

Abolition of the statutory default retirement age - what about pensions?

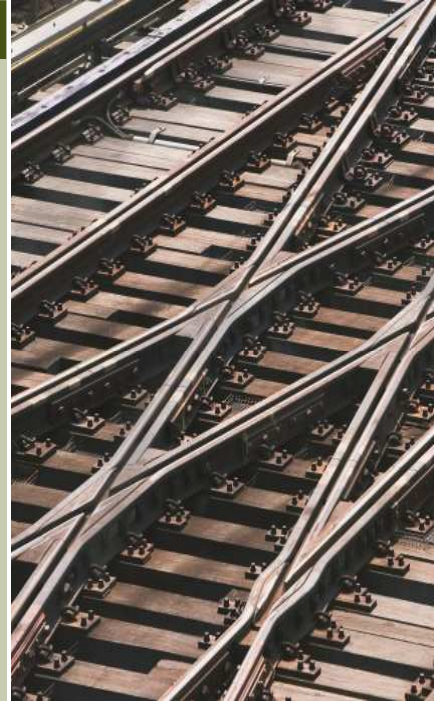
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Pension briefing

HIGHLIGHTS

- The statutory default retirement age (DRA), which had allowed employers to require employees aged 65 or over to retire without risking unfair dismissal claims, has been abolished with effect from 6 April 2011.
- Following the abolition of the DRA, employers must allow workers aged 65 or more to continue in employment and may only dismiss them on lawful grounds such as redundancy or poor performance.
- In general, benefit provision must continue as if the individual were aged less than 65, but some exemptions will apply.
- The "objective justification" defence to unequal treatment is unlikely to be available where employees aged 65 or over are denied benefits not covered by a specific exemption.
- Issues have arisen as to the pension and other benefits that must be provided for employees who continue in service after age 65. Defined benefit (DB) schemes (including those closed to future accrual but with deferred members still in service with the employer) can cause particular difficulties. However, defined contribution (DC) arrangements should also be reviewed, especially where contributions vary with age or enhanced ill health or death benefits are provided.

This note examines some of the questions that arise in relation to pension provision for employees in service over age 65.



BACKGROUND - ABOLITION OF DRA

The default retirement age (DRA), that allowed employers to enforce compulsory retirement of employees aged 65 or over without risking unfair dismissal claims, has been abolished with effect from 6 April 2011. Transitional provisions allow compulsory retirements under the DRA procedures where the employee was notified of retirement before 6 April 2011. Employers may retain a compulsory retirement age where this can be objectively justified - in practice, this is likely to prove difficult to argue successfully. Regulations¹ have been issued.

MUST I PROVIDE PENSION BENEFITS FOR EMPLOYEES AGED 65 OR OVER?

The basic position is that an employee aged 65 or over must be given the same benefits as those offered to employees aged less than 65. Provision of different benefits for those over or under age 65 would constitute age discrimination and will be unlawful unless it may be objectively justified, or it falls within one of the very few exemptions.

Pensions by their nature are inherently age discriminatory. Working out how to comply with anti-discrimination requirements within the structure of existing benefits can be challenging. The rest of this note examines some of the issues in further detail.

¹ The Employment Equality (Repeal of Retirement Age Provisions) Regulations 2011/1069

CONTINUED ACCRUAL	
BENEFIT	MUST BE PROVIDED FOR EMPLOYEES AGED 65 OR OVER?
Continued accrual - defined benefit (DB) schemes	Accrual should continue, despite the higher cost of DB accrual in respect of older members. Members may be given the choice of ceasing pensionable service and receiving a late retirement uplift (see the box below) as an alternative to continued accrual
Continued accrual - defined contribution (DC) scheme	Continue paying member and employer contributions as for employees aged under 65. DC contributions that increase with age fall within an exemption in the Age Equality Regulations and so are not unlawful, provided that the scale used to set the contributions is aimed at making the benefits from the arrangement equal (or "more nearly equal") for members of different ages. Where contributions increase for older members, check whether the scale for calculating contributions will continue to be appropriate when scheme has active members aged over 65.

