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Current issues

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Articles this month:

DC oversight shake-up
We're anti-scammin' (we hope you're anti-scammin' too)
New rights for parents of tiniest tots
Sister schemes to share surplus
Think-tank's thoughts on small DC pots
HMRC newsletters

DC oversight shake-up

The Pensions Regulator announced changes to its supervision of defined contribution (DC) master-trust schemes.[1] It says that they will allow speedier identification of emerging risks, and help make DC master trusts into '*the gold standard in pensions provision.*' It's part of a move towards a more-prudential approach, under which the Regulator will be watchful for system-wide risks, in addition to scheme-level ones.

Now that master trusts account for around 90% of trust-base DC pensions, the Regulator has concluded that the time is right to prioritize value for money. Investment, data quality and retirement innovation get special mention.

DC schemes will be sub-divided, for supervisory purposes, using the following categories:

- 'monoline' master trusts[2]
- commercial master trusts
- non-commercial master trusts and collective schemes
- single and connected-employer schemes

[1] *Oversight of largest DC schemes evolves with a sharper focus on member outcomes* (PN25-03).

[2] This odd terminology may be unfamiliar to some readers (they won't find an explanation in the Regulator's announcements), although it has been in use for a few years. The Department for Work and Pensions has used it (*Evolving the regulatory approach to master trusts*, November 2023) to differentiate between DC master trusts that were set up to provide employers great and (especially) small with ways to comply with their statutory automatic-enrolment duties—NEST being the paradigmatic example—from commercial master trusts that target their customers rather than offering a mass-market solution.

The schemes in each market segment will experience a degree of regulatory contact appropriate to the level of risk that it's perceived to present. Each monoline and commercial master trust will be assigned a group of experts specializing in, variously, financial analysis, business strategy, investment and governance.

The Regulator intends to use real-time data to alert it to arising risks. It expects to issue fewer, more-targeted demands for information, and that meetings will become more-focused affairs between experts. It points to a separate report on the outcome of a master-trust supervision pilot, involving three large schemes, as evidence for the expected benefits of the changes.[3] It hopes that problems will be resolved sooner, that its expectations of schemes will be clearer, that it'll gain greater insights about the challenges and risks in the industry, and that regulatory burdens will be reduced.

If parts of this sound eerily familiar, it may be because aspects of it were aired previously, by the Department for Work and Pensions in November 2023, and by the Regulator itself in a speech given last November.

We're anti-scammin' (we hope you're anti-scammin' too)

The Pensions Regulator posted a blog describing the state of its activities on pension scams. It provides examples of how it works with other organisations and agencies to gather information about, raise awareness of, and combat fraudulent endeavours, and how the pensions industry can help.

The scale of the problem

The Regulator quotes Action Fraud statistics indicating that, in 2023, £17.7m of losses to pensions fraud was reported—an average of £47,000 per person. However, it also cites a Financial Conduct Authority (FCA) estimate that only one-in-five instances of fraud are reported. It encourages scheme members and industry actors to report suspicions immediately, to Action Fraud.

Collective action

For its part, the Regulator's blog emphasizes work with the FCA and support for law-enforcement agencies in anti-scam activity, noting its leadership of the Pension Scams Action Group (PSAG).[4] Particular mention is given to the 'multi-million-pound ScamSmart campaign' of awareness-raising, and Dot Cotton's recent brush with pensions scammers in the BBC's long-running (some might say interminable) *EastEnders* soap opera.

The Regulator has also encouraged industry organisations to take 'the pledge' (to combat pension scams).[5]

Intelligence

The Regulator has sought to enhance its information-gathering capacities, to obtain '*a clearer picture of emerging scam activity*'. To that end, it has entered into 'senior-level strategic partnerships' with other PSAG members, and has seconded people to the City of London Police and the National Economic Crime Centre.

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[3] *Market oversight: DC and master trust supervision.*

[4] Not to be confused with the similarly named Pension Scams Industry Group (PSIG), which is a member of the PSAG.

[5] Hymans Robertson has answered the call.

Educate yourself

The blog closes by promoting a webinar, Fighting Pension Fraud, that the Regulator will be running in conjunction with City of London Police, on 25 March 2025. For educational material on fraud, generally, it suggests directing scheme members to the Stop! Think Fraud campaign by UK Government, City of London Police, National Cyber Security Centre and National Crime Agency.

New rights for parents of the tiniest tots

The Government is, from 6 April 2025, introducing new statutory leave and pay rights for parents of newborns who require extended hospital stays. The details are in draft regulations laid before Parliament.

The new rights, under the *Neonatal Care (Leave & Pay) Act 2023*, will apply to parents of babies born on or after 6 April, if neonatal care commences within the first 28 days after birth, and lasts for at least a week. It will entitle parents to up to twelve weeks of leave (in additional to existing family leave rights), in blocks of at least one week, provided it's taken within the 68 weeks following birth.

