**Core Unit 2 – Regulation of Retirement Provision**

**Mock Examination Notes**

*Recommended Time: 2 hours 30 minutes*

# One of the three main aspects of the Pension Regulator’s anti-avoidance regime is TPR’s power to issue contribution notices. Explain when a contribution might be issued, the implications for employers and when TPR would use a “material test”.

**15 marks**

Answer should cover:

*Contribution notices (10 marks):*

* Pensions Act 2004 - TPR has power to issue a contribution notice against a “person” ;
* can be sponsoring employer, companies or individuals “connected or associated” with sponsoring employer;
* person within the previous 6 years has been party to an act or deliberate failure to act (or a series of acts or failures to act):
  + main purpose, or one of the main purposes of which, was (broadly) to avoid or reduce the amount of a section 75 debt which was, or which may have become, due to a defined benefit occupational pension scheme (which occurred on or after 27 April 2004), or
  + where TPR considers that the act or failure to act has “detrimentally affected in a material way the likelihood of accrued scheme benefits being received” from a defined benefit occupational pension scheme (which occurred on or after 14 April 2008);
* contribution notice may only be issued where TPR considers it is reasonable to do so;
* before any transaction involving a DB scheme takes place, parties need to consider the impact of the transaction on the scheme - if the pension scheme will suffer a material detriment the parties should consider requesting clearance from TPR and the need to mitigate the detrimental impact on the scheme;
* potential recipients of a contribution notice can also seek clearance from TPR in the usual way before proceeding with a transaction;
* statutory defense against a contribution notice being issued under the ‘material detriment’ power;
* where a contribution notice is issued by TPR, recipient required to pay a contribution to the relevant scheme, which may (depending on the circumstances) be up to the full amount of the scheme’s buy-out deficit.

*Material detriment test (5 marks)*

* the transfer of a scheme out of the UK;
* the transfer of a sponsoring employer out of the UK or the replacement of a sponsoring employer with

an entity that does not fall within the UK;

* sponsor support being removed, substantially reduced or becoming nominal;
* the transfer of the liabilities of a scheme to another pension scheme or arrangement which leads to a

significant reduction of sponsor support in respect of those liabilities or funding to cover those liabilities;

* a business model or the operation of a scheme which creates from a scheme, or which is designed to

do so, a financial benefit for the employer or some other person.

(Relevant section of the manual is Part 4 Chapter 1.8.2)

# List the Financial Conduct Authority’s Principles of Good Regulation.

**5 marks**

Answer should include 5 from the following:

* Efficiency and economy (FCA must use its resources efficiently and economically);
* Proportionality (any burden or restriction that imposed on a person or activity must be proportionate to the expected benefits, taking into account the costs to firms and consumers).
* Consumer responsibility (consumers should take responsibility for their decisions);
* Senior management responsibility (a regulated firm’s senior management is deemed responsible for that firm’s activities and is held responsible for the risk management and controls within the firm);
* Openness and disclosure (FCA should ensure that relevant market information about regulated persons is published, to reinforce market discipline and improve consumers’ knowledge about their financial matters);
* Transparency (FCA should exercise its functions as transparently as possible).

(Relevant section of the manual is Part 1 Chapter 3.5.1)

# In relation to defined contribution scheme investments list the key governance requirements for trustees set out in the Occupational Pension Schemes (Charges and Governance) Regulations 2015, and the content that must be included in the annual Chair’s statement.

**10 marks**

Answer should include:

*Key governance requirements – any 5 of the following (5 marks)*:

* core financial transactions must be processed promptly and accurately;
* the value of costs and charges borne by members must be assessed;
* a statement of investment principles governing decisions about investments for the purposes of the

default arrangement must be prepared;

* default arrangements must be designed in the members’ interests and kept under regular review;
* the scheme deed and rules must not restrict the choice of administrators, fund managers or advisers to

the scheme;

* a chair of trustees (the Chair) must be appointed with responsibility for signing off an annual statement

describing how the governance requirements have been met.

*Chairs statement - any 5 of the following (5 marks)*:

* latest statement of default investment strategy;
* details of any review of the default strategy and resulting changes (or if no review, date the last review took place);
* description of how the requirements in relation to core scheme financial transactions have been met;
* report on charge levels in default funds and the range of charges in other funds and whether they deliver value to members;
* report on transaction costs, or an explanation of why they have not been able to obtain them and an assessment of the value they represent;
* assessment of how the combined knowledge and understanding of the trustees, together with advice available, enables them properly to exercise their functions.

(Relevant section of the manual is Part 5 Chapter 1.1.5)

# Describe why the Pensions Regulator has issued guidance on record keeping, outlining how the guidance categorises data and the trustee/manager duties relating to good record keeping.

