PENSIONS (NORTHERN IRELAND) ORDER 2005

S.I. 2005 255

EXPLANATORY MEMORANDUM

INTRODUCTION

1. The Pensions (Northern Ireland) Order 2005 ("the Order") was made on 9th February 2005. This Explanatory Memorandum has been prepared by the Department for Social Development ("the Department") in order to assist the reader in understanding the Order.

2. This Memorandum needs to be read in conjunction with the Order. It is not, and is not meant to be, a comprehensive description of the Order.

BACKGROUND AND POLICY OBJECTIVES

3. The Order makes provision for Northern Ireland corresponding to provisions of the Pensions Act 2004 ("the Act"). It is intended to improve members' security while ensuring, through simplification and deregulation in some areas, that the costs of providing good schemes do not rise.

4. The Order has 9 Parts comprising 294 Articles and 11 Schedules.

5. The Act establishes a new UK-wide Non-Departmental Public Body (NDPB), the Pensions Regulator ("the Regulator") to replace the Occupational Pensions Regulatory Authority (Opra). The Regulator will take over Opra's responsibilities for the regulation of occupational pensions and of certain functions of personal pensions and stakeholder pensions. Like Opra, the Regulator will be funded by a levy on schemes. The Regulator will also assume a number of new functions. The Act also establishes the Pensions Regulator Tribunal to deal with references from determinations by the Regulator.

6. The Act sets up a second NDPB: the Board of the Pension Protection Fund (PPF). The PPF will provide compensation for members of defined benefit (normally final salary) and hybrid occupational pension schemes in the event of a scheme's sponsoring employer becoming insolvent, leaving the scheme with insufficient funds to pay its members the pension they were expecting. The PPF will also be funded by levy. The Act establishes the PPF Ombudsman as the external appeals body in relation to the PPF. The Board of the PPF will subsume the functions of the Pensions Compensation Board (PCB).

7. This Order makes provision for the functions of these bodies in relation to Northern Ireland (Parts II and III).

8. New provisions in Part IV replace the Minimum Funding Requirement with a new scheme specific system, allowing schemes greater flexibility in developing funding strategies appropriate to their circumstances.

9. The Act provides for a new function of the Secretary of State for Work and Pensions and the Department to promote and facilitate financial retirement planning. Part V of the Order makes provision for disclosure of certain information to facilitate such planning.

There is provision for reserve powers to require employers to provide employees with access to pension planning information and to compel occupational or personal pension schemes to provide combined pension forecasts incorporating state pensions data.

10. Part VI covers a number of matters relating to the administration of occupational and personal pension schemes.

11. Part VII provides for cross-border activities within the European Union. It introduces regulatory measures that will support the operation of pan-European occupational pension schemes.

12. Part VIII deals with State Pensions: in particular it improves the position of pensioners who defer taking their State Pension. Plans for an increase in increments, originally planned for 2010, have been brought forward to 2005. It also introduces the option for deferrers to take the deferred pension as a lump sum.

13. Part IX deals with a number of ancillary matters.

CONSULTATION

14. Prior to the making of the Order, there was a UK-wide consultation on the following documents: the Green Paper, *Simplicity, security and choice: Working and saving for retirement [Cm 5677]*; and, the Action Plan, *Working and saving for retirement: Action on occupational pensions [Cm 5835]*, issued in Northern Ireland by the Department. The responses were taken into account when developing the provisions of the Act and the Order.

OVERVIEW

PART II – The Pensions Regulator

15. This Part sets out the statutory objectives and functions that provide an overarching framework for the Regulator's activities.

16. The Regulator will operate a targeted and proportionate system, applying greater regulatory scrutiny where members' benefits are most at risk. This approach will be supported by increased powers to gather, retain and share information. The information gathered will be used to help identify those schemes where members' benefits are more likely to be at risk.

