SACKER & PARTNERS

CONSULTATION ON DRAFT REGULATIONS:
WORKPLACE PENSION REFORM - COMPLETING THE PICTURE
COMMENTS OF SACKER & PARTNERS LLP

Note: *Where required for information purposes, we have explained the relevant background of the Consultation Paper. These comments appear in italics and in square brackets. This text was not included in the response submitted to the DWP.*

A. Background

The purpose of this document is to set out our comments on the draft regulations contained in the Department for Work and Pensions' (DWP) consultation: "Workplace Pension Reform - Completing the Picture" which was published on 24 September 2009.

Sacker & Partners LLP (Sackers) is a firm of solicitors specialising in pensions law. With 50 pension lawyers, we act for in excess of 800 pension schemes, including household names and a number of FTSE-100 clients. The views expressed in Sackers' response to this consultation have been collated following discussions with a sub-group of the firm's solicitors.

We have limited our response to those questions which most naturally fall within our sphere of expertise and experience. We set out some general comments in section B, and responses to some of the specific consultation questions in section C.

B. General comments

1. To ensure that the automatic enrolment requirements are workable in practice, it is essential that the obligations on employers are realistic, easy to understand and easy to communicate (both by those responsible for implementation and by employers themselves). We therefore welcome the comments made in the DWP's response to its March 2009 consultation on the draft Pensions (Automatic Enrolment) Regulations that, following the responses received during the consultation, it intends "to simplify the processes and remove unnecessary prescription".

2. Phased introduction of the requirements is a sensible approach, given the numbers and diversity of employers who will be required to comply with the automatic

enrolment obligation. This should help to ensure that the bodies responsible for dealing with automatic enrolment (including the Pensions Regulator (TPR) and the Personal Accounts scheme administrators) will be able to process the information received from employers without a substantial backlog building up.

3. However, the number of stages proposed (25-30) is high, and risks causing confusion to employers who may be uncertain as to when the requirements apply to them until they are notified by TPR. If it is not practical to use a smaller number of implementation dates, employers will need to receive clear communications informing them of their particular start date, so that there is no confusion as to when the requirements apply.

4. We note that there will be a small test group of randomly selected smaller employers (those with fewer than 50 jobholders) who will be required to automatically enrol their jobholders ahead of other employers of their size. This is a sensible approach. However, a completely random selection could lead to very small employers (such as those with only one or two jobholders) being required to comply early with the automatic enrolment requirements and, in our view, could pose too great a burden on them. We therefore suggest that a minimum number of jobholders is considered for this test group. In addition, both the employers and employees in the test group will be required to contribute for longer overall than other entities of a similar size, potentially putting them at a disadvantage when compared with their competitors. This could be addressed by seeking the consent of those employers selected to participate in the test group or providing some incentive for them to participate.

5. It would also be useful if the test group of smaller employers covered a broad range of industries, so that any difficulties which may be particular to different sectors can be factored in at an early stage.

6. For employers, communication will be a key issue at all stages of the automatic enrolment process, but particularly when they are first introducing it to their workforce. Is it the DWP's intention that there will be standard communications available for employers to use (which can be adapted as necessary), to explain why automatic enrolment is being introduced and how it will work in practice? A common concern for employers when promoting pension arrangements (particularly defined contribution (DC) where members need to be encouraged to make investment

decisions) is the fine line between providing information and giving investment advice (which they will not be authorised to do). Guidance and standard form communications which deals with such issues are likely to be warmly welcomed.

7. There will also need to be clear lines of communication in place between those responsible for implementing the 2012 reforms (including the DWP, TPR and the Personal Accounts Delivery Authority) and employers, to ensure that the policy aims of automatic enrolment are properly understood by those required to operate it. (Clarification of the division of responsibility between these departments would also be helpful).

8. It will need to be made very clear to employers that any closure of a defined benefit (DB) scheme during the transitional period, and subsequent enrolment of jobholders into an alternative DC scheme will result in having to pay backdated contributions. This could be significant if up to three years' contributions become payable. Employers will need to be able to factor this in to any changes to their pension arrangements.

[The employer obligation to automatically enrol employees into either a workplace pension arrangement or the Personal Accounts Scheme will be both "staged" and subject to "transitional arrangements". The proposed staging process will, if adopted, see the obligation introduced in 25-30 batches, over three years, based on the size of the employer, applying first to larger employers and then to smaller ones. Under the transitional arrangements, the contribution requirements for DC schemes (for both members and employers) will be gradually phased in over a period of three years. For employers who sponsor DB and hybrid schemes, the transitional provisions will permit delayed implementation of the obligation until the end of the three year staging period.]

