously. Smaller schemes report much lower compliance with Key Governance Requirements[23] – The Pensions Regulator's most recent evidence shows that between 56-76% of small and medium pension schemes comply with none or only 1 of TPR's key governance requirements[24], compared to 11-28% of larger schemes and Master Trusts. This accounts for 308,000 pension scheme members in less well governed schemes, which has a negative impact on member outcomes. However, this is dependent on the quality of advice given.

62. With an expected decrease in the time taken for a bulk transfer to be processed, members should also be transferred into better schemes sooner than under previous regulations.

<u>Measure 2: Removal of the Scheme Relationship condition</u>

Impacts to business

63. The removal of the scheme relationship condition should not impose any direct monetised costs or benefits to business.

64. Although there is likely to be a small saving to business by removing the current costs associated with the scheme relationship condition, this currently only affects an estimated 3%[25] of transfers equating to roughly 2 transfers per year.

65. There is no estimate for what these costs might be, however through engagement with a stakeholder it is assumed it is simply the cost of transferring one member. As this affects such a small proportion of transfers and the cost is expected to be small, the benefit to industry would be proportionately small. It would therefore seem disproportionate to complete further analysis at this time.

66. Any additional cost of familiarisation of the new regulations is not anticipated. Trustees will typically be made aware of the regulation changes via the regular updates supplied by their scheme lawyers, therefore familiarisation would only apply to those wishing to perform a transfer before this pack was received. For those who have not previously processed a bulk transfer, there would be no need to read the regulation change, as they would have no prior knowledge of the scheme relationship condition. For those who have previously processed a bulk transfer it is estimated there will be no cost, as it would take a measurably too small amount of time to read the change in legislation.

67. Trustees will need to ensure continued care is taken when considering the receiving scheme. As this is assumed under their current fiduciary duty, it is not an additional cost for this measure.

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23 http://www.thepensionsregulator.gov.uk/docs/dc-research-summary-report-2017.PDF
24 Small pension schemes with 12-99 members. Medium pension schemes with 100-999 members.
25 From one response to the call for evidence, a large administrator estimated that the scheme relationship condition is currently a problem during roughly 3% of bulk transfers without member consent. The responses from the call for evidence also suggested that this condition is not currently causing costs in transfers performed by smaller schemes, providers and administrators, as they may not perform transfers where this condition is currently a barrier

Wider Considerations

68. It is anticipated that the removal of this condition would increase the number of bulk transfers processed each year as they would no longer need to go through the current additional burdens of the process. It is also anticipated that it will aid consolidation of smaller schemes as they will be able to transfer members to larger schemes with greater ease.

69. It is anticipated that there could be some wider indirect benefits from the removal of the scheme relationship condition. By removing this condition, it allows transfers to be processed with greater ease. This should also reduce the number of schemes where no sponsoring employer now exists, as trustees will be able to transfer members with ease, where the current regulations are preventing them.

Benefit to members

70. The removal of the scheme relationship condition should also benefit members, as the provider would now have a wider choice of schemes to transfer them into with ease. This should allow members to be transferred into better schemes. This is an indirect benefit as it depends upon the decision of the trustees.

Measure 3: Maintaining and extending the charge cap protection

Impacts to business

71. Measure 3(1) - This measure is not expected to limit the volume of bulk transfers without member consent, as in practice no evidence has been received that transfers of currently capped deferred members were taking place to schemes charging in excess of the cap under the current regime. It is anticipated that this measure will prevent the development of higher cost poor value schemes.

72. There would be no direct cost of retaining members' charge cap protection. Under current legislation, the Occupational Pension Schemes (Charges and Governance) Regulations (Northern Ireland) 2015[26], transfers without member consent must retain members' charge cap protection if the scheme is used for automatic enrolment. For schemes to which the current legislation does not apply, this would not be a direct cost.

73. Measure 3(2) - Regarding the 5 year trigger, schemes will need to keep records indicating when members made their previous investment decision. It is anticipated that most trustees will have access to this information when it is needed, or will have received a clear steer from relevant members on whether they wish to remain in an uncapped arrangement in the new scheme, through contact with members in the lead up to transfer.

26 https://www.legislation.gov.uk/nisr/2015/309/contents/made

74. Trustees will of course wish to consider, when switching members between investment options, or moving them to a different scheme, the level of charges in the receiving arrangement and whether such a move is in the members' best interests. This is within their current fiduciary duty and does not constitute an additional cost.

Benefit to members

75. The continuation of charge cap protection should benefit members by providing a 'backstop' maximum level of charges which can be levied on them, equal to the level of the charge cap.

76. Members will also benefit from the 5 year trigger on transfers between or within schemes without their consent. Where the member has recently made an active choice of investment option, trustees can choose to move them into a fund which resembles their original investment decision, if they feel that is in the members' best interests, rather than be forced to place them in a default arrangement.

Summary of costs

77. The estimated **cost to business in the first year is £1,238**, and the estimated **saving to business in all subsequent years is £0.62m per year**.

78. The estimated Equivalised Annual Net Direct Cost to Businesses (EANDCB) is **-£0.5m** per year.

79. There is some uncertainty around these figures as there is limited evidence to inform some of the assumptions. The assumptions that are likely to have the greatest impact on the cost/savings of the appraisal are the total number of bulk transfer per year and the costs of an actuarial certificate and of a financial professional.

80. However, the best evidence suggests that measures will be deregulatory with a small saving to industry each year.

<u>Small and Micro Business Assessment (Bulk transfers)</u>

81. It is not expected that these regulations will have a disproportionate impact on small and micro businesses. The legislation applies to activities that are undertaken by small businesses. It applies to all schemes wishing to perform a bulk transfer, and the impacts on all schemes is expected to be deregulatory.

82. Under current regulations the cost of obtaining an actuarial certificate is proportionally higher for smaller schemes. The new regulations will allow trustees and managers of smaller schemes to transfer members and consolidate, if they wish to, more easily and for a lower cost.

83. Familiarisation costs will be proportionally higher for smaller schemes. However, as they only apply to schemes which have previously performed a bulk transfer

without member consent this will only apply to a small number of schemes. This cost is relatively small and it is assumed small and micro pension schemes will be able to meet these requirements, and will also benefit from the regulations.

84. It should be noted that small and micro businesses are not the same as small and micro pension schemes. Many small and micro businesses use large pension schemes and there will be no disproportionate impact.

Other Impacts

<u>Equality</u>

85. Proposals for the Pensions Act (Northern Ireland) 2015 were subject to a full Equality Impact Assessment. In accordance with its duty under section 75 of the Northern Ireland Act 1998, the Department has conducted a screening exercise on these legislative proposals and, as they make mainly technical amendments, has concluded that they would not have significant implications for equality of opportunity and considers that an Equality Impact Assessment is not necessary.

<u>Environmental</u>

86. There are no implications.

<u>Rural proofing</u>

87. There are no implications.

<u>Health</u>

88. There are no implications.

<u>Human rights</u>

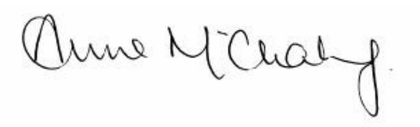
89. The Department considers that the regulations are compliant with the Human Rights Act 1998.

<u>Competition</u>

90. There are no implications.

I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.

Signed for the Department for Communities



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15 March 2018

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