17. The Order introduces a range of functions for the Regulator including:

- provision of information, education and advice to trustees and managers, employers etc.;
- issuing of improvement notices or third party notices to remedy breaches;
- powers in relation to winding up of occupational pension schemes;
- maintenance of a register of schemes and a register of prohibited trustees;
- powers to gather information, including powers to enter premises etc.;
- to freeze a scheme whilst investigations take place to protect members' benefits or scheme assets;
- issuing contribution notices, financial support directions and making orders regarding transactions at an undervalue;
- increased powers covering the suspension and removal of trustees.

18. The Regulator will also be able to issue codes of practice. This will provide those involved in pensions with practical guidance in relation to their duties and responsibilities under pensions legislation, thus assisting schemes in improving compliance and encouraging best practice. In certain areas the Regulator will be obliged

to provide codes of practice, for example, on disclosure of information to scheme members.

19. This Part also sets out certain provisions in relation to the Pensions Regulator Tribunal, which will hear references from the Regulator's determinations.

20. Part II also places duties on trustees or managers, and other scheme professionals to provide information and to report certain events and breaches of the law to the Regulator.

Part III – The Board of the Pension Protection Fund

21. This Part sets out the functions of the Board of the PPF. The main aim of the PPF is to provide protection for members of defined benefit and hybrid schemes. It will compensate members of such schemes should the employer become insolvent and leave the pension scheme under-funded. It will also assume the functions of the existing PCB.

22. Scheme members will become eligible for compensation when the sponsoring employer is insolvent (and there is no hope of corporate rescue or business rescue with the pensions liabilities attached), and the pension scheme has insufficient assets to buy out the PPF level of benefits. Existing pensioners (with some exceptions) will receive 100% of the pension actually in payment, while deferred pensioners (those below the Normal Pension Age) will receive 90% subject to a cap, calculated using a combination of individuals' scheme rules and PPF standardised rules.

23. Compensation will provide for survivors' benefits, and for indexation on rights accrued after 1997, in line with the rate of increase in the Retail Prices Index (RPI), capped at 2.5%, and all deferred rights revalued in line with the increase in RPI capped at 5% from the assessment date.

24. There will be a compulsory annual levy on all defined benefit and hybrid schemes (collected by the Regulator). The levy will consist of an administration levy, a fraud compensation levy and pension protection levies (to be calculated on the basis of both scheme features and risk-based factors in the long-term, though initially only on scheme features).

25. There will be a procedure for dealing with disputes of facts and law regarding PPF decisions and issues of maladministration. This will include internal dispute resolution procedures followed by referral to the PPF Ombudsman, a new office created to deal with PPF disputes.

26. *Chapter 1* makes provision relating to the functions of the Board of the PPF and provides for the administration levy.

27. *Chapter 2* makes provision relating to action to be taken in relation to insolvency events.

28. *Chapter 3* makes detailed provision relating to the operation of the PPF, the pension protection levies and the circumstances in which the Board of the PPF will assume responsibility for a scheme.

29. *Chapter 4* makes provision for fraud compensation payments to be made to a scheme where the value of the assets of the scheme have been reduced due to an act or omission constituting a prescribed offence and the employer is unlikely to continue as a going concern.

30. *Chapter 5* provides for powers to gather and disclose information, including powers to enter premises etc.

31. *Chapter 6* provides for dealing with reviews of decisions of the Board, including reference to the PPF Ombudsman etc.

32. *Chapter 7* makes miscellaneous provision relating to the PPF including the discharge of pension sharing orders.

Part IV – Scheme Funding

33. This Part deals with the statutory framework for the scheme funding requirements that are to replace the Minimum Funding Requirement (MFR) which applies to defined benefit schemes. Under the arrangements set out in this Part, schemes will not be required to fund to a common funding measure. Pension scheme trustees, having taken advice from the actuary, will be required to agree with the sponsoring employer a strategy for funding the pension commitments and for correcting any funding deficits, and to set this out in a Statement of Funding Principles. The new funding framework carries forward the existing statutory requirements for regular actuarial valuations and for a scheme to have in place a schedule of contributions. In general, subject to the provisions of this Part, schemes are required to meet a statutory funding objective to have sufficient and appropriate assets to provide for their liabilities.

