

PENSION SCHEMES ACT 2015

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 3 – General Changes to Pensions Legislation about Pension Schemes

Section 36: Pensions promise obtained from third party

101. This section relates to the possibility of a pensions promise, for the purposes of a defined benefits or shared risk scheme being obtained from a third party (as set out in section 5). It contains a power to enable the Secretary of State to make regulations to require that trustees or managers of a scheme must not obtain any such promise from a third party unless conditions set out in the regulations are met. Regulations under this section may also provide for civil penalties to apply to a person who fails to comply with them. This section also makes changes to section 34(7) of the Pensions Act 1995 to add this section to the list of provisions that section 34, which makes its own provisions in relation to trustees' power of investment, cannot override.

Section 37: Duty to act in the best interests of members

102. Regulations under this section may require managers in non-trust based schemes to act in members' best interests when taking certain specified decisions. This duty may apply in relation to shared risk schemes and schemes offering collective benefits.
103. Regulations may provide for the duty to override obligations that are inconsistent with that duty, but do not otherwise affect any other duty that might arise. Where a manager has breached or threatened to breach such regulations to act in members' best interests, regulations may provide that the manager will be subject to the same consequences as the consequences of breaching a fiduciary duty to the members.

Section 38: Disclosure of information about schemes

104. Section 113 of the Pension Schemes Act 1993 sets out a power for the Secretary of State to make regulations in relation to occupational and personal pension schemes, setting out requirements to keep certain persons informed of various matters including the scheme's constitution, its administration and finances, and the rights and obligations that may arise under the scheme.
105. This section amends section 113, removing the list at subsection (2) of the persons who can be kept informed under provisions of the regulations, and instead specifying that it applies in respect of 'persons of prescribed descriptions' – that is, the persons who should be kept informed will be set out in secondary legislation.
106. The section also introduces a requirement for schemes to have regard to any guidance prepared by the Secretary of State when complying with disclosure requirements.

Section 39: Extension of preservation of benefit under occupational pension schemes

107. This section amends Part 4 of the Pension Schemes Act 1993, which concerns the preservation of benefit for early leavers of occupational pension schemes. Pension scheme members whose pensionable service is terminated before reaching normal pension age are entitled to payment of the benefit accrued up to that point, providing they have two years' qualifying service or have previously transferred their rights into the scheme from a personal pension. (Members who leave without a preserved benefit are entitled to transfer the value of the benefits they have accrued or receive a refund of their own contributions.)
108. The preserved benefit to which such members are entitled – termed 'short service benefit' – is the same as that which would have been payable if they had remained members in pensionable service in the scheme until retirement.
109. The Pensions Act 2014 introduced a requirement that, where all benefits for a member are money purchase benefits, a preserved pension must be provided after 30 days' qualifying service.
110. **Section 39** amends section 71 of the Pension Schemes Act 1993 so that schemes must provide a short service benefit where leavers have at least 30 days' qualifying service and all the pension benefit is a non-salary related one (that is, not calculated either by rate or amount with reference to the member's salary) or where it is a collective benefit. If any of the pension benefit is salary related, the two year rule still applies.
111. Where a benefit may be calculated on a salary related basis in some circumstances and a non-salary related basis in others (e.g. an underpin benefit which pays the higher of the two calculations), it will be treated as salary-related for these purposes.
112. If a member's pensionable service began before the amendments came into force, the previous requirements for preservation of benefits will continue to apply.
113. The section also ensures the uniform accrual rules do not apply in respect of collective benefits.

Section 40: Revaluation of accrued benefits

Schedule 1: Early leavers: revaluation of accrued benefits

114. When a member stops being an active member of a scheme more than a year prior to retirement, the accrued benefits are required to be 'revalued' at the scheme's normal pension age to provide a measure of inflation protection over the period of deferral. Sections 83 to 86 of, and Schedule 3 to, the Pension Schemes Act 1993 set out the procedure for revaluation based on benefit type.
115. The existing section 84 of the Pensions Schemes Act 1993 takes the final salary method as its default method of revaluation for accrued benefits. This method requires benefits to be increased by inflation capped at 5 or 2.5 per cent each year, but there is an alternative for average salary, flat rate or money purchase benefits. In these cases, the legislation allows for revaluation using the average salary and flat rate methods, where trustees or managers consider these methods, respectively, to be more appropriate than the final salary method, and the money purchase method where benefits are money purchase or benefits from a personal pension scheme.
116. The basic principle behind the non-final salary provisions is that both active scheme members and those who have left the scheme before normal pension age should be treated in the same way. Their rights in relation to accrued benefits should not be affected because they have, for example, changed their place of employment and consequently left that pension scheme.