Similarly to other statutory family leave rights, employees will have the right to return from leave with their pension rights as if they'd not been absent, on terms no less favourable than if they'd remained at work. During paid neonatal-care leave, pension rights will continue to accrue as if employees were working and being paid as normal, except that member contributions can't exceed the relevant fraction of actual pay.

The interaction of family leave and pension rights is not always straightforward; even legal experts (of which we are not one) can and do reach different conclusions. Readers should seek suitable advice before taking any action on the matter.

Sister schemes to share surplus

The trustee of a defined benefit (DB) pension scheme obtained the approval of the High Court for a proposed merger with a 'sister' scheme.[6] The judge gave his blessing to the merger even though it will dilute the surplus available to augment the benefits of existing members, and both schemes are currently in the process of winding up as a consequence of the sponsoring employer's insolvency.

Background

The employer had had two DB schemes, one for staff and another for executives. They both closed to new members in 2005, and to future accrual in 2011 (prior to the insolvency). The trustee of the staff scheme sought the Court's endorsement of their plans to—

- amend the scheme's rules to give themselves power to accept a bulk transfer; and
- exercise that power to create an unsegregated, merged scheme.

The judge accepted that the application was appropriate because of the 'momentous' nature of the decision. The staff scheme was overfunded, whilst the executive scheme had a funding deficit. A beneficiary was chosen

[6] *Arcadia Group Pension Trust Ltd v Smith* [2025] EWHC 11 (Ch).

to represent the interests of the members of the staff scheme. She had concluded, having had the benefit of legal advice, that there were no realistic grounds on which to oppose the application.

The questions for the Court were whether the trustee’s plan was within the scope of its power, and whether it would be a proper exercise of that power. The Court’s focus was on whether the trustee’s decision was justifiable, and properly reached—not vitiated (impaired) by conflicts of interest—rather than whether it was ‘correct’.

Historical practices were highly relevant to the judge’s conclusions. The schemes had always been run by their trustees ‘side-by-side', as ‘sister schemes’. There was considerable overlap in the two schemes’ trustee directors. They approached the management of the schemes jointly, sharing administrators and advisers, running joint trustees’ meetings and a joint investment committee. Members of the staff scheme could and did go on to membership of the executive scheme when promoted.

The trustees would also negotiate the sponsor’s contribution and then split it between the two schemes based on actuarial advice, aiming to achieve funding parity. Historically, there had been more concern about the staff scheme’s funding position. When the sponsor had paid a special contribution in connection with restructuring, it had also been split with the intention of getting them both to the same funding level. In the event, that meant that the staff scheme received the whole payment. It also got more of the employer’s deficit-reduction contributions, and the lion’s share of the sums distributed by under arrangements entered into by the ultimate owner when the sponsor became insolvent.

On one view, the trustees’ approach was a little too successful. The staff scheme reached the position where its trustee would be able to buy out its members’ benefits in full, whereas the executive scheme was only 87% funded on the same measure. They had been differently affected by the market volatility of 2022, insurer pricing, and mortality experience. Any payments resulting from the employer’s liquidation would be unlikely to eliminate the executive scheme’s buy-out deficit, and would only increase the disparity, because its section 75 debt at the time of the insolvency was around one-fifth that of the staff scheme’s.

Ruling

The Court had no doubts about the change being within the scope of the staff scheme’s power of amendment, which clearly continued to operate until the scheme was wound up, and vested solely in the trustee following the sponsor’s insolvency. It was highly significant that the staff scheme’s rules expressed their object as being the provision of members’ ‘scale’—that is, un-augmented—benefits (although the trustee had augmentation powers in the event of a surplus).

On the question of whether the action planned by the trustee was a proper use of the amendment power, the judge concluded that it was right to consider the way the schemes had been run in the past. Although the rules had been amended at one point to prevent inward transfers from other schemes, the judge noted that the amendment power had been retained without additional fetters afterward, and didn’t think there was any reason to think that it was intended to have narrower scope now, or that the rule against transfers was immutable, when circumstances had changed. Undoing the ban on new members and transfers didn’t undermine the scheme’s expressed object (provision of scale benefits), which would still be achieved, whilst also providing the members of the executive scheme with their intended benefits.

As regards the trustee’s decision-making, the judge thought it noteworthy that arrangements had been made for the re-appointment of a director who was not conflicted by connections to the executive scheme. The unconflicted director was given the decision-making responsibility. The judge said that although there was no legal obligation to merge the schemes, there was a strong moral rationale for it. The historical funding approach had favoured the staff scheme, so it could be said that the executive scheme was the effective source of the surplus. No objections to the plan had received from staff-scheme members, the Pension Protection Fund, or the Pensions Regulator.

The relevant (and no irrelevant) matters having been considered, and the conflict of interest managed in a way that prevented the decision from being tainted, the Court approved it.

There were clearly some very unusual facts and circumstances at play in this case. Nevertheless, the crucial role of the trust purposes, the trustee's conflict management efforts, and its thought process may be of relevance to others faced with decisions about the use of surplus.