9. In addition, a major concern for employers and individuals alike will be to ensure that only those who will actually benefit from automatic enrolment will be enrolled into a qualifying scheme or a Personal Account. This means that jobholders will need to be provided with sufficient information about the potential impact on their overall benefits to ensure they do not lose out on means tested state benefits at a later stage. Further thought needs to be given as to how this can be achieved, so that employers are not at risk of mis-selling pensions to their employees. For example, will guidance

be made available which will enable individuals to make reasoned decisions about whether or not to opt-out?

10. We echo the general concerns voiced by the pensions industry that the introduction of the automatic enrolment obligation could lead to a levelling down of benefits provided via existing schemes. There is also a risk that the complicated proposals put forward for dealing with implementation of the automatic enrolment obligation in relation to hybrid and shared risk schemes will dissuade employers from offering these benefits at all.

11. Finally, while we understand the need to ensure that external providers have sufficient lead-in time to be able to deliver various elements of the employer compliance regime, we were disappointed with the DWP's decision to limit the consultation period to six weeks. Given the scope of the consultation document and the significance of the reforms, six weeks is insufficient time for the industry to collate and submit full responses.

C. Consultation questions

The Employers' Duties (Implementation) Regulations 2010

Q2 Regulation 3 (Early automatic enrolment)

In our view, employers are unlikely to consider initiating early implementation of the automatic enrolment obligation unless they already have in place a qualifying scheme in which to enrol members. Both the time limits for enrolling members (which will apply from the early commencement date) and the fines for non-compliance are likely to act as deterrents to most employers to signing up early.

Given that an employer will be required to apply to TPR for permission to take on the automatic enrolment obligation early, it should not cause an additional administrative burden for the application to include a simple declaration that the employer is in a position to discharge its automatic enrolment duties.

The general drafting of this regulation appears to be overly prescriptive.

The Occupational and Personal Pension Schemes (Automatic Enrolment) Regulations 2010

Q4 Regulation 13 (Automatic re-enrolment dates)

We recognise that there may be circumstances where, for example due to an administrative error by a scheme's third party administrator, a member may inadvertently be removed from membership of the scheme.

Similarly if a trustee has wide unilateral powers, there is a risk that it alone could take action which inadvertently leads to a technical breach by the employer of its automatic enrolment duty. For example, this could conceivably occur in a large multi-employer or industry-wide scheme where the trustee has unilateral powers enabling it to close the scheme (or a section of the scheme), or change the benefits provided, resulting in the scheme no longer meeting the qualifying criteria. Emphasis therefore needs to be placed on communication between trustees and employers to ensure that such technical breaches do not occur inadvertently.

In these circumstances, the employer should be given the opportunity to re-enrol any affected members (or enrol them in an alternative qualifying scheme) within a reasonable period, for example 30 days of discovering the technical breach.

Q6 Regulation 29 (Staged increase in appropriate age)

[The consultation document makes reference to proposed changes to the State Pension Age. The Pensions Act 2007 made provision for this to increase incrementally until it reaches 68 for both men and women in 2046. Respondents to the consultation were asked whether the "appropriate age" (i.e. the age at which payment of pension will commence) for the purposes of the test scheme (the standard by which contracted-in DB schemes will be measured) should increase in line with increases to the state pension age. In this context, it should be noted that in 2010, the Government will be reviewing the "default retirement age" of 65, and, it is possible that the state pension age will also be reviewed following the 2010 General Election.]

The ultimate answer to this question will depend in part on the outcome of the Government's review of the default retirement age in 2010 (and on any changes to pension age made by a subsequent government after the General Election).

While it would be logical for normal pension age in qualifying schemes to fit with the state pension age from time to time, an evolving pension age may be difficult to administer and is likely to bring an additional layer of complexity to arrangements which need to be easily communicated to employers and members alike. This will be particularly important for defined benefit and hybrid schemes.

If qualifying schemes are expected to increase their retirement age in line with changes to the state pension age, the regulations will need to incorporate a statutory override provision which allows them to do this.

Q8-11 Regulation 38 (Prescribed requirements for non-UK Qualifying Schemes)

The ability to automatically enrol jobholders into a non-UK scheme is likely to be useful for a small number of employers whose jobholders are internationally mobile.

In order to protect any individuals who are enrolled into overseas schemes, those non-UK schemes which are used as an automatic enrolment vehicle should meet a minimum standard, not only in terms of the benefits which are provided but also the standard of regulation in the country where the scheme is established. One way of achieving this minimum standard may be to limit non-UK qualifying schemes to schemes in countries where there is a good track record of pensions regulation, for example within the EU and/or OECD countries.

