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VIA EMAIL

House of Commons Public Bill Committee

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To the Committee

Pension Schemes Bill 2025: response to Call for Evidence

We are corporate lawyers advising a range of pension scheme trustees and employers, including some of the largest schemes in the UK. We thank you for the opportunity to provide evidence in relation to the Pension Schemes Bill 2025, which will have a significant impact on our clients and the pensions industry as a whole. We hope that our thoughts below, which come from our analysis of the draft Bill published on 5 June 2025 and discussion with clients and others in the industry, are helpful in your consideration of the Bill.

Power to pay surplus to employers (Clauses 8 – 9)

Please note that the comments in this section have also been provided to the Department for Work and Pensions, through our work with the Legislative and Parliamentary Subcommittee of the Association of Pension Lawyers (APL). They incorporate comments from other members of that Subcommittee.

1. The Bill includes a power to modify scheme rules by resolution in the circumstances set out in draft sections 36B(2) and (3) of the Pensions Act 1995 (PA95), to allow payment of surplus to employers. There are some situations where it is not clear whether the new resolution-making powers would apply:

    - **Where the power in a scheme's rules requires employer consent or is exercised by joint decision.** For example, where the rules say something like:

      The Employer may, after consulting the Trustees, reduce any surplus reported by the Actuary on an actuarial valuation by any one or more ways as are permitted by relevant legislation.

      In this case, s36B(2) would not apply (because it applies only where 'no power is conferred on any person to make payments to the employer').

      It is unclear whether s36B(3) would apply: this is available where 'a power is exercisable by the trustees (whether or not by virtue of subsection (2)) to make payments to the employer'. On the face of it, the example rule above gives an employer power, not one that is 'exercisable

by the trustees'. Our view, however, is that this should be read alongside section 37, which effectively converts such a power into a trustee power, meaning that the power is, in fact, 'exercisable by the trustees'. This may still be subject to employer consent, and s.36B(3) should make it clear that that does not prevent the power from being used.

A way to make this clearer in the draft legislation (if this reflects the Government's intention) would be to amend draft 36B(3) to:

Where a power is exercisable by the trustees (whether or not by virtue of subsection (2), whether acting alone or with one or more other persons, and taking into account section 37) to make payments to the employer…

- **Where a scheme has a rule which allows return of surplus on winding-up (or other circumstances), but not on an ongoing basis.**

  It seems that s36B(2) would not be available to introduce a power to pay surplus while ongoing in respect of such a scheme (which is a common combination): the rules do not satisfy the condition that 'no power is conferred on any person to make payments to the employer'. 36B(3) refers to removing or relaxing restrictions on an existing power – this would not allow a power to pay surplus while ongoing to be introduced (unless you could interpret the need to be in wind-up in the existing rule as a restriction that could be removed, but this feels like a stretch).

  Our suggested amendment to s36B(2) is:

  Where no power is conferred on any person to make payments to the employer out of funds held for the purposes of the scheme (other than any power which is only exercisable when the winding up of the scheme has been triggered), the resolution may confer a power to ~~do so~~ make such payments on the trustees (whether exercisable before or after winding up of the scheme has been triggered), subject to any restrictions specified in the resolution.

- **Where a scheme's power of amendment prohibits amendments to the scheme to return surplus to employers, or where the scheme has other provisions which would conflict with a new override power, such as a requirement to apply any surplus only for the purpose of augmenting benefits.** It is not clear that 36B would override any existing restrictions. Our suggested amendment to address this is to 36B(1):

  The trustees of a trust scheme may by resolution modify the scheme in accordance with subsection (2) or (3) (including making any consequential amendments to facilitate the relevant power)

- **Where a scheme's rules include a power to pay surplus but no resolution was passed to preserve the power under section 251.** We think the effect of the repeal of section 251 under clause 8(2) is that the power automatically gets reinstated (i.e. it was not expunged from the rules by the lack of resolution previously, but rather remained in the rules but could not be used while s.251 required a resolution) – is that correct? Perhaps this could be clarified in the explanatory notes.

2. Draft s36B(4) states that the resolution-making powers do not apply where a scheme is being wound up. As currently drafted, this requirement appears to apply at the point the resolution is made but not to the point at which the power is exercised, so a resolution could be passed while a scheme is not in winding-up that confers a power to pay out a surplus when the scheme is later in winding-up. We think it is important to have this flexibility as otherwise it may prove very challenging for employers to agree a "package" in respect of surplus payments/benefit enhancements with trustees if the position of surplus on winding up is "off limits". Furthermore, schemes could otherwise end up in situations

where surpluses can be trapped on winding up (see, for example, the recent Pensions Regulator determination in relation to the Littlewoods Pension Scheme). This is reflected in our suggested amendment to section 36B(2) above.