**10 marks**

Answer should include:

* Poor record keeping in schemes can result in significant costs in areas such as administration, buy-outs and wind- ups, including error correction and claims from members (not to mention reputational damage);
* To address this issue, TPR published detailed regulatory guidance in 2010 aimed at trustees, providers and administrators on the testing and measurement of member data;
* TPR guidance categorises the data into three types:
* Common Data — data necessary and applicable to all members of all schemes;
  + absence is likely to mean member cannot be identified or traced, or their benefits calculated with any degree of certainty (for example name, date of birth, sex, address, membership status);
* *Conditional Data* — scheme specific, varying from scheme to scheme;
  + will depend on many factors including scheme type and design, member’s status in the scheme, system design and events that have occurred during their membership of the scheme.
* *Numerical Data* — numerical information regarding members’ records;
  + will help put the results of other measures into perspective.
* Trustees/managers should ensure that a data review exercise is carried out at least once a year;
* Review is an assessment of the accuracy and completeness of the above types of data;
* data improvement plan must be out in place to address poor quality data;
* such a plan should have a defined end date within a reasonable timeframe.

(Relevant section of the manual is Part 5 Chapter 1.8.1)

# Under trust law, pension scheme trustees have an overarching duty to administer the pension scheme in accordance with the primary purpose for which the scheme was established (i.e., to secure the benefits).

# Explain the overarching duty of a pension scheme trustee, and five of the additional, more specific duties pension scheme trustees have under trust law.

**20 marks**

Answer should include any 5 of the following:

*Overarching duty* *(10 marks)*:

* often described as “a duty to act in the best interests of the members of their scheme”;
* refined by the High Court in the Merchant Navy Ratings case to be a duty to administer the pension scheme in accordance with the primary purpose for which the scheme was established;
* purpose of the trust is and the benefits the beneficiaries are intended to receive before being in a position to decide whether a proposed course is for the benefit of beneficiaries or in their best interests;
* the beneficiaries of a trust should be identifiable from the trust deed. In the context of a pension scheme;
* the beneficiaries will normally include:
  + the active, deferred and pensioner members of the pension scheme;
  + the spouses, civil partners, and dependents of those members;
  + the scheme’s sponsoring employer (certainly for a DB scheme).
* sponsoring employer of a defined benefit pension scheme could also be regarded as a beneficiary of the scheme, on the basis that the sponsoring employer will be responsible for making up any shortfall in the scheme’s funding position and because (under most schemes) the sponsoring employer would be among the list of potential recipients of any surplus on the winding-up of the scheme;
* purpose of a defined benefit occupational pension scheme has been identified as being “to provide the stated and accrued benefits to (and in respect of) the members at a cost acceptable to the employer”;
* this reiterates the need for trustees to take account of the employer’s interests and, in particular, the cost to the employer of operating the scheme as well as seeking to ensure that members’ accrued benefits are paid in full.

*Additional duties – any 5 of the following with a short description of each (10 marks)*:

* Duty to act in accordance with the trust deed: - a trustee must act in accordance with the provisions of the trust deed, except insofar as those provisions are modified by the consent of all beneficiaries, overriding legislation or by the Court;
* Duty to act impartially: - a trustee must be impartial in the execution of the trust and must consider the interests of all of the beneficiaries (and of the different classes of beneficiary) when making decisions in respect of the trust;
* Duty to exercise reasonable skill and care: - lay trustees should use such skill and care in the management of the trust as men of ordinary prudence and vigilance would use in the management of the affairs of a third party for whom they felt morally bound to provide;
* Duty to act without charge: - as a general rule a trustee must not delegate his duties or powers or the receipt of trust monies to a co-trustee or to a third party unless authorised by the trust deed or by statute.;
* Duty to act jointly: - in the case of a non-charitable trust (such as a pension scheme) if there is more than one trustee all must act together in the management of the trust, with some exceptions;
* Duty not to profit from trust property: - trustees must not use or deal with trust property for their own private advantage or they will be personally liable to account for their profits;
* Duty to prepare and disclose accounts: - a trustee must keep clear and accurate accounts of the trust property, and, at all reasonable times, at the request of a beneficiary, disclose full and accurate information as to the amount and state of the trust property, and permit the beneficiary or his solicitor to inspect the accounts and other documents relating to the trust property.

(Relevant section of the manual is Part 2 Chapter 2.7.1)

# In relation to the Proceeds of Crime Act (POCA), outline the two important features of money laundering offences and the three main money laundering offences.

**5 marks**

Answer should cover:

* Features:
  + the offences involve some dealing in “criminal property” - broadly defined to include any funds that constitute a person’s benefit from criminal conduct or represent, even indirectly, such a benefit;
  + there is no requirement for actual knowledge of another’s wrongdoing - suspicion is enough;
* Offences:
  + It is an offence to conceal, disguise, convert or transfer criminal property.
  + It is an offence to enter into or become concerned in an arrangement if you know or suspect this

facilitates, by whatever means, the acquisition, retention, use or control of criminal property by or on

behalf of another person. Arguably this may present the most risk for those in the pensions industry.