Think-tank's thoughts on small DC pots

The Institute for Fiscal Studies has issued a report on small defined-contribution (DC) pots. In summary, it says that—

- there's a strong case for automatic consolidation;
- as a start, multiple pots with the same provider should be merged;
- auto-consolidation should only apply, initially, to pots of less than £1,000, but that the threshold should be indexed and subject to review;
- either of the pot-follows-member and default-consolidator approaches would be preferable to the status quo; and
- exploration of member-choice or lifetime-provider models should only happen once automatic consolidation is in operation.

HMRC newsletters

In our haste to release last month's edition of CI, we overlooked the January 2025 publication of *Pension Schemes Newsletter 166* by His Majesty's Revenue and Customs (HMRC). Please accept our apologies. By way of compensation, this month we've stopped the presses and squeezed in breaking news from the early March publication of *Pension Schemes Newsletter 167*.

Pension Schemes Newsletter 166

The January edition of the *Newsletter* contains articles on—

- the recent consultation exercise on the Governments proposal to levy **inheritance tax on certain death-benefit payments**, saying that it's considering the responses submitted, and will publish its formal outcome and draft legislation later in the year;
- **pension tax codes**, saying that automatic adjustments to the tax codes for new pensioners will, from April 2025, avoid end-year over- or under-payments, because it will automatically update temporary tax codes when the person would benefit from being on a cumulative code;
- submission of **2024 – 25 pension scheme returns via the Managing Pension Schemes (MPS) service**, saying that it won't be possible to submit returns (or amendments) for earlier years using third-party software, that more information will be requested than in the past (some details are given), and offering copies of the template for uploading data in bulk;
- **residency status reports for relief-at-source scheme administrators**;
- the **deadlines for applying for lifetime-allowance protections**, and the transfer of the enhanced protection look-up service into the MPS, from late 2025;
- a probable **delay to the payment of top ups to low earners in net pay arrangement schemes** (it's now likely to happen in 2026);
- **self-assessment tax returns for members of public-sector schemes** who haven't had annual-allowance pension savings statements yet (in summary, they'll be able to use provisional figures; those not using scheme pays could be liable for interest if they underestimate their pension input amount; those who reasonably choose not to submit a return having estimated that no AA charge is due will be able to appeal if that assessment turns out to be wrong); and
- updated **pension flexibility statistics**.

HMRC subsequently updated the section on its plan to improve its pensions tax-coding practices. Its change log said only that the '*Tax Codes for Pensions section has been updated to provide clarification on tax codes for pensions.*' However, a before-and-after comparison showed that HMRC had backed off from saying that members would '*pay the right amount of tax <u>from the outset</u>*' (emphasis added), so that it now says only that they'll pay the correct tax '*faster*'. It also added the caveat that '*The rules for taxing first pension payments are not changing as part of this and the normal rules of PAYE will continue to apply.*'

The coding issue has been a source of friction for people using the defined-contribution flexibilities. In summary, the PAYE system assumes that one-off, initial payments will be repeated. People taking such payments (for example, via flexi-access drawdown) remain susceptible to over-taxation, and may have to submit refund claims.

Pension Schemes Newsletter 167

The March 2025 *Newsletter* contains the following:

- the usual advertisement for **the MPS service** (with sections on what to do about duplicate registrations, and an upcoming enhancement to the financial information that is available—administrators will be able to see breakdowns of money they owe/are owed);
- a reminder of the **changes scheduled for qualifying recognized overseas pension schemes (QROPS)** on 6 April 2025 (EEA schemes will no longer be treated differently from those in the rest of the world);
- clarification of the **real-time information (RTI) reporting processes** for pension commencement excess and stand-alone lump sums; and
- updates for **relief-at-source** scheme administrators.

And Finally…

AF has previously recounted his initial delight upon seeing reference to 'mini umbrella company fraud' in HMRC briefings, and his despondency upon discovering that it had nothing to do with skulduggery in the manufacture of cocktail accoutrements.

The subject recently served up another round of elation-swiftly-followed-by-dejection, when the concept of 'muppet directors' was added to the mix. We're rather afraid that, with our scene-setting, we've already given the game away that this is not about Waldorf and Statler reprising their (pre-Purgatory) roles as the ghostly grasping businessmen (Jacob and Robert Marley) in Brian Henson's peerless retelling of Charles Dickens' *A Christmas Carol*. Instead, it's about the use of stooges to make fraudulent companies look (a bit more) legit.

It reminded *AF* of past episodes of puerile amusement at headlines about non-executive directors, or NEDs. You see, in Scotland, 'ned' means something like 'hooligan, lout or petty criminal'.

It's a usage of considerable vintage, it seems, traceable back as far as 1930. It might help explain why the Scottish person in your office smirked or snorted at business-media headlines involving (some quick Googling ensues) '*Next Gen NEDs*', '*The NED Awards*' (from the Non-executive Directors' Association), '*Could you be a NED?*' (from— tee-hee-hee—NED Space), and '*PR's Unsung Heroes: NEDs*'.

It could also explain why you may have seen it written, less-acronym-amenably, as NXD…

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