NORTON ROSE FULBRIGHT

UK Pensions Briefing: Brexit and pensions

Where we are now

January 2021

Now that the Brexit implementation period has ended, trustees and employers need to consider the implications for their pension schemes and what practical steps they should be taking to ensure the smooth running of their schemes.

This is an update to our October 2020 pensions briefing on what Brexit could mean for pension schemes.

Background

The UK formally left the EU on January 31, 2020. During the implementation period that followed the UK remained a member of the single market and customs union and continued to be subject to EU rules. That period ended at 11pm on December 31, 2020 when a "no deal" Brexit was avoided thanks to the trade deal set out in the EU-UK Trade and Cooperation Agreement (TCA).

Both during the implementation period and now that it has ended, the situation for pension schemes remains broadly unchanged. However, there are certain practical consequences as we explain in this briefing.

The effect of Brexit on UK pensions law

Much of UK pensions legislation is derived from EU Directives or CJEU decisions, particularly in relation to equality and final salary scheme funding. It remains broadly unchanged following the end of the implementation period and is not expected to change significantly in the short term. Equality and scheme funding, in particular, are well-established areas of UK pensions law and regulation, and it seems unlikely that there would be the political desire to make any changes for now.

For example, any scheme trustees or employers hoping that Brexit would be a solution to GMP equalisation will be disappointed. The UK courts have already decided that pensions must be equalised for the effects of GMPs and Brexit does not change this.

However, there may be some changes and divergence from EU law over time. Theoretically the UK government could repeal some legislative requirements. In addition, any future decisions by the CJEU will not be binding on the UK courts (although the courts may have regard to such decisions if the decisions are "relevant").

The Supreme Court and Court of Appeal (and equivalents in Northern Ireland and Scotland) can also depart from pre-January 1, 2021 CJEU decisions where they consider it right to do so. In doing so, they would need to apply the same test as the Supreme Court would apply if departing from its own existing decisions. In other words, we may not see this happen often.

Cross-border schemes

The legislation governing cross-border schemes ceased to apply at the end of the implementation period without a detailed new regime replacing it. For now, cross-border schemes should comply with guidance from the Pensions Regulator (TPR) which plans further updates "in early 2021". In particular:

- UK-based schemes need to check whether EEA-based employers can continue to pay contributions. This will depend on the rules of the relevant EEA member state, and
- UK-based employers using a scheme based in the EEA need to check it complies with UK rules and that the host EEA member state allows them to continue paying contributions. Employers should also consider the tax implications of paying contributions into the scheme and, if it is used for auto-enrolment, whether that can continue.

TPR estimates that there are only about 40 schemes which operate cross-border between the UK and another member state. Trustees of such schemes will now need to keep monitoring updates from TPR and from the relevant authority in their scheme's host EEA member state. TPR also suggests that any employers who are considering setting up new "cross-border" arrangements should wait for the UK government to clarify its policy on this.

As regards state pensions, the DWP has confirmed that (as required by the TCA) anyone who moves to live in the EU can still claim their UK state pension and it will be increased each year in line with the rate paid in the UK. This is regardless of when that person left the UK. Previously, only someone who had moved before January 1, 2021 was to be entitled to these increases. The DWP has also confirmed that social security contributions made in EU countries will continue to count towards qualification for a UK state pension.

Practical issues for trustees to consider

We set out below some key steps we recommend trustees take to ensure the continued smooth running of their pension scheme. TPR has issued guidance that refers to several of these issues.

Investment and insurance

The relative certainty achieved by agreeing a trade deal may mean less volatile markets than may have been expected in a "no-deal" Brexit scenario. Nevertheless, trustees of both DB and DC schemes should monitor developments. TPR advises trustees of defined benefit schemes to try to avoid "knee-jerk decisions" in response to changes in asset values; pension schemes are long-term investments and trustees should not be overly fixated on short-term market movements. That said, trustees should be speaking to their investment advisers about the continued suitability of overall investment strategies and contingency planning, any risks to scheme investments and what (if any) mitigations may be appropriate

To the extent they have not already done so, trustees should also check whether any funds which they are invested in are domiciled in EU countries and if so, they should discuss the implications of the end of the implementation period – in particular the end of "passporting" – with their investment advisers as soon as possible. A UK temporary permissions regime came into effect at the end of the implementation period, aiming to ensure a relatively smooth transition in this area. However, we would advise that trustees engage early with their investment advisers to ensure that there will not be any operational issues arising in relation to their EU investment funds and, if there are, to discuss 'work arounds' or alternatives.

As regards insurance, pension schemes wishing to undertake a "buy-in" or move to a "buy-out" with EU- or EEA-based members in scope should first discuss with their insurers whether they anticipate any regulatory obstacles which could result in delays or additional expense.

Employer covenant

Now that the outcome of the negotiations between the UK and the EU is known, trustees should discuss with their advisers the likely impact of the end of the implementation period and the TCA on their employer's particular business and covenant. If they have concerns, they should start a dialogue with the employer about future contribution payments and any expected changes to these.

Data protection

Trustees should check whether their schemes receive personal data from the EU or EEA. If so, they should consider building satisfactory data protection clauses into the relevant service provider contracts to ensure this data flow can continue after April.

For now, the TCA allows personal data to continue to flow freely between the UK and the EU (and EEA) for four months from January 1, 2021, which may be extended to six months. However, the UK information commissioner recommends putting in place alternative transfer mechanisms (such as standard contractual clauses) by the end of April "as a sensible precaution" to avoid any interruption to the flow of data to the UK after that time. This is while we continue to wait for the EU's verdict on whether UK data protections are adequate.

Contracts and governing documents

Trustees should review their contracts with administrators, actuaries and other third party service providers and update them as necessary to reflect the new context (including, if necessary, for data protection – see above). A number of tidying up changes may be required to pension schemes' governing documents, as well as to contracts with third parties, which may contain now outdated references to EU legislation or to the EU (or EEA).

Trustees should also ensure that overseas service providers, for example, investment managers, have the necessary authorizations to provide the services after the end of the implementation period.

Guarantees from EU companies

Trustees should review any guarantees that have been made in support of their schemes by EU companies to check there are no enforcement issues and to consider whether the strength of the guarantee or other security has been affected by recent events.

Paying benefits to overseas members

Some banks have closed the UK bank accounts of members living in certain European countries because of changes to passporting arrangements at the end of the implementation period. Trustees should liaise with their administrators and affected members to ensure their pensions can continue to be paid.

Member communications

Trustees should liaise with their advisers and administrators to ensure they are prepared to answer questions from members (particularly those resident in the EU) about how the end of the implementation period will impact their pension savings.

Conclusion

Although the implementation period has now ended and the EU and UK's future trade relationship has been formalised, that is not the end of the story so far as pension schemes are concerned. Sectors relevant to pensions, notably financial services, have arguably experienced something akin to a "no deal" Brexit and the future regulatory framework remains to be determined. Trustees will need to monitor developments and continue to assess the implications for their pension schemes, particularly in relation to pension scheme investments.

For help with Brexit-related issues, please contact the Norton Rose Fulbright pension team.

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