Part V – Financial Planning for Retirement

34. This Part makes provision in consequence of Part 4 of the Act which provides for the Secretary of State for Work and Pensions and the Department to promote and facilitate financial planning. In particular, it provides for the disclosure of certain information to facilitate such planning and provides powers to require schemes to provide combined pension forecasts and for employers to provide their employees with access to information and advice about pensions and saving for retirement.

Part VI – Occupational and Personal Pension Schemes: Miscellaneous Provisions

35. This Part sets out a number of measures which will apply to occupational and personal pension schemes. These broadly fall into three groups: the first provides simplifications for the administration of pension schemes; the second deals with employers' and schemes' obligations; and finally, the third covers some clarifications and corrections where existing law has been found to be unclear.

36. *Articles 216* and *217* make provision in relation to definitions of occupational pension schemes and personal pension schemes in the Pension Schemes (Northern Ireland) Act 1993, and in relation to those treated as "employers" for the purposes of the Pensions (Northern Ireland) Order 1995.

37. *Articles 218* to *226* deal with member-nominated scheme trustees and (where every trustee of a scheme is a company) directors. One third of a scheme's trustees are to be member-nominated in a process involving all of the active members of a scheme. Employers will no longer be able to opt out of these arrangements but, if necessary, the employer may propose alternative arrangements that may be adopted if approved by the members through a statutory consultation procedure. Trustees of occupational pension schemes will be required to gain sufficient knowledge of the law as it relates to pensions and trusts and of the fundamental principles relating to funding and the investment of assets. In the same vein, trustees must prepare, review and maintain a written statement of the principles governing investment decisions.

38. *Articles 227* and *228* provide new rules governing payments to an employer from an actuarial surplus in an ongoing occupational pension scheme and how such a surplus should be determined.

39. *Articles 229* to *231* require an occupational pension scheme with its main administration in the United Kingdom not to accept a funding payment unless it is set up under irrevocable trusts. Where a scheme has its main administration outside the European Union (non-EU schemes), employers may not make contributions unless the scheme is established under trusts and has a trustee in the UK. Where the trustees of a non-EU

scheme appoint someone to act on their behalf in the UK, that person may be treated as a trustee.

40. *Article 232* implements Article 7 of the EU directive on Institutions for Occupational Retirement Provision (Directive 2003/41/EC) ("the Directive"), by providing that, subject to prescribed exceptions, an occupational pension scheme in the UK must limit its activities to those relating to providing retirement benefit.

41. *Article 233* prohibits a scheme from indemnifying a trustee for any fine or penalty for a failure to comply with his duties.

42. *Articles 234* and *235* oblige employers to offer a minimum level of pension provision to employees transferred to them (provided they had access to an occupational pension scheme with the employer pre-transfer).

43. *Articles 236* to *238* provide that employers will be required to consult with scheme members when they are proposing to make prescribed decisions relating to their pension scheme arrangements.

44. *Article 239* substitutes Article 67 of the Pensions (Northern Ireland) Order 1995 (restriction on powers to alter schemes). This makes it possible for schemes to modify members' subsisting pension rights either by obtaining the members' consent to do so or by replacing their existing rights with other rights of actuarially equivalent value. This will provide schemes with greater flexibility to reduce administrative costs and complexity.

45. *Articles 240* and *241* make provision relating to employees who leave an occupational pension scheme within a vesting period (which currently may be up to two years). Under existing arrangements, such leavers do not build up any rights in the scheme. Instead, they are given a refund of contributions. *Article 241* provides that early leavers (employees who have been scheme members for at least three months, but who leave before their rights have vested) will be entitled to either a cash transfer or a refund of their contributions. This will allow people to build up pension rights from each employment where they have joined a pension scheme.

46. *Article 242* provides for the protection of pension rights during periods of paid paternity leave and adoption leave.

47. *Article 243* clarifies the existing law to ensure that the rules relating to the inalienablity of occupational pensions do not apply to payment of pension made in error.

48. *Article 244* removes the requirement for occupational pension schemes to accept voluntary contributions from scheme members.

49. *Articles 245* and *246* make provision in relation to payments made by employers to pension schemes and impose a duty on trustees and managers to monitor payment of contributions by employers and to report failure to pay contributions to the Regulator etc.