117. The methods are set out in Schedule 3 to the 1993 Act. For the final salary method, the annual Occupational Pensions (Revaluation) Order sets out the percentages to be used for people retiring during the following year. The average salary and flat rate methods state that benefits are to be revalued in the same way as they would have been had the member remained in pensionable service. In the money purchase method the requirement is to apply the same investment return on the accrued benefits to both active and deferred members.
118. The Pensions Act 2011 (Consequential and Supplementary Provisions) Regulations 2014 amended the 1993 Act to introduce an additional cash balance method for cash balance benefits not calculated by reference to final salary which accrued after section 29 of the Pensions Act 2011 was commenced. This also required active and deferred members to be treated in the same way.
119. [Schedule 1](#) amends the Pension Schemes Act 1993. There will be no changes to the method applicable for benefits which accrued before the changes come into force or for relevant pension credits rights where entitlement arose before the changes come into force. A new ‘default method’ will apply for all benefits except those which are money purchase, salary related or flat rate. (‘Salary related’ will include final salary cash balance schemes). The default is simply to revalue benefits as they would have been had the member remained in pensionable service.
120. The exceptions for the default method remain money purchase benefits, flat rate benefits and what are now termed ‘salary related’ benefits. A salary related benefit must be revalued using the final salary method except where those benefits are average salary and trustees or managers consider the average salary method more appropriate. Money purchase benefits should be revalued using the money purchase method. These methods continue to apply the definitions set out in Schedule 3 to the 1993 Act where referenced.
121. Collective benefits will be revalued using the default method.
122. The Schedule (see new section 84D) also sets out the revaluation procedure for hybrid benefits – those benefits which are made up of different components, the highest of which is paid. In this case, each component will be revalued separately before deciding which is the highest. This replicates the effect of provision currently contained in secondary legislation. At new section 84E there is provision for schemes which have used certain alternative methods of revaluation (primarily public service pension schemes) to continue to do so.
123. There is also a power (at new section 85A) to add revaluation methods for personal pension schemes. This is to allow for the possibility that in the future the design of personal pensions introduces a wider range of benefits than are provided for by the new provisions.

Section 41: Collective benefits exempt from indexation

Section 42: Regulatory own fund schemes exempt from indexation

Section 43: Power to create other exemptions from indexation

124. The Pensions Act 1995 makes provision for the indexation of pensions under occupational pension schemes (other than public service pension schemes). Section 41 excludes collective benefits from the requirement to annually increase pensions in payment set out in section 51 of the 1995 Act.
125. [Section 42](#) amends the provision in section 51 of the Pensions Act 1995 to ensure schemes set up as “Regulatory Own Funds” will be exempt from requirements to index benefits. This is as it may not always be appropriate for such schemes to index the benefits offered. Section 42(3) introduces a definition of a Regulatory Own Fund which refers directly to Article 17 of European Council Directive ([2003/41/EC](#)).

126. [Section 43](#) amends section 51 of the Pensions Act 1995 to insert a regulation making power that may disapply the requirement to annually increase pensions in payment to a pension or part of a pension of a specified description. The power cannot be used to remove the requirement to index pensions that came into payment or parts of pension attributable to pensionable service that has occurred before the day on which regulations come into force, or to a pension or any part of a pension under a defined benefits scheme. The regulations will therefore not be able to affect rights already accrued or benefits under a defined benefits scheme.

