EXPLANATORY MEMORANDUM TO

THE OCCUPATIONAL AND PERSONAL PENSION SCHEMES (CONDITIONS FOR TRANSFERS) REGULATIONS 2021

2021 No. 1237

1. Introduction

1.1 This explanatory memorandum has been prepared by the Department for Work and Pensions (DWP) and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument introduces new powers for trustees and managers of occupational and personal pension schemes to protect their members[1] from scams in the exercise of those members' statutory right to transfer pension benefits out of their scheme to another occupational or personal pension scheme. The statutory right to transfer accrued rights to benefits, or pension credit rights, to another pension scheme will only be able to be exercised by the member when one of the new conditions for transfers is met. These requirements will apply to statutory transfers from all occupational and personal pension schemes. They will apply to transfers initiated on or after 30th November 2021.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Extent and Territorial Application

4.1 The territorial extent of this instrument is Great Britain.

4.2 The territorial application of this instrument is Great Britain.

4.3 The Department for Communities will make corresponding legislation for Northern Ireland in line with the parity principle that applies to the United Kingdom pensions system.

5. European Convention on Human Rights

5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

6.1 The Pension Schemes Act 2021[2], section 125 (exercise of right to cash equivalent), inserts new subsections (6ZA) to (6ZC) into section 95 (ways of taking right to cash equivalent) and subsections (5A) to (5C) into section 101F (power to give transfer notice) of the Pension Schemes Act 1993[3] ("the 1993 Act"). Those sections provide

1 References to members of pension schemes in this document include reference to consumers in relation to personal pension schemes.
2 https://www.legislation.gov.uk/primary+secondary?title=pension%20schemes%20act%202021
3 https://www.legislation.gov.uk/ukpga/1993/48/contents

for the different ways in which trustees or managers of an occupational or personal pension scheme may, further to application or notice from the member of their scheme ("the transferring scheme"), use the cash equivalent value of, respectively, either the member's accrued rights to benefits, or pension credit rights, so as to make a transfer of that value into another occupational or personal pension scheme. New subsection (6ZA) and new subsection (5A) require the Secretary of State to prescribe conditions which must be met before a member will be able to exercise either of those statutory rights to transfer. New subsections (6ZB) and (5B) set out the nature of the conditions that may be set; new subsections (6ZC) and (5C) provide a power to require the trustees or managers of the member's scheme to notify the member of the prescribed conditions where the member is seeking to exercise those rights. Section 125 also makes amendments to sections 98 (loss of right to cash equivalent), 99 (trustees' duties after exercise of option) and 101J (time for compliance with transfer notice) of the 1993 Act, which are supplementary to the amendments of sections 95 and 101F of that Act.

6.2 These regulations provide a package of protection measures for members, giving trustees and managers of transferring schemes new powers to intervene in statutory transfers where there is a scam risk; whilst also ensuring that transfers to certain types of scheme can proceed without more than a check of the scheme type. These powers will enable trustees and managers of transferring schemes to prevent transfers where one or more of the indicators of high scam risk have been identified ("red flags"), or in other circumstances ("amber flags"), to mandate that the member take prescribed pension transfer scams guidance, from the Money and Pensions Service (MaPS), before the transfer can go ahead.

7. Policy background

What is being done and why?

7.1 An individual's statutory right to transfer their pension benefits to another pension scheme of their choice is extremely powerful in giving individuals control over their pension savings and supports the wider agenda of pensions freedom and choice. However, there have been instances where fraudsters have exploited that freedom to their advantage. Currently, trustees and managers of pension schemes have no power to prevent a transfer where they have concerns that it may be a scam, as the member can insist on the transfer proceeding.

7.2 Both the Pensions Regulator (TPR) and the Financial Conduct Authority (FCA) expect trustees and scheme managers will carry out effective due diligence[4] [5]before a transfer is processed and alert the member to any risks they identify. This due diligence is a legal requirement for trustees in as much as they must carry it out as part of their wider fiduciary duty to act in the best interests of the member. Personal pension scheme managers have a contractual obligation to act in their customers' best interests. The voluntary industry group, the Pension Scams Industry Group (PSIG), has also produced a Code of Good Practice[6] for combating pension transfer scams, which sets out robust due diligence processes for trustees and pension providers to follow, to help them identify pension scams.