50. *Article 247* provides for a new priority order where a scheme is being wound up. The new priority order will ensure that members of schemes wound up due to employer insolvency, with sufficient funds to meet more than the benefits guaranteed by the PPF, do not find themselves in a worse position than if the scheme had less funds and was covered by the PPF. It also ensures that the same priority order is provided for the distribution of assets when a scheme starts to wind up and the employer is solvent.

51. *Articles 248* and *249* provide that, in situations where an employer is still solvent but chooses to wind up a pension scheme, the trustees will choose the date from which the assets and liabilities should be valued. If the liabilities turn out to be more than the assets, then the difference is a debt due from the employer to the trustees. If an employer becomes insolvent, and the assets are less than the liabilities immediately

before it occurred, then the employer's debt is taken as arising immediately before the insolvency event.

52. *Article 250* makes provision relating to the resolution of disputes. Trustees or managers will have to ensure the implementation of dispute resolution systems that will provide procedures by which any person who has an interest in a scheme can approach them with a dispute and have it resolved within a reasonable period of time.

53. *Articles 251*to *253* make provision consequential on the new post of Deputy Pensions Ombudsman, which is created by the Act, and clarify the Ombudsman's jurisdiction in relation to those involved in scheme administration.

54. *Article 254* abolishes the restriction that the amount of compensation provided by the PCB must be less than the amount of the loss. Schemes with an insolvent employer may now be compensated for the full amount lost as a result of acts of dishonesty. It also allows the Board to review a determination without an application being made.

55. *Articles 255* to *257* deal with changes to the indexation requirements. Schemes will only be required to index pensions already in payment by inflation, capped at 2.5%, each year. This will ease funding liabilities for employers in the future and will avoid the serious effect on pensioners' incomes that could arise if indexation were to be removed entirely.

56. *Article 258* provides that the statutory revaluation requirement is satisfied if the total pension or benefit is revalued fully in line with the RPI.

57. *Articles 259* to *261* make provision relating to contracting out of the earnings-related part of State Pension; in particular they amend the definition of "working life" for the purposes of guaranteed minimum pension (GMP) and allow, in certain circumstances, for the payment of a lump sum instead of a GMP.

58. *Article 262* clarifies the law relating to stakeholder pensions by making clear that the cap on charges which may be levied applies to contributions made by the member and any contributions made on the member's behalf. It also makes clear that stakeholder schemes must be contracted out schemes.

Part VII – Cross-Border Activities Within European Union

59. This Part introduces provisions required to comply with the requirements of the Directive concerning the activities and supervision of institutions for occupational retirement provision that are engaged in "cross-border activity". A key objective of the Directive is to put a regulatory framework in place that will enable an occupational pension scheme located in one EU Member State to accept contributions from an employer based in another Member State. This Part sets out the circumstances in which a scheme in Northern Ireland can accept contributions from an employer based outside the UK.

Part VIII – State Pensions

60. This Part deals with a number of changes to be made to State Pensions. It allows that, where a person is entitled to more than one State Pension, they will be able to choose which of these they wish to receive.

61. Currently, if a person does not claim their State Pension from the date they reach pensionable age, either because he is working or for other reasons, he will not receive a pension for the period between pension age and the date of claim. Instead, he will qualify for an incremental increase to his weekly pension from the point at which he does claim. The current rate of the rise in increments is 7.4%, the Order provides for this to be raised to 10.4%. Pensioners will also be given the option of receiving a taxable lump sum (after at least 12 months deferral) comprising the pension foregone and a rate of return 2% above base rate.

Part IX – Miscellaneous and Supplementary

62. This Part contains 20 Articles under 5 headings: "Dissolution of existing bodies – information"; "Electronic working"; "General"; "Regulations and orders"; and, "Miscellaneous and supplementary".

63. Information obtained by the PPF Board as a result of the dissolution of the PCB will be subject to the information provisions of Articles 179 to 183 and 185 of the Order and any restrictions on holding information to which the PCB was subject shall also apply to the Board of the PPF. Similarly, where information held by Opra is transferred to the Regulator, it is to be treated as "restricted information" for the purpose of Articles 77 to 82 and therefore subject to limitations on its disclosure.

