Trustee Accelerator Programme, Unit 4
5 March 2025

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Topics

- Scheme Design
- DC contributions
- Decumulations for DC schemes
- DC fund range
- Default fund design
- De risking options
- Unitised funds
- Chair's Statement

Summary

The presenter emphasised the importance of understanding acronyms and industry terminology, ensuring participants could ask questions as they arose. Key topics included DC scheme design, contribution structures, and the importance of individual fund management. The distinction between defined benefit and defined contribution schemes was clarified, highlighting that in DC schemes, only the contributions are guaranteed, not the eventual benefits. Factors influencing the size of the retirement pot were discussed, including contribution amounts, investment returns, and the impact of inflation.

Two main types of DC schemes were identified: trust-based and contract-based, each with its own regulatory framework and operational structures. The meeting highlighted the advantages of Master Trust schemes in terms of centralised governance and economies of scale, especially for small employers with limited experience in pension management. The discussion also touched on the declining popularity of Small Self-Administered Schemes (SSAS) and the implications of tax relief in pension contributions, noting the differences between net pay and relief at source arrangements. The need for clarity around contribution rates and the potential for employers to enhance employee contributions beyond the statutory minimum was stressed. The first half of this session concluded with a brief overview of upcoming topics, including post-retirement issues.

Key Points

Introduction to the Trustee Accelerator Program

The speaker introduced the Trustee Accelerator Program, specifically Unit Four, they outlined the structure of the session, indicating that they would keep it succinct and encouraged participants to engage by asking questions throughout.

Defined Contribution (DC) Schemes Explained

The discussion shifted towards an explanation of Defined Contribution (DC) schemes, contrasting them with Defined Benefit (DB) schemes. The key distinction highlighted was that in DC schemes, the contributions made are defined, but the eventual retirement benefits depend on investment performance and the amount contributed over time. The speaker emphasised the importance of understanding the individual nature of DC funds and how various factors influence the size of the retirement pot.

Contribution Factors and Investment Returns

Five main factors influencing the size of the retirement pot in a DC scheme were discussed, including the amount contributed, the time before retirement, and the returns on investments. The speaker elaborated on the benefits of starting contributions early and the compounding effect of investment returns. They also noted the impact of fees and inflation, outlining how these could erode the value of pension savings if not properly managed.

Types of DC Pension Schemes

Different types of DC pension schemes were outlined, including trust-based schemes governed by trustees and contract-based schemes typically operated by insurance providers. The implications of each structure on asset ownership and regulatory oversight were discussed. Master trusts, collective schemes, and small self-administered schemes (SSAS) were also explained, highlighting the evolution of these schemes in response to regulatory changes and industry needs.

Salary Sacrifice and Tax Relief Mechanisms

The meeting discussed the mechanism of salary sacrifice and its implications for pension contributions and tax relief. The concept of salary sacrifice was explained as a method where employee contributions are deducted before tax, effectively increasing the value of pension contributions without impacting take-home pay. The discussion also touched on different types of tax relief available, including net pay arrangements and relief at source, each having distinct administrative and financial implications for employers and employees.

Questions

Question	Description	Answered?	Answer Summary
What are the factors influencing the size of a pension pot at retirement?	The speaker is looking to understand the various factors that can affect the value of a pension pot when members retire, specifically regarding contributions, time, and investment returns.	yes	The factors mentioned include the amount and regularity of contributions, the time invested before retirement, and the investment returns.
Can you explain the differences in investment options between trust-based and contract-based schemes?	A participant seeks clarification on whether the investment opportunities differ between trust-based and contract-based pension schemes, particularly in terms of asset classes and permitted investments.	yes	It was clarified that both types of schemes generally have a broad range of asset classes available, though there are exceptions for certain schemes.

What distinguishes defined contribution schemes in terms of investment risk?	The speaker is summarising the differences between defined benefit and defined contribution schemes, focusing on who bears the investment risk.	yes	It was explained that in defined contribution schemes, the investment risk is entirely borne by the members, whereas in defined benefit schemes, the sponsor bears the risk.
What are the contribution structures in trust-based and contract-based schemes?	The speaker is explaining how contribution rates and structures differ between trust-based and contract-based pension schemes, emphasizing the legal and regulatory aspects.	yes	The speaker outlined that contribution rates in trust-based schemes are defined in the scheme rules, while in contract-based schemes, they are part of the employment contract.
What are the benefits and implications of salary sacrifice for employers and employees?	The speaker discusses the concept of salary sacrifice, its mechanism, and its potential benefits for both employers and employees regarding tax contributions.	yes	The benefits of salary sacrifice include tax savings for both parties, although it can be administratively burdensome for employers.
What are the differences in tax relief mechanisms	The speaker is explaining the differences in how tax relief is applied	yes	The differences were explained: in net pay schemes, tax relief is given at

between net pay and relief at source schemes?	in net pay and relief at source schemes, detailing the implications for employees.		the point of contribution, while relief at source requires employees to claim additional relief if they are higher earners.
Does the amount of salary sacrificed impact tax calculations for employees?	A participant enquires about whether choosing not to use salary sacrifice could lead to disadvantages for both the employer and the employee when it comes to tax contributions.	yes	It was discussed that while not using salary sacrifice could mean losing out on tax savings, it also creates administrative burdens for employers.

