The Transfer of Employment (Pension Protection) (Amendment) Regulations 2013

Public consultation

The NAPF's response

April 2013

Overview

The NAPF welcomes the Government's consultation on simplification of the Transfer of Employment (Pension Protection) Regulations 2005. However, we have significant concerns about the Government's approach, which perpetuates differing protection for transferring employees depending on whether they are eligible to join occupational or contract-based pension schemes. Where both the transferor employer and the transferee employer provide money purchase arrangements, a transferee employer should not be required to pay higher contributions than the transferor employer paid; but neither should the transferee employer pay lower contributions just because the transferor employer provided an occupational scheme.

The Government also fails to achieve its stated purpose in the draft amendments intended to allow the employee to set the rate of any required matching contribution.

The NAPF recommends that the amended regulations should:

- require that the transferee employer pay contributions on the same basis as the transferor employer where the transfer is from one employer who provides a money purchase scheme to another employer who provides a money purchase scheme;
- retain the current requirements for a transferee employer who provides a non-money purchase scheme, and
- clarify that the rate of any matching contribution up to 6% of pensionable earnings (which should continue to be an option where the transfer is from an occupational defined benefit scheme) will be determined by the employee.

About the NAPF

The NAPF is the leading voice of workplace pensions in the UK, speaking for 1,300 pension schemes with some 16 million members and assets of around £900 billion. NAPF members also include over 400 businesses providing essential services to the pensions sector.

Introduction

1. The Pensions Act 2004 requires that where employees who were eligible to participate in an occupational scheme are transferred, the transferee employer (the "transferee") must provide a benefit from an occupational pension scheme or a stakeholder scheme in accordance with The Transfer of Employment (Pension Protection) Regulations 2005 ("the Regulations"). In the absence of this legislation, even employees who participate in a good quality occupational pension scheme with the transferor employer (the "transferor") would have no right to any pension from a transferee. This is because transfer of undertakings legislation, in accordance with European law, does not apply to most benefits from occupational pension schemes.

2. In contrast, because arrangements relating to group personal pension plans ("contract-based schemes") usually form part of the employment contract, they are governed by transfer of undertakings legislation in accordance with European law, and the contribution structure of the transferor's scheme must be continued by the transferee.

3. The Regulations currently do not treat transferring employees who are eligible for an occupational scheme the same way they would be treated if they had been eligible for contract-based provision. The Regulations do not mandate that the transferee provide the same benefits, or even benefits of equal value, to those provided by the transferor. Instead, they require that the transferee employer provide either:
    - a benefit of a value of 6% of pensionable pay (plus up to a 6% of pensionable pay in value from an employee contribution) in a defined benefit scheme, or
    - a contribution structure whereby the transferee matches the contribution of the employee, up to 6% of pensionable pay, to either a defined benefit or defined contribution scheme.

4. The difference in treatment depending on whether the transferor operated an occupational or contract-based scheme is exacerbated by the auto-enrolment legislation. More employers will be participating in pension arrangements, including occupational schemes such as NEST, so the Regulations will come into play more often. Under the current Regulations, the transferor may only be responsible for a contribution of 1% during the transitional period, whereas the transferee must pay up to 6% if the employee is prepared to pay matching contributions. However, a transferee will only need to pay up to a 6% contribution, even where the transferor paid more.

5. The NAPF understands that one of the purposes of the amendments is to provide more equality of treatment between transferees who by law must provide an occupational pension scheme and those who are allowed to provide contract-based arrangements.

6. An additional purpose of the draft regulations is to make clear that it is the employee who controls the amount of any matching contributions, up to 6%.

The proposed amendments

Transfers to defined contribution arrangements

7. The proposed amendments allow a transferee providing a money purchase scheme to choose either to duplicate the charging structure of the transferor or to pay a matching contribution of up to 6% of pensionable earnings. Therefore, the proposed change to the Regulations does not end the inequality of treatment of employees who transfer from an occupational scheme as compared to those transferring from contract-based arrangements. It simply changes the nature of the inequality, to the disadvantage of the employee transferring from an occupational scheme.

8. Under the current Regulations, employees transferring from an occupational money purchase pension scheme might be better or worse off than they would have been (and the transferee could incur more or fewer costs than the transferor) had the transfer been from a contract-based scheme. This would depend on:
    - whether the transferor provided a money purchase or non-money purchase scheme, and
    - assuming that it was a money purchase scheme, whether:
        - the employer was contributing more than or less than 6% and
        - the employee was required to contribute more or less than the match in order to get the employer contribution.

9. Under the amended Regulations, there are no situations in which the transferee must make an employee better off than he would have been if transferring from a contract-based arrangement, but the employee may be worse off. If the transferor was providing only the minimum required by auto-enrolment, that will be the employee's entitlement, but if the transferor was paying a contribution of more than 6%, the transferee need only pay up to a 6% matching contribution. This contrasts with the simpler situation for an employee covered by contract-based provision, who will get what he or she received when employed by the transferor.