* + It can be an offence to acquire, use or simply possess tainted funds.

(Relevant section of the manual is Part 3 Chapter 1.6)

# In relation to the Data Protection Act 2018, list the notification requirements of data controllers and outline the key considerations surrounding the disclosure of personal data.

**15 marks**

Answer should cover:

*Notification requirements (5 marks)*:

* Data controllers who process personal data must submit an annual notification to ICO;
* Some exemptions – must be recognised by ICO as exempt;
* Failure to notify is a criminal offence;
* ICO uses the details notified by the data controller to make an entry describing the processing in the register of data controllers (available to the public for inspection);
* The information which data controllers must notify to the ICO includes:
  + a description of the personal data that is being processed;
  + a description of the category or categories of data subject in respect of whom personal data is being processed;
  + the purposes for which the data is being processed; and
  + any person to whom the data needs to be disclosed.

*Disclosure (10 marks):*

* Confidentiality is very important;
* The information normally found within pension scheme records is extensive and should not, under any circumstances, be disclosed to any individual or body that does not have the right to access it;
* Disclosure of personal data can occur in a number of ways:
  + by word of mouth;
  + by printed matter; or
  + by visual display (e.g., computer terminal screen).
* Data controller must take adequate steps to ensure that data is kept securely and is only disclosed to appropriate persons for the purpose that was notified to ICO;
* Failure to ensure the confidentiality of data carries a penalty;
* ICO can impose a penalty of up to the greater of 4% of annual worldwide turnover or €20 million on a data controller where one or more of the data protection principles have been seriously contravened provided that the contravention is likely to cause substantial damage or distress;
* The penalty may only be imposed where the breach is deliberate or where the data controller must or might have known that there was a risk of contravention but failed to take reasonable steps to prevent it;
* If unlawful disclosure occurs, and the data controller cannot demonstrate that reasonable security measures have been taken, the data controller may lose its registration;
* Particular care needs to be taken with sensitive personal information (such as medical records or reports), which should not be disclosed to anybody without the relevant individual’s express consent.

(Relevant sections of the manual are Part 3 Chapter 1.1.2 and 1.1.4)

# What are “authorised payments”, and what tax charges “unauthorised payments” attract?

**10 marks**

Answer should cover:

* Finance Act 2004 prescribes certain payment that can be made without a tax charge (over and above normal Income Tax on pensions);
* Types of authorised payments:
  + pensions and pension death benefits;
  + lump sums and lump sum death benefits;
  + transfers to other registered pension arrangements or to a ‘qualifying recognised overseas pension

scheme’ (QROPS);

* + certain ‘scheme administration’ payments;
  + payments pursuant to a pension sharing order.
* Unauthorised payments can generate up to four tax charges:
  + Unauthorised payments charge — a tax charge at a rate of 40%, based on the value of the

unauthorised payment;

* + Unauthorised payments surcharge — where 25% or more of the value of a member’s benefits is paid out in the form of an unauthorised payment an additional tax charge at a rate of 15% will be due, based on the value of the unauthorised payment;
  + Scheme sanction charge — a tax charge on the Scheme Administrator. The scheme sanction charge

is due on most unauthorised payments and the tax rate is normally 15% of the value of the payment, but this increases to 40% if HMRC have been unable to recover the unauthorised payments charge from the recipient;

* + Deregistration charge (rare) — if a scheme pays out more than 25% of its assets in the form

of unauthorised payments in any year then it may have its registration withdrawn and a

deregistration charge will be applied equal to 40% of the value of the scheme’s assets.

(Relevant section of the manual is Part 1 Chapter 1.5 and 1.5.1)

# In relation to the cessation of contracting out, outline how the increase in National Insurance Contributions (NICs) can be recovered by an employer.

**10 marks**

Answer should cover:

* Some employers have provisions in their scheme rules to enable them to amend their schemes to recover
* this additional cost:
* Others will be prevented from making such changes by their scheme rules or by the requirement for trustee consent for such changes, or both of these;
* Statutory override:
  + Pensions Act 2014 S24(2) gives employers sponsoring CORS schemes power to amend scheme rules to adjust for the increased NIC liability;
  + Changes may be made either to increase employee contributions or reduce the future accrual of benefits in respect of the scheme members;
  + Actuarial certificate required to reduce future accrual;
  + Extent to which employer can amend the scheme rules using the statutory override limited to that estimated as matching the amount of increase in the employer’s NICs;
  + Applies regardless of scheme rules and trustee consent not required;
* New Regulations:
  + The Occupational Pension Schemes (Power to Amend Schemes to Reflect Abolition of Contracting out) Regulations 2015, effective 6 April 2015;
  + The Occupational Pension Schemes (Schemes that were Contracted-out) Regulations, effective 6 April 2016;
* Most employers will seek to offset the extra cost or implement wider scheme changes to reduce scheme costs.

(Relevant section of the manual is Part 6 Chapter 1.2.1)