expert insight

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Budget changes and their impact on trustees

With the possible exception of the Pensions Act 1995, the announcement from this year's Budget of the removal of the requirement to annuitise defined contribution (DC) schemes represents the biggest change I have witnessed in my 21 years of working in the UK pensions industry.

When you consider the underlying logic (encouraging pensions saving by offering flexibility), and the associated changes (including the Guidance Guarantee, changes to trivial commutation rules etc.), and think through the implications (e.g. investment strategy, communications, funding of defined benefit (DB) schemes given transfers out remain permitted), you get a sense of a sea change which the Pensions Minister is attempting to effect before the next election, scheduled for May 2015.

For us as trustees, that timescale is the key source of the difficulty we have faced in dealing with these changes. The budget was announced on 19 March 2014. The consultation response relating to transfers from DB to DC schemes was published on 21 July 2014. Details relating to the scope and content of the Guidance Guarantee, whether flexibility will be permitted within DB schemes and the precise nature of the taxation regime are yet to be revealed (due Autumn 2014).

The bulk of the changes are scheduled to take effect from 6 April 2015. Members who are due to retire now may wish to wait to take advantage of some of the flexibilities being introduced. But as trustees we are unable to communicate to them the precise conditions which will prevail, neither are we clear as to how this will integrate with existing scheme rules. We are required to signpost the availability of independent free guidance four to six months in advance of a member's retirement date, but we don't know how that guidance will be provided.

As trustees we have therefore focused our efforts to date on data-gathering:

- We've sought to understand the nature of the population we are dealing with
- How many forthcoming retirements are there?
- How big are the fund sizes in question?
- Can members take advantage of interim flexibilities (e.g. changes to the triviality limits)?
- How prepared are our administrators to deal with what could potentially be a significant number of transfer value requests?
- How are our administrators managing pension liberation fraud risks which larger numbers of transfer values could introduce?
- What is the interaction of the changes with the existing scheme rules (noting the permissive statutory over-ride)?
- What do our standard communications upon retirement say and how do they need to be altered based on what we know?

We've also commenced preparatory work on understanding the impact of the changes on investment strategies. Default life-styling approaches within DC schemes, for example, need careful consideration.

This planning phase is complicated not only because of the uncertainty in terms of the detail, but also uncertainty arising through a lack of knowledge as to how many members will actually seek to take advantage of the flexibility on offer. Estimates as to how many members will seek to take their benefits as cash taxed at their marginal rate vary widely. Until data based on first hand experience is available, we are alive to the knowledge that our planning is merely based on assumptions. At times the whole process seems akin to completing a jigsaw puzzle when you have a few of the pieces missing, and you don't know what the picture looks like. This at a time when we have only recently reached a steady state following work relating to the DC Code of Practice...

We acknowledge that with clear communication, good processes and strong governance there could be a great amount of appeal to the flexibilities on offer. However, there is also the danger that the industry doesn't get it right, especially in terms of communication. If getting their hands on pension cash early ultimately strips them of value, members will not see these changes as a positive and as a long-term consequence engagement could decline.

Successfully guiding our schemes' members through these changes is looking like the biggest challenge that we will face this year and for many more to come.

Adrian Kennett
Director
Dalriada Trustees
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