10. The NAPF believes that this is an opportunity to make the treatment of members of money purchase schemes, whether those schemes are contract-based or occupational, more similar on transfer of employment. **We agree that the transferee should not be required to pay more than the transferor paid in contributions. We also agree that to require transferees to replace defined benefit provision with equally valuable defined benefit provision would discourage transfers of undertakings disproportionately. However, where the transfer is from one employer who provides money purchase benefits to another employer who provides money purchase benefits, we do not understand why the Regulations do not require that the contribution structure continue, as is the case for contract-based schemes.**

Transfers to defined benefit arrangements

11. There is no commentary accompanying the change to the Regulations for transfers to a transferee who operates a defined benefit arrangement, and so we do not know the policy intention. The current Regulations require that where the transfer is to a non-money purchase arrangement, the transferee must provide benefits the value of which is at least 6 per cent of pensionable pay (plus an additional employee contribution of 6% in value) or must pay a 6% matching contribution. Under the amended Regulations, the 6% matching contribution alternative is replaced by an alternative under which the transferee's contributions equal those of the transferor. (See proposed Regulation 3(1C), which is applicable to defined benefit plans under Regulation 2(1)(b) by operation of Regulation 3(1B)).

12. As discussed above, we believe that looking at the contributions made by the transferor is appropriate in the defined contribution context, but we do not see why the transferor's contributions are relevant where the transfer is to a defined benefit scheme. After all, the transferor may have had artificially high or low contributions in the preceding years due to a temporary contribution cessation or payment for redundancy-related benefits. The establishment of a defined benefit scheme for transferring employees where the transferor provided a defined contribution scheme would be very unusual and so it is difficult to see what purpose this change is designed to achieve.

13. The current regulations, which require that benefits or contributions be of a certain value, are more appropriate where transfers are between defined benefit schemes than any requirement based on comparative employer contributions.

Matching contributions

14. The language intended to clarify that the member will set the amount of the matching contribution fails to achieve its purpose. Regulation 3(1D) states that subject to the 6% ceiling, the transferee's contributions must be "at least equal to the contributions made by the employee provided the amount of the employee's contributions are permitted under the scheme rules." However, because employers generally have the power to set the level of contributions under money purchase scheme rules, this language puts the matching contribution firmly within the employer's control. This should be corrected because we believe that the 6% matching contribution remains an important alternative when the transfer is from a defined benefit scheme. In addition, the reference to "remuneration" in Regulation 3(1E) is inappropriate as "remuneration" is not defined. The term "pensionable pay" is used elsewhere in the Regulations and should be employed here as well.

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Questions

1. **Do you consider that the proposed changes to regulation 3 will correctly reflect the original policy intention as set out in the Explanatory Memorandum attached to the 2005 Regulations, and do the changes make the regulations workable in practice? If you do not believe that this has been achieved, please set out detailed reasons.**

   No, we do not believe that the policy intention of allowing the employee to set the rate of the matching contribution, up to 6% of pensionable pay, is met by the language in the amended Regulations. It looks as though this was intended to be achieved by a new requirement in Regulation 3(1D), which is satisfied where "the transferee's contributions are at least equal to the contributions made by the employee provided the amount of the employee's contributions are permitted under the scheme rules." The language following the word "provided" appears to limit employee contributions to those permitted under the scheme rules. Under money purchase scheme rules the contribution rate will often be under the employer's unilateral control. Therefore the proposed language allows the employer to set the rate of any matching contribution.

   If the objective is to establish employee control over the matching contribution, it might be better to state that the requirement is met when the transferee's contributions at least equal the employee's contributions, "provided that the scheme rules allow or require the employee to contribute no less than 6% of pensionable pay to the scheme".

2. **Do you consider that the proposed introduction of an alternative method of satisfying the 'relevant contributions' will remove the risk that transferee employers might face substantially higher pension contributions than the transferor employer whilst maintaining the principle of adequate pension protection for transferring employees?**

   The proposed alternative method will remove the risk that the transferee employer will pay more than the transferor employer, but it does not require that the transferee employer pay the same contributions as the transferor employer where the transferor paid more than a 6% matching contribution. We believe that this is a flaw in the amended Regulations for the reasons discussed above, and that the treatment of employees transferring from money purchase occupational pension schemes should be the same as that of employees transferring from contract-based provision. There should not be an advantage to transferees depending on whether the money purchase scheme of the transferor was occupational or contract-based.

   As amended, the Regulations would leave employees transferring from good pension provision in an occupational money purchase pension scheme in a worse position than they would have been had the employer provided the same benefit through a contract-based arrangement. This does not, in our view, maintain the principle of adequate pension protection for transferring employees.