Section 44: Removal of requirement to maintain register of independent trustees

127. This section removes the statutory requirement for regulations to provide that the Pensions Regulator compile and maintain a register of trustees (the relevant regulations are the [Occupational Pension Schemes \(Independent Trustee\) Regulations SI 2005/703](#)).
128. Section 23 of the Pensions Act 1995 allows the Pensions Regulator to appoint an independent trustee to a scheme whose employer has suffered an insolvency event. The Regulator can only appoint a trustee from the trustee register, which it must establish and maintain. But the Regulator has another, general power (under section 7 of the Act) to appoint trustees to replace a person found not to be ‘fit and proper’ to be a trustee. In relation to this there is no requirement to appoint from a register of trustees. Section 44 of the Pension Schemes Act 2015 removes the requirement to maintain a register of trustees under section 23 of the 1995 Act, in order that the Regulator can instead follow the same procedure as when appointing trustees under section 7 of the 1995 Act.

Section 45: Rules about modification of schemes

129. Section 67 of the Pensions Act 1995 contains provisions to protect members against detrimental modifications to their ‘subsisting rights’ – that is, ‘any right which at that time has accrued to or in respect of the member to future benefits under the scheme rules; or any entitlement to the present payment of a pension or other benefit which the member has at that time, under the scheme rules’.
130. Section 45 of the Pension Schemes Act 2015 replaces the existing regulation making power to disapply section 67 of the 1995 Act for the exercise of a power in a prescribed manner and replaces it with a power to disapply in prescribed cases.
131. Modifications can only be made if the value of the benefits is the same before and after the change or if the member agrees. Some changes can only be made if the member agrees: these are called ‘protected modifications’. Section 67A of the 1995 Act sets out the circumstances in which a modification to members’ rights is a ‘protected modification’.
132. Currently, section 67A states that a change is a ‘protected modification’ where money purchase benefits would replace non-money purchase benefits, or where the change would result in a reduction to a pension in payment.
133. [Section 45](#) of this Act amends section 67A of the 1995 Act to include a modification where a right to benefits that include a pensions promise is to be replaced by a right to benefits where there is no pensions promise, where a right to a retirement income in respect of which there is a pension promise becomes a right to benefits other than retirement income and where a right or entitlement to a benefit which is not a collective benefit is replaced with a right or entitlement to collective benefits.
134. [Section 45](#) of this Act also amends section 67A of the 1995 Act to provide that a reduction to a collective benefit in payment is not a “protected modification”.
135. It also updates the list of relevant override provisions in section 67A of the 1995 Act to include regulations made under Part 2 of this Act and regulations made under Schedules 17 and 18 to the Pensions Act 2014. This means where these regulations override

conflicting provision in the scheme rules, that the regulations are treated as part of the scheme rules for the purposes of the subsisting rights provisions.

Section 46: Other amendments to do with Parts 1 and 2

Schedule 2: Other amendments to do with Parts 1 and 2

136. **Schedule 2** makes consequential amendments to existing pensions legislation to take account of the categories of scheme defined in Part 1 and collective benefits defined in Part 2. The Schedule also makes some resulting changes to replace references to money purchase schemes to limit the number of ways of categorising schemes in legislation.
137. Where there are references in existing legislation to a ‘money purchase scheme’, these are generally replaced by references to ‘a scheme under which all the benefits that may be provided are money purchase benefits’. This does not change the effect of the legislation – rather, they are technical changes to limit the number of categories that can be attached to pension schemes.
138. In other cases, the new categories are themselves substituted for existing definitions.

Pension Schemes Act 1993

139. Section 124 of the Pension Schemes Act 1993 places a duty on the Secretary of State to pay unpaid contributions to schemes in the event of employer insolvency and consequent default on employer contributions. The amount the Secretary of State is required to pay is the least of three amounts set out in paragraphs (a) to (c) of subsection (3). Subsection (3A) states that where the scheme is a money purchase scheme, the amount is the lesser of the amounts specified in paragraphs (a) and (c) (paragraph (b) is not relevant to money purchase schemes). Schedule 2 of the Pension Schemes Act 2015 amends the wording to replace ‘money purchase scheme’ with ‘defined contributions scheme, or a shared risk scheme under which all of the benefits that may be provided are money purchase benefits’. The Schedule inserts a new subsection (3A) so that it also applies to a shared risk scheme under which all the benefits that may be provided are money purchase benefits or collective benefits. This updates the provision to ensure it applies in the right way to schemes which offer collective benefits and that they are covered by the appropriate provision, as well as ensuring all schemes which are shared risk and have only money purchase and collective benefits, and schemes which are defined contributions and provide a guaranteed income after the point of retirement, are captured.