Q12 Regulation 40 (Postponement of the automatic enrolment date)

We agree with the DWP's comments that the issue of automatic enrolment is a finely balanced one for jobholders on short-term contracts.

There may be relatively significant costs for employers in terms of automatically enrolling such jobholders and ultimately (if the Personal Accounts scheme is not used as the automatic enrolment vehicle) removing them from the arrangement in question at the end of their contract. However, given that those on short-term contracts are likely to make up a significant proportion of the target group at which these pension reforms are aimed, the suggestion put forward in the present consultation - to prevent employers from using postponement for jobholders on short-term contracts - would ensure that those in this group are protected and have the opportunity (perhaps for the first time) to save for their retirement. It would also potentially help promote pension saving generally.

An employer with an existing pension arrangement would need to take a policy decision as to whether jobholders on short-term contracts could be automatically enrolled into that scheme, or whether, for the administrative difficulties referred to above, they would enrol such individuals into the Personal Accounts scheme. However, they would need to ensure that where both a workplace pension arrangement and the Personal Accounts scheme are used by the same employer for different groups of jobholders, this is not carried out in such a way that would lead to direct or indirect discrimination (for example, sex or age). This issue is something which should be highlighted to employers.

As a general point, account should also be taken of the position for employees who leave a qualifying scheme within two years of joining. Under existing rules, members with between three months and two years service will either be entitled to a refund of their contributions or to transfer their benefits to another arrangement. However, given that it is not intended to permit transfers into the Personal Accounts scheme, contrary to the policy intention of encouraging greater pension saving, more members may be persuaded, as a result, to take a refund of their contributions.

The Employers Duties (Registration and Compliance) Regulations 2010

Q21 Regulation 4 (Registration: Re-registration)

Re-registration is a practical way of ensuring that the information held by TPR remains accurate and up-to-date. The three yearly period is reasonable and should not create undue burdens for employers, provided the forms required to be completed are limited to key information and there are adequate reminders.

Q22 Regulations 6 and 7 (Records)

Requiring records to be kept for six years is reasonable and is consistent with existing duties for trustees of occupational pension schemes under the Scheme Administration Regulations.[1] It also ties in with general requirements relating to tax records.

Q24 Regulation 7 (Records: Trustees, managers and providers)

It will be essential from an employer's own perspective to keep records of those jobholders who have opted-out, in order to keep track of compliance with its

[1] Regulation 14: The Occupational Pension Schemes (Scheme Administration) Regulations 1996

automatic enrolment obligations. The suggested provisions of regulation 7 seem reasonable.

Q25 Regulation 9 (Due date for deductions)

Using the 19th of the month following the month in which contributions were deducted (or in which employer contributions are due) as the time limit for paying over contributions to the relevant arrangement ties in with the existing provisions of the Scheme Administration Regulations.

Q28 Regulation 13 (Fixed penalty notices)

The effectiveness of any financial penalty is likely to depend on the size of the employer, with £500 providing a substantial deterrent for smaller employers but much less so for larger ones.

The consultation document notes that in most cases, a fixed-rate penalty will have been preceded by informal contact from TPR and a statutory compliance notice. Is TPR intending to produce guidance which will cover expected timescales for action in such circumstances?

Q29 Regulation 13 (Fixed penalty notices)

We consider that offering a discount for early payment of penalties somewhat defeats the object of, and lessens the impact of, the imposition of such penalties. With a view to keeping compliance simple and comprehensible, we think it unnecessary (and potentially counterproductive) to offer early payment discounts.

Q30 Regulation 18 (Inducements)

In the early stages of the roll out of the automatic enrolment obligation, not all jobholders will be aware of the longer-term consequences of any inducement to opt-out.

In order to ensure a consistent approach with other legislation, the look back period for investigating inducements could tie in with, for example, the rules relating to internal dispute legislation or the legislation relating to employment law claims.

The Occupation Pension Schemes (19 Day Rule) (Amendment) Regulations

Q31 Regulation 2

As noted in the consultation document, there are risks associated with the proposed approach of extending the period during which contributions can be held by the employer, on behalf of the member, before paying them over to the scheme at the end of the opt-out period. This is primarily an issue for DC schemes, where the individual is at risk of losing out on positive investment returns.

However, given the need to manage risk and minimise costs, on balance we see this as a sensible approach in order to minimise the complexity surrounding refunds of contributions from a scheme when individuals elect to opt-out.

Sacker & Partners LLP

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