4https://www.thepensionsregulator.gov.uk/en/pension-scams/carry-out-checks-on-pension-transfers
5https://www.handbook.fca.org.uk/handbook/PRIN/2/1.html
6 http://www.combatingpensionscams.org.uk

7.3 In addition, TPR and FCA have produced considerable guidance for the industry and pension savers on how to spot a pension scam, including the ScamSmart[7] website and associated advertising campaigns.

7.4 Despite this, people are still losing their life savings to scammers and there have been repeated calls from parliamentarians, industry, and consumer protection groups, for stronger measures to protect pension scheme members from potentially fraudulent transfers.

7.5 In December 2016, the Government consulted upon a package of measures aimed at tackling pensions scams, and in its 2017 Pension scams: consultation response[8], promised to implement a trio of consumer protection measures to help combat pension scams and protect savers, to:

- ban pensions cold calling,
- make it harder for fraudsters to open pension schemes; and
- limit the statutory right to transfer to some occupational pension schemes.

7.6 The first two commitments were introduced in 2019. The Finance Act 2018[9], created tighter scheme registration rules to make it harder for fraudsters to open new schemes. A ban on cold calling in relation to pensions, to help prevent fraudsters contacting individuals, was also introduced from January 2019.

7.7 These regulations deliver on the final commitment to limit the statutory right to transfer by creating conditions which must be satisfied before a transfer can take place, giving trustees and scheme managers power to take action where they have concerns about a transfer. They are intended to provide a safeguard against scams, whilst continuing to allow transfers to legitimate schemes to proceed without undue delay.

7.8 The new requirement to mandate proof of an employment link and a residency link delivers the policy set out in the 2017 consultation response. It was widely agreed by the majority of respondents to the consultation that such links would need to be established in order for the statutory right to be exercised to transfer to an occupational pension scheme or an overseas pension scheme. The addition of red and amber flags addresses the concerns raised during the passage of the Pension Schemes Bill that the methods being used by scammers have continued to evolve since the 2017 consultation response.

7.9 There was considerable interest in clause 125 of the Pension Schemes Bill 2019[10]. The clause, as originally drafted, sought to limit the statutory right to transfer to address concerns that scammers were exploiting those rights in order to steal members' pension savings. Those protections would be achieved by requiring the demonstration of an employment link, if transferring to an occupational pension scheme (OPS), or evidence of residency if transferring to a Qualifying Overseas Pension Scheme (QROPS). There was a total of ten amendments put forward between both Houses to this clause. The amendments put forward indicated both Houses felt that the clause did not go far enough to provide protection against the methods being used by scammers. Through discussions with Parliamentarians, the pensions industry and

7 https://www.fca.org.uk/scamsmart
8 https://www.gov.uk/government/consultations/pension-scams/pensions-scams-consultation
9 https://www.legislation.gov.uk/ukpga/2018/3/contents
10 Pension Schemes Bill 2019-21 - House of Commons Library (parliament.uk)

other key stakeholders DWP developed a government amendment to address these concerns, retaining the requirements of the clause, but enabling other indicators of scam risk to be captured.

7.10 All transfers between occupational and personal pension schemes will be covered under the new requirements. The new protections will apply to all transfers initiated from the day the regulations come into force, on 30th November 2021.

7.11 Before a statutory transfer can now proceed, one of the two conditions set out in these regulations must be satisfied.

The First Condition

7.12 This condition is satisfied where the trustees or managers of the transferring scheme satisfy themselves that the receiving scheme is one of the following:

- a Public Service Pension Scheme[11]; or
- a Master Trust[12]; or
- a Collective Money Purchase Scheme[13].

The Second Condition

7.13 This condition applies to all statutory transfers that are not covered by the First Condition and places a requirement on all schemes to decide whether red and amber flags may be present. These regulations set out what constitutes these flags. This condition directly addresses the demands of Parliament and industry for greater powers for trustees and scheme managers to prevent transfers where they identify indicators of high scam risk as a result of their due diligence processes.

Red Flags

7.14 There is a red flag present where the trustees or managers decide that:

- the member has failed to provide a substantive response to a request for evidence or information; or
- the member has not provided the specified evidence that they have taken the transfer scams guidance from Money and Pensions Service (MaPS); or
- a person without the appropriate regulatory status has carried out a regulated activity for the member in respect of the transfer; or
- the member's request to make the transfer has been made as a result of unsolicited contact for the purpose of direct marketing of the transfer; or
- the member has been offered an incentive to make the transfer; or
- the member has been, or considers that they have felt, pressured to make the transfer.