DEATH IN SERVICE BENEFITS	
BENEFIT	MUST BE PROVIDED FOR EMPLOYEES AGED 65 OR OVER?
General exemption	There is a general exemption for removing insured benefits or a "related financial service" from employees aged 65 or over ² . This age limit will rise in line with increases in state pension age. Unfortunately, the exemption is not clearly drafted and the extent of arrangements it will cover is uncertain.
Life assurance arrangement provided by employer	Need not be offered to members aged 65 or over. Removal of this benefit falls within the general exemption.
Provision of insurance or a related financial service through an occupational pension scheme	The position is not clear but a purposive interpretation of the exemption would mean that this benefit may be withdrawn from employees aged 65 or over.
Death in service benefits backed by insurance but payable under scheme rules	Not exempt under the regulations: continue to provide the benefit. Consider amending the scheme rules to bring the provision of death benefits within the insurance exemption (subject to gaining the trustees' consent, if needed).
Death in service benefits provided from an occupational pension scheme through "self-insurance" (that is, provided out of the assets of the scheme)	Continue to provide the benefit. The meaning of "related financial service" in the general exemption is unclear but probably will not cover self-insured benefits.

ILL HEALTH BENEFITS	
BENEFIT	MUST BE PROVIDED FOR EMPLOYEES AGED 65 OR OVER?
Enhanced pensions on ill health	Must continue to be provided, and calculated as required under the scheme rules. Where an ill health pension is calculated by reference to prospective service to normal pension age, the prospective service will be zero where the member has already reached this age.

² The exemption applies where an employer "make[s] arrangements or afford[s] access to" insurance or a related financial service.

DEFERRING RETIREMENT AFTER AGE 65	
BENEFIT	MUST BE PROVIDED FOR EMPLOYEES AGED 65 OR OVER?
Pension payable at normal retirement age (NRA) of 65 or less	<p>Pensions may continue to come into payment at NRA, whether or not the member is still in service with the employer.</p> <p>Members working beyond NRA will have a <i>right</i> to take their pension at NRA unless:</p> <ul style="list-style-type: none"> the scheme rules allow pension payment to be deferred beyond NRA; AND the rules require a member to have ceased service with the employer before a pension may be paid.
Enhanced deferred (late retirement) pensions	<p>Members who cease accruing DB benefits <i>before</i> the scheme's normal pension age and who defer taking pension until sometime after that age must be given an enhancement (a "late retirement uplift") to compensate for the pension coming into payment late and so being paid for a shorter time.</p> <p>We recommend that members who cease DB accrual <i>at or after</i> normal pension age and defer taking pension are also given a late retirement uplift, although the legislation does not require this (see the box below).</p>

FLEXIBLE RETIREMENT	
BENEFIT	MUST BE PROVIDED FOR EMPLOYEES AGED 65 OR OVER?
Allowing members to take flexible retirement (drawing all or part of their pension while remaining in service with the employer)	<p>It is not necessary to allow a member to draw a pension at the same time as working, provided that the rules allow for a pension to be deferred where the member reaches NRA and is still in service with the employer.</p> <p>Where flexible retirement is allowed, consideration should be given to the treatment of death in service or ill health benefits during the flexible retirement period.</p>
Death in service benefits while working and drawing a pension	<p>Members should be treated as if they had died or fallen ill in retirement (possibly subject to an uplift if death in service or ill health benefits would be higher than the "in retirement" benefits). Members should be told the position should they die or become incapacitated while working and drawing pension before deciding to take flexible retirement.</p>

ACTIONS

- Check what pension, death in service and ill health benefits are provided to employees aged up to 65.
- Are any of these benefits subject to the exemption for insured benefits?
- Check whether your employment contracts give specific rights to these benefits - if so, the benefits must be provided beyond age 65 or the employment contracts changed.
- Where current benefits must be extended beyond age 65, are any rule amendments needed?
- Review your policy on flexible retirement. Amend your rules as necessary to ensure flexible retirees are not inadvertently entitled to a windfall of both "in service" and "in retirement" benefits.
- Communicate the benefits to be provided for employees aged 65 or over to the relevant employees and to the scheme administrators.

Trustees/administrators should continue to write to members six months before normal retirement date. Dialogue will be needed between employers and trustees to ensure that each has the information needed to process contributions, pay and benefits correctly.

LATE RETIREMENT UPLIFTS

- An enhancement to the level of pension (a "late retirement uplift") may be given where a member chooses, or is required, to defer the start of their pension beyond the scheme's normal pension date.
- Under the Pension Schemes Act 1993, a late retirement uplift must be given where the member has left pensionable service before normal pension age and defers drawing benefits until after that age.
- Technically, no late retirement uplift is needed where the member remains in pensionable service until normal pension age (or later) but questions of fairness - and whether the member should have been told that he could opt out of pensionable service before normal pension age and be entitled to an uplift - would arise if an uplift was not offered.
- For members who continue to work after 65, opting out of pensionable service and having a late retirement uplift on their deferred pension may be more beneficial than continuing accrual, especially if ongoing accrual requires member contributions.
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