3. We assume that in a multi-employer scheme it is intended that the trustee should have power to determine the split of any surplus between employers. This may be a matter for regulations but we would like to flag at this stage that there may be practical issues in industry-wide schemes where there are competing interests in play. Regulations might impose a requirement for employer consent – but presumably that would mean the consent of the receiving employer rather than all employers.

4. We note that there is no power to modify section 36B by regulations, except to take schemes out of scope altogether. Would it be helpful to include this flexibility? For example, see clause 9(6) of the Bill amending section 76(8): 'Regulations may provide that in prescribed circumstances this section does not apply, or applies with prescribed modifications, in prescribed circumstances or to schemes of a prescribed description.'

5. Clause 9 (draft section 37(2B)(d)) provides that '*Regulations must be made…requiring members of the scheme to be notified in relation to a payment before it is made*'. In some cases trustees may agree a programme of staged surplus payments, and the current drafting suggests that members would need to be notified prior to each staged payment. This would be onerous and could raise member concerns unnecessarily. We suggest that this regulation-making power should be amended to clarify that notifications to members can cover an agreed series of surplus payments.

6. Some sectionalised schemes have more than one trustee body – for example, in a sectionalised scheme with segregated sections, where there is a trustee board which is responsible for managing the scheme as a whole and separate trustee boards for each of the sections. The view of the APL Subcommittee was that it would be helpful if the legislation was amended to cater for this and, in particular, to make clear which set of trustees can exercise the power in these circumstances.

7. There is an anomaly in the drafting of s36B in the way it applies to sectionalised schemes. Under s37 of the PA95, where you are dealing with a sectionalised scheme, each section is treated as if it were a separate scheme (see regulation 18, Occupational Pension Schemes (Payments to Employer) Regulations 2006). The result is that when, for s37 purposes, you are considering whether or not a 'scheme' is winding-up, you look at whether the individual section is winding-up. This makes sense.

   However, the proposed new s36B(4) departs from this section 37/regulation 18 'for scheme read section' principle as it says '*This section does not apply— (a) to a scheme that is being wound up'*. On its face (because regulation 18 does not currently cover s36B(4)), the reference to 'scheme' would mean that, in a sectionalised scheme, if one section is winding-up and another is not, s36B does still apply even to allow amendments to the section which is being wound-up (because the scheme as a whole isn't winding-up).

   This seems like an odd result if the Government does intend to restrict the changes to schemes that are not in winding-up - we would also therefore expect the new powers to apply at section level. This could be achieved by amending regulation 18, Occupational Pension Schemes (Payments to Employer) Regulations 2006 to cover the new provisions, or by including a similar regulation in the new surplus regulations to be published.

8. Also in relation to winding-up: even where payment of surplus on winding-up is possible, currently once a scheme (or section of a sectionalised scheme) starts winding-up, no surplus payment can be made until all liabilities are secured. That locks a surplus up, as winding-up can take a long time. Is there scope for the 'ongoing' regime under section 37 to apply while winding-up of a section is taking place (noting that relevant conditions and trustee fiduciary duties would still apply to any payment)?

9. In relation to the timing of the surplus payment changes, the roadmap suggests that regulations and guidance will come into force by the end of 2027. We have heard from many in the industry who would like to see changes sooner, and the delay is causing issues for employers and schemes trying to deal with surpluses now. Delay may reduce the potential for schemes in this position to choose to run on. While we appreciate the volume of changes being dealt with in the Pension Schemes Bill and the limit on Government and Parliamentary time, could these changes be made separately rather than part of the general 'package'?

10. Also on timing, we note that clause 101(4) provides that the amendments contained in clauses 8 and 9 will come into force on the day the Bill receives Royal Assent, which appears to mean that trustees could amend a scheme to allow for surplus payments to employers (where no such power currently exists) in advance of the regulations coming into force – noting that current legislative restrictions and fiduciary duties would apply to any such payments. If it is not feasible to bring all of the changes into effect sooner, is the intention that these provisions will come into force before regulations are made?

11. A number of tax issues could helpfully be addressed. We have summarised some of these below but would be happy to provide more detail.

- Being able to make one-off payments to members from surplus as an authorised payment would help the aim of ensuring members gain some benefit from surplus release by receiving a material lump sum rather than a minimal increase in annual pension.

- A more tax efficient way of using DB surpluses to fund DC contributions in another scheme would help employers make use of surpluses in a way that still supports retirement.

- There is a mis-match between the tax legislation and pensions legislation on allowing payment of a surplus on winding-up a section of a scheme: pensions legislation permits this but tax legislation does not. This is another example of the so-called 'rules lottery' – availability of surplus will depend on whether an employer chose to operate a single scheme with different sections or different schemes for groups of employees.

  We believe this could be resolved without a change of the law by HMRC amending its Pensions Tax Manual, however HMRC has been approached on this and they have not been open to the suggestion, therefore clarification in the legislation would be helpful (which we believe could be done by amending existing regulations).