Pensions Act 1995

140. Section 37 of the Pensions Act 1995 makes provision in relation to payments to employers when a trust-based occupational scheme is in surplus. Paragraph 7 of Schedule 2 of the Pension Schemes Act 2015 amends subsection (1A) of section 37 of the 1995 Act to disapply that section in relation to funds held for the purposes of collective benefits. Funds held for the purposes of providing collective benefits should only be used to provide those benefits except in very limited circumstances. Employer liability in respect of collective benefits is limited to the employer contributions and they cannot be required to make any additional payments where the funds are insufficient to meet the targets. Correspondingly, they should not, as a general rule, have a right to any surplus in the fund. Regulations made under section 24 of the 2015 Act will set out any exceptions to the rule that the funds must only be used for provision of collective benefits.
141. Sections 51 and 51A of the Pensions Act 1995 relate to indexation requirements for pension schemes (that is, the method by which pensions in payment are increased annually to take account of inflation). Schedule 2 of the Pension Schemes Act 2015 amends subsection (1)(a)(iii) of section 51 of the 1995 Act, which exempts pensions in money purchase schemes from indexation requirements in certain circumstances,

by substituting ‘defined contributions scheme’ for ‘money purchase scheme’. It consequently amends section 51A of the 1995 Act to replace ‘money purchase scheme’ with ‘defined contributions scheme’. This means that the indexation requirements exclude all defined contributions schemes, including money purchase schemes, schemes offering collective benefits, and those that are defined as self-annuitising under section 51A.

142. Section 73 of the Pensions Act 1995 deals with distribution of liabilities when an occupational pension scheme winds up. Paragraph 11 of Schedule 2 of the Pension Schemes Act 2015 amends subsection (2) of section 73 of the Pensions Act 1995 to reflect the new scheme categories found in Part 1 of the 2015 Act .
143. [Paragraph 11](#) applies the existing provisions on wind up to the new categories of defined benefits, shared risk and defined contributions schemes. The provisions on winding up do not apply to schemes under which all the benefits that may be provided are money purchase benefits or prescribed schemes or schemes of a prescribed description. This maintains the current position.
144. An ‘employer debt’ is a reference to a statutory debt arising under section 75 of the Pensions Act 1995. Section 75 of the Pensions Act 1995 applies to an occupational pension scheme (other than a scheme which is a money purchase scheme, or a prescribed scheme or a scheme of a prescribed description) where there is a funding deficit in circumstances where either the scheme is winding up or a prescribed event has occurred in relation to the employer.
145. Paragraph 12 of Schedule 2 to the Pension Schemes Act 2015 provides that section 75 of the 1995 Act will not apply to an occupational pension scheme which offers only collective benefits, money purchase benefits, or a combination of the two.
146. [Paragraph 12](#) also provides that where a scheme offers a combination of collective and non-collective benefits, the scheme is to be treated for the purposes of Part 1 of the Pensions Act 1995 as two separate schemes, with one scheme relating to the collective benefits and the other relating to the other benefits. Not all benefits in a defined contributions scheme will necessarily be money purchase – some or all may be collective benefits.
147. Sections 87 and 88 of the Pensions Act 1995 make provision requiring trustees or managers of occupational money purchase schemes to prepare schedules of payments for scheme members. Schedule 2 of the Pension Schemes Act 2015 amends this requirement so that it applies to all defined contribution schemes and any shared risk schemes under which either all of the benefits that may be provided are money purchase benefits, or a combination of money purchase and collective benefits. The wording of subsection (2)(a) of section 87 of the 1995 Act is altered to place focus on the type of benefits that are being offered, in order that ‘relevant benefits’ are considered regardless of whether a scheme is a defined contributions or a shared risk scheme
148. Section 124 of the Pensions Act 1995 is amended so that the terms ‘defined contributions scheme’, ‘defined benefits scheme’ and ‘shared risk scheme’, as set out in Part 1 of this Act, apply in that Act and to include a definition of “occupational” in relation to a defined benefits scheme, shared risk scheme or defined contributions scheme.