7.15 If the presence of a red flag is identified the statutory transfer cannot proceed.

11 https://www.legislation.gov.uk/ukpga/1993/48/contents
12 https://www.legislation.gov.uk/ukpga/2017/17/contents
13 https://www.legislation.gov.uk/ukpga/2021/1/contents

Amber flags

7.16 In addition, the regulations also set out amber flags that may indicate potential risk of a scam. There is an amber flag present where the trustees or managers of the transferring scheme decide that:

- the evidence provided by the member in response to a request for evidence or information under the regulations is incomplete; or
- some or all of the evidence provided in response to a request for evidence or information may not be genuine, or may not, as required, have been provided directly by the member; or
- the evidence provided by the member does not demonstrate the employment link or the residency link; or
- there are any high risk or unregulated investments included in the receiving scheme; or
- there are any unclear or high fees being charged by the receiving scheme; or
- the structure of investments included in the receiving scheme is unclear, complex or unorthodox; or
- there are any overseas investments included in the receiving scheme; or
- there has been a sharp or unusual rise in the volume of requests either to the same receiving scheme or involving the same adviser or firm of advisers (or both).

7.17 If the presence of an amber flag is identified, the transfer can only proceed if the member takes specified scams guidance from MoneyHelper[14], part of the Money and Pension Service (MaPS), and provides the trustees or managers of the transferring scheme with specified evidence confirming that they have taken it. Where that evidence is not so provided, this is a red flag (see 7.13, second bullet) and the statutory transfer cannot proceed.

Seeking further evidence or information to assess the red and amber flags

7.18 The trustees or scheme managers have the power to seek, at their discretion, evidence or information from the member in order to decide whether the red or amber flags may be present in respect a transfer.

7.19 Where they consider that they already have enough information to decide that the substantive red flags (*see* 7.13, third to sixth bullets) and substantive amber flags (*see* 7.15, fourth to ninth bullets) are not likely, on the balance of probabilities, to be present in respect of a transfer, they can proceed to make that decision without further activity to seek evidence or information from the member (unless the employment link or residency link applies).

7.20 Where they must seek evidence or information from the member in respect of the employment link or residency link, or decide to seek, at their discretion, evidence or information from the member in order to decide whether the substantive red or amber flags may be present in respect a transfer, they then must decide whether they have reason to believe (a lower standard of proof to the balance of probabilities) whether any of the red or amber flags present. Provided they do not, the statutory transfer may

14 https://www.moneyhelper.org.uk/

proceed. Where, however, they do find any of the red flags present (including where the finding of an amber flag has resulted in the MaPS guidance requirement being applied but the member has not provided the specified evidence of having taken that guidance), the statutory transfer may not proceed.

Employment and Residency Links

7.21 Trustees or scheme managers must request evidence from the member if the transfer relates to:

- an occupational pension scheme; or
- a Qualifying Overseas Pension Scheme (QROPS), that is not an occupational pension scheme; or
- a QROPS that is an occupational pension scheme.

7.22 There is an employment link where the trustees or scheme managers decide that:

- the member's employer is a sponsoring employer of the receiving scheme.
- the member is in employment with the sponsoring employer, which has lasted for a continuous period of at least 3 months; or
- is that the member must have been paid an average gross weekly salary, during the last 3 months, which was at, or above, the lower earnings limit; or
- contributions to the receiving scheme have been paid by, or on behalf of, the sponsoring employer, or by, or on behalf of, both the sponsoring employer and the member.

7.23 This instrument requires trustees and scheme mangers to base their decisions on the following specified evidence:

- a letter from the member's employer; and
- a schedule of contributions or payment schedule; and
- payslips, or other written evidence of pay; and
- copies of the personal bank or a building society statements, or a copy of a building society passbook, showing the deposit of salary for the period.

7.24 There is a residency link where the trustees or scheme managers decide that the member is resident in the country or territory where the QROPS is established. The residency requirement is the same as that applicable in the exclusion from the overseas transfer charge (OTC) in section 244B of the Finance Act 2004, although the evidence required to demonstrate it is prescribed. Therefore, there is broad alignment with the exclusion from the OTC, which pension schemes already assess.