- HMRC has taken the view (see its Pension Schemes Newsletter 163) that the authorised surplus payment charges set out in section 207 of the Finance Act 2004 arise on the value of the gross amount of the authorised surplus payment and not the amount received by the sponsoring employer on the refund of surplus. We, and others in the industry, disagree with this interpretation of the legislation, which would make the tax on extraction of surplus higher and therefore less attractive. Clarity on this issue is essential so that schemes and employers can plan appropriately.

Small pots consolidation (clauses 20 – 37)

12. In the provisions on small pot consolidation, there doesn't seem to be an initial step where the auto-enrolment scheme has to inform the data platform that it has a small pot and request the proposals – presumably will become clear in regulations (and the regulation-making power is very broad, so could cover this).

13. Clause 23 exempts a pot from small pots consolidation requirements where '*the trustees or managers of the scheme that holds it determine that it is in the best interests of the individual for whom the pot is held that it should not be transferred in accordance with small pots regulations'.* While the examples given in the explanatory note are helpful, clause 23 as currently drafted has no restrictions and could

open the door to members bringing complaints against trustees where they get a worse outcome in a consolidator than they would have if they stayed in their original scheme (for example, they could argue that trustees should have used this power not to make a transfer). Is it intended that the prescribed conditions for exemption from consolidation will provide appropriate restrictions to mitigate this risk?

Scale and asset allocation (clauses 38 – 40)

14. Application of the new requirements to existing master trusts is unclear. The main scale and asset requirements (clause 38) are inserted into the auto-enrolment criteria for master trusts and GPPs. However, clause 39(1) amends the master trust authorisation provisions in the Pension Schemes Act 2017 (PSA17) to insert an investment capability requirement and the scale requirement. Although that would only apply on a new application for authorisation, (existing) PSA17 section 19(1) says: *'If the Pensions Regulator stops being satisfied that an authorised Master Trust scheme meets the authorisation criteria, it may decide to withdraw the scheme's authorisation'*. This appears to mean that all existing master trusts, rather than just new applicants or those used for AE, could have their authorisation removed if they don't comply with the new authorisation requirements. Is that the intention?

Default pension benefit solutions (clauses 42 – 50)

15. Clause 44(7)-(9) allows trustees to request (and may require them to request) information on members' financial circumstances or plans for retirement in order to design or review default pension benefit solutions and to determine what solution and rate of decumulation may be appropriate for a member. This raises issues with the boundary between guidance and regulated advice (which we note is being reviewed separately) and imposes a significant burden on schemes to decide on the best solution for an individual. Schemes are not financial advisers and we believe they would be uncomfortable with this. There would also need to be provisions to cover the scenario where a member refuses to share information.

16. Clause 45(3) provides that regulations may require trustees to monitor the rate of decumulation under pension benefit solutions used by members and inform them if they consider that the rate of decumulation should be reviewed. Arguably, this represents interference with members' right to choose how they use their funds (running contrary to the spirit of pension freedoms). It is also a level of monitoring that a member might expect from a paid IFA but is potentially a huge additional burden for trustees/providers. Again, we do not expect that schemes will feel comfortable with this obligation.

17. There is an overlap here with proposals for guided retirement and targeted support, in which providers will use their expertise and data to describe cohorts of individuals with common characteristics and support them to make informed choices – difficulties could arise where the information provided (for example about decumulation rates) differs from pre-retirement information or changes over time/in response to external circumstances; or indeed where it does not change and members argue that it should have done.

General provisions

18. Clause 93 amends s91 PA95 to allow a charge or lien on, or set-off against a person's entitlement for in certain circumstances. One of these circumstances is that a dispute as to amount 'has been resolved by the parties to it'. Could more detail be given on how this resolution can be shown. For example, where a member has been through a scheme's internal dispute resolution process and not appealed a decision, is that sufficient? This would be helpful in allowing schemes to recover overpayments.

Smaller drafting comments:

19. Clause 16(5) says that the Pensions Regulator may decide that subsection (1)(c)(ii) is not to apply, but there is no (1)(c)(ii). The guidance notes say this is supposed to allow the Pensions Regulator not to

close the scheme to new members, but that is not one of the listed consequences of a 'not delivering' rating.

20. There appears to be an inconsistency between proposed new section 28C(1) and 28C(4). 28C(1) refers to asset allocation for the 'totality of the assets held in funds of the scheme', whereas (4) refers to qualifying assets being those held in a default fund. Reading them together, it could mean that the amount of relevant assets in the default fund has to create an overall percentage investment in qualifying assets in the fund as a whole (so the actual percentage required in the default would need to be higher to create the overall percentage). We assume this is not the intention.

Please do let me know if you would like any more information or assistance, or to discuss any of the above matters further. We are very happy to help.

Yours faithfully

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