Welfare Reform and Pensions Act 1999

149. Section 38 of the Welfare Reform and Pensions Act 1999 makes provision about the treatment of pension credits in winding up. Currently it does not apply to a money purchase scheme. The amendment made by paragraph 19 of Schedule 2 replaces the reference to a money purchase scheme with a reference to a scheme under which all the benefits that may be provided are money purchase benefits. This does not change the effect.

Pensions Act 2004

150. Paragraphs 23 to 38 of Schedule 2 make amendments to the Pensions Act 2004. The majority of the amendments made to the Pensions Act 2004 by paragraphs 26 to 38 of Schedule 2 take out a number of references to money purchase schemes and update provisions in the 2004 Act to take account of the new pension scheme categories and the introduction of collective benefits. In most cases, the effect of the provisions is to extend exemption of the provision from schemes offering only money purchase benefits to schemes in which all benefits are collective or a combination of collective and money purchase. However, in paragraph 26 of Schedule 2 there is a further qualification – with the effect that the provision (which relates to freezing orders) does apply to schemes with only money purchase benefits which include a third party promise.
151. Paragraphs 24, 30, 33 and 36 of Schedule 2 also amend the definition of pensions legislation in sections 13, 90, 254 and 291 of the Pensions Act 2004 to include provisions in and made under the Pension Schemes Act 2015, ensuring that the Regulator can take action where there are breaches of the 2015 Act and regulations made under it and to allow for modification of the provisions where schemes receive contributions from a European employer.
152. Section 126 of the Pensions Act 2004 defines those occupational pension schemes which are eligible to be taken over by the Board of the Pension Protection Fund. Paragraph 31 of Schedule 2 amends the Pensions Act 2004 to include reference to the new categories of occupational pension scheme in Part 1 of the 2015 Act, (defined benefits, shared risk and defined contributions schemes) as eligible for the Pension Protection Fund. This paragraph also has the effect that occupational pension schemes that offer only money purchase and collective benefits, and occupational pension schemes that offer only collective benefits are not eligible for the Pension Protection Fund.
153. Section 318 of the Pensions Act 2004 defines terms used throughout that Act. Paragraph 38 of Schedule 2 to the Pension Schemes Act 2015 inserts the new scheme category and collective benefit definitions introduced by the 2015 Act and omits the definition of ‘money purchase scheme’. It also updates the list of overriding provisions contained in the definition of “scheme rules” in the Pensions Act 2004, to include regulations made under Part 2 of the 2015 Act, and under Schedule 17 and 18 to the Pensions Act 2014. This means that where these regulations override conflicting provision in the scheme rules the regulations are treated as part of the scheme rules for the purposes of the 2004 Act.

Pensions Act 2008

154. Sections 20 to 28 of the Pensions Act 2008 set out the requirements that a pension scheme must meet if it is to be a qualifying scheme for the purposes of meeting an employer’s enrolment duties under pensions legislation. (This is sometimes referred to as ‘automatic enrolment’.)
155. The amendments made by Schedule 2 to the Pension Schemes Act 2015 replace the existing definitions of ‘defined benefits scheme’, ‘money purchase scheme’ and ‘hybrid scheme’ in these sections with the new definitions set out in Part 1 of the 2015 Act, and change the section headings accordingly. The quality requirements are on the whole unchanged (except where stated).
156. Section 26 of the 2008 Act is amended to refer to a personal pension scheme ‘that is a defined contributions scheme’. The requirements are the same except it will no longer be a requirement that all benefits under the scheme must be money purchase benefits.
157. Section 99 of the 2008 Act is amended to substitute the definition of ‘defined benefits scheme’ and insert the definitions of ‘collective benefit’, ‘defined contributions scheme’ and ‘shared risk scheme’ as set out in Part 1 of the 2015 Act, as well as defining

*These notes refer to the Pension Schemes Act 2015
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‘occupational’ as it applies to these pension schemes. The original references to ‘defined benefits’, ‘money purchase scheme’ and ‘hybrid scheme’ are omitted.