7.25 The evidence required to demonstrate residency is less specific than is required to establish an employment link, being:

- a copy of the member's formal residency documentation; and
- at least two other pieces of evidence confirming the member's residency.

7.26 Failure to provide evidence of either an employment or residency link will mean an amber flag is present (*see* 7.15, third bullet). Additionally, where trustees and scheme managers have concerns about the evidence provided, an amber flag is also triggered (*see* 7.15, second bullet).

8. European Union Withdrawal and Future Relationship

8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

9.1 Not applicable to this instrument.

10. Consultation outcome

10.1 As pensions are a reserved matter for Scotland and Wales, the consultation on the regulations covered the entirety of Great Britain; no specific consultation was required for Scotland or Wales. The Department for Communities will make corresponding legislation in Northern Ireland.

10.2 Intensive stakeholder engagement took place before and after the consultation. Stakeholders included: TPR, the FCA, Pension Scams Industry Group (PSIG), scheme administrators and professional trustees. These stakeholders represented the views and interests of the majority of pension providers and pension savers.

10.3 Between 14th May and 10th June 2021, the Department for Work and Pensions ran a formal, public consultation, 'Pension scams: empowering trustees and protecting members', seeking views on proposed draft regulations implementing section 125 of the Pension Schemes Act 2021[15]. The Department asked seven questions about the proposed conditions on the statutory right to transfer. The Department received 69 responses from pension providers and administrators, legal firms, independent financial advisers, professional bodies, industry groups, regulators, consumer groups, and individual members of the public.

10.4 The majority of respondents strongly supported the government's intention to protect against pension transfer scams and the principles of the regulations. Many of the respondents raised general points about how the regulations would work in practice and whether there would be transitional arrangements, rather than concerns around the policy itself.

10.5 We have made subsequent amendments to the regulations based on where:

- a significant number of respondents have made the same, or similar points,
- where we believe suggestions have made it easier for schemes to operate the new requirements and/or improve protection for members, and
- where we consider that the alternative suggestions are workable.

11. Guidance

11.1 The Pension Regulator will be providing guidance to support the regulations.

12. Impact

12.1 The main impact is on the pensions industry, specifically occupational and personal pension schemes which facilitate the transfer of pension benefits to other pension schemes. There is no, or no significant, impact on charities or voluntary bodies.

15 https://www.legislation.gov.uk/ukpga/2021/1/part/5/crossheading/transfer-rights

12.2 The Equivalent Annual Net Direct Cost to Businesses of the package of measures contained in this instrument is £3.1m.

12.3 Costs principally stem from increased administration costs for the transferring schemes in scope. These administration costs include the wages of the administrator performing the required activities and potential postal costs of communication with employers and members.

12.4 There is no, or no significant, impact on the public sector.

12.5 A full Impact Assessment is submitted with this memorandum and published alongside the Explanatory Memorandum on the legislation.gov.uk website.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses.

13.2 The costs to business fall predominantly on pension schemes and pension service providers, and in certain circumstances on employers, including small and micro businesses who operate small and micro pension schemes. There is no evidence to suggest that a disproportionate number of statutory transfers will be moving to or from small employers' schemes. Therefore, we do not believe there to be a disproportionate impact on small and micro businesses.

14. Monitoring & review

14.1 DWP have publicly committed to a review of these regulations within 18 months of them coming into force to ensure they remain effective in targeting the evolving methods used by scammers.

14.2 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015 Guy Opperman MP, Parliamentary Under-Secretary of State for the Department for Work and Pensions has made the following statement:

"Having had regard to the Statutory Review Guidance for Departments published under section 31(3) of the Small Business, Enterprise and Employment Act 2015, in my view, it is not appropriate to make provision for review in the Occupational and Personal Pension Schemes (Conditions For Transfers) Regulations 2021."

15. Contact

15.1 Julian Barker at the Department of Work and Pensions, Telephone: 07941893143 or email: julian.barker@dwp.gov.uk can be contacted with any queries regarding the instrument.

15.2 Fiona Frobisher, Deputy Director for Private Pensions and Arm's Length Bodies, at the Department of Work and Pensions can confirm that this Explanatory Memorandum meets the required standard.

15.3 The Minister for Pensions and Financial Inclusion, Guy Opperman at the Department for Work and Pensions can confirm that this Explanatory Memorandum meets the required standard.