64. Under Electronic working, the Order makes comprehensive provision about the form in which notifications and other documents may be supplied electronically, and the timing and location of things done electronically.

65. The Articles under "General":

- set out which provisions are to override any rules of personal or occupational pension schemes with which they conflict;
- allow provisions of the Order to be modified to encompass and fit any particular complexities associated with hybrid or multi-employer schemes;
- allow modification of pensions legislation that refers to employers;
- make provision about the admissibility of statements and information that is covered by legal professional privilege etc.;
- make provision in relation to liens; and,
- set out which provisions of the Order will apply to the Crown.

66. Under "Regulations and orders", any regulations under the Order that impose an obligation on someone can provide that a breach of the obligation is a criminal offence or that it exposes the person in breach to a civil penalty. This Part also provides for consultation on any proposals for regulations under the Order.

67. Articles under "Miscellaneous and supplementary" introduce Schedule 10, which makes minor and consequential amendments to existing legislation so that it will work satisfactorily alongside provision made in the Order, and Schedule 11, which specifies which statutory provisions are repealed, and to what extent. This Part also allows the Department to modify certain provisions of the pension legislation for the purpose of consolidation and to make transitional provisions, and allows consequential amendments to be made to the Order pursuant to the Civil Partnership Act 2004.

Schedules

Schedule 1: The Pensions Regulator

68. This Schedule will enable the Regulator to delegate any of its functions to an executive member of the Regulator, any other member of the staff of the Regulator, or any of its committees (other than the appointments committee, the Determinations Panel and any of that panel's sub-committees). It also sets out the powers that the Regulator may authorise the Determinations Panel to exercise on its behalf.

Schedule 2: The Reserved Regulatory Functions

69. This Schedule lists the reserved regulatory functions of the Regulator which may be exercised on its behalf by the Determinations Panel. Part 1 lists those from the Pension Schemes Act; Part 2 from the 1995 Order; Part 3 from the 1999 Order; and, Part 4 lists the relevant functions under this Order.

Schedule 3: Restricted information held by the Regulator: certain permitted disclosures to facilitate exercise of functions

70. This Schedule provides a list of bodies to which the Regulator may disclose restricted information and the functions for which it can be disclosed.

Schedule 4: The Board of the Pension Protection Fund

71. This Schedule enables the Board to authorise any executive member of the Board; any other member of staff; or any of its committees or sub-committees to exercise functions of the Board. This Schedule also gives the Board the power to make arrangements for the exercise of certain of its functions on its behalf, in order to ensure that the mechanisms by which the PPF delivers its business are flexible enough to allow it to operate effectively from day one.

Schedule 5: Transfer of property, rights and liabilities to the Board of the PPF

72. This Schedule makes additional provision for situations where the assets and liabilities of a scheme are transferred to the Board. The property, rights and liabilities to be transferred include: property (situated anywhere in the UK or elsewhere); rights and liabilities that would not otherwise be able to be transferred or assigned; rights and liabilities under UK law.

Schedule 6: Pension compensation provisions

73. This Schedule explains how PPF compensation is to be paid to members of pension schemes for which the Board assumes responsibility.

Schedule 7: Restricted information held by the Board of the PPF: certain permitted disclosures to facilitate exercise of functions

74. This Schedule sets out the list of bodies to which the Board may disclose restricted information and the functions for which it can be disclosed.

Schedule 8: Reviewable matters

75. This Schedule sets out the list of “reviewable matters” that are subject to challenge.

Schedule 9: Deferral of retirement pension and shared additional pensions

76. This Schedule relates to the provisions of Part VIII; it provides the framework of the new deferral proposals. These changes are to be put into effect by amending and extending existing provisions. In this case, the key piece of legislation amended by this Schedule is Schedule 5 to the Contributions and Benefits Act, which currently details how increments are to be calculated where a person has deferred their pension.

Schedule 10 and Schedule 11: Minor and consequential amendments; Repeals

77. These Schedules make minor consequential amendments and repeals.