Part 2

Summary

The meeting continued with an introduction to the concept of decumulation, explaining it as the process of withdrawing money from a pension, contrasting it with the accumulation phase where individuals save and contribute to their pension schemes. It outlined various decumulation options available under defined contribution schemes, referencing the Pensions Act of 2014, which introduced significant changes to how individuals access their retirement savings. Three main options were discussed: annuitisation, flexi-access drawdown, and uncrystallised funds pension lump sum (UFPLS). This prompted a discussion on the implications of choosing an annuity, highlighting its advantages of guaranteed income, yet noting the associated risks, particularly regarding longevity and lack of flexibility. Participants raised questions concerning tax implications, with clarifications provided on the one-off nature of tax-free cash withdrawal limits.

The conversation underscored the importance of setting sustainable withdrawal rates in flexi-access drawdown to avoid depleting funds prematurely. Additionally, the topic of inheritance tax was touched upon with revisions expected in upcoming years. The discussion also included the different investment strategies within pension schemes and emphasised the distinction between active and passive fund management. The role of trustees in overseeing investment performance and ensuring value for money was highlighted, alongside the significance of default fund design to accommodate the majority of pension scheme members. Towards the end, information regarding upcoming examinations for pension trusteeship was shared, alongside resources for preparation. Participants were encouraged to reach out with further questions, ensuring a supportive environment for those preparing for their assessments.

Key Points

Understanding Decumulation

The meeting began with an introduction to the concept of decumulation, which refers to the phase where individuals withdraw money from their pension pots after retirement. The speaker explained the difference between accumulation (saving into a pension) and decumulation (withdrawing from a pension). There are various options available for decumulation, which emerged from the Pensions Act of 2014, and members can combine these options based on their needs. The speaker emphasised the importance of understanding these decumulation options for effective retirement planning.

Decumulation Options and Annuities

The discussion included an in-depth look at three main decumulation options: annuitisation, flexi-access drawdown, and uncrystallised funds pension lump sum (UFPLS). Annuities were highlighted as a traditional option that provides income for life, though they have become less popular since the introduction of pension freedoms in 2015, allowing more flexibility. The speaker also explained the unique aspects of annuities, such as their role in hedging longevity risk and the absence of a payout upon death if the individual dies shortly after retirement.

Flexi-Access Drawdown Risks

Flexi-access drawdown allows retirees to withdraw money from their pension pots without a set payment structure, providing them with more control over their finances. However, this flexibility comes with significant risks, including the potential for running out of money if withdrawal rates are set too high. The speaker stressed the importance of selecting a sustainable withdrawal rate, generally recommended around 4%, to maintain the longevity of the retirement fund.

Tax Implications and UFPLS

The meeting covered the tax implications associated with pension withdrawals, particularly highlighting that the first 25% can be taken tax-free. The speaker clarified that UFPLS allows retirees to withdraw money in an ad-hoc manner, which could supplement their income while maintaining flexibility. The tax treatment of these withdrawals is critical, as any amount exceeding the tax-free limit will be taxed at the individual's marginal rate, which can be a significant consideration for retirees.

Investment Strategies in Pension Schemes

The final part of the meeting focused on investment strategies within defined contribution pension schemes, discussing concepts like unit-linked funds and the blend of asset classes used in investments. The speaker explained the difference between active and passive management strategies and their implications for performance. The governance responsibilities of trustees were highlighted, particularly in overseeing investment performance and ensuring value for money for members, which is essential for the long-term sustainability of pension funds.

Questions

Question	Description	Answered?	Answer Summary
Is the lump sum tax-free restriction an annual restriction or a one-off?	A participant seeks clarification on the nature of the tax-free lump sum withdrawal from pension funds, asking if this regulation applies annually or is limited to a one-time opportunity when first accessing their pension.	yes	The response clarified that the tax-free lump sum is a one-off based on the value of the fund at the time of first withdrawal.
Does the guaranteed annual income from an annuity link to inflation?	A participant wants to understand whether the income received from purchasing an annuity will be adjusted for inflation or if it remains fixed,	yes	The discussion confirmed that while annuities can have options for inflation linkage, the basic example provided was

	highlighting a concern about the long-term buying power of the annuity payments.		a fixed income without inflation adjustments.
How do pension firms manage longevity risk for long-living retirees?	A participant is seeking to understand how pension firms mitigate the financial risks associated with retirees who might live significantly longer than average, which could impact the sustainability of their pension fund.	yes	The answer highlighted the importance of setting sustainable withdrawal rates and the use of conservative investment strategies to ensure funds last throughout retirement.
Is it the trustee's responsibility to ensure active fund managers outperform their fees?	A participant questions whether trustees are accountable for ensuring that the costs associated with active fund management are justified by the performance of those funds, thus ensuring value for money for the pension scheme members.	yes	The response explained that while trustees have a fiduciary responsibility to monitor fund performance and fees, they rely on investment advisors to guide their decisions.