The Trustee toolkit downloadable

Funding your DB scheme

Tutorial six: Additional employee funding

By the end of this tutorial you will better understand:

- what benefits can be provided from an additional voluntary contribution scheme
- the trustees’ responsibilities when additional voluntary contributions are paid to the scheme
- why some scheme liabilities are insured
- the impact of insured scheme liabilities on funding
- what insured benefits may be provided by the scheme

This tutorial is part of **Scenario three**.

Glossary

A detailed glossary of technical terms can be downloaded from the Resources tab when you log in at **www.trusteetoolkit.com**

The Pensions Regulator

Case study: Pre-April 2006

Members of DB schemes may have the opportunity to make additional employee contributions.

Up until April 2006, the Clayton Brewery scheme, like all occupational pension schemes, had to provide an additional voluntary contribution (AVC) arrangement. This allowed members to pay extra contributions with equivalent tax advantages to the main scheme.

Effectively, members were not allowed to contribute to multiple occupational schemes but they could have a freestanding AVC, but the same constraints on contributions etc applied. A few highly paid employees also chose to fund their pensions through salary sacrifice.

Case study: Post-April 2006

Schemes no longer have to provide an AVC facility.

What changed in April 2006?

Scheme members now have the freedom to run an additional pension alongside their occupational pension scheme. The tax legislation does not impose limits on the benefits which a member can accrue. However, there are significant tax charges where certain annual and lifetime thresholds are breached. Members need to take advice if they believe they may exceed the annual or lifetime allowances. Trustees may need to suggest to members with stakeholder pensions that they take advice.

What does this mean for the Clayton Brewery scheme?

Like other schemes, the Clayton Brewery scheme has to maintain its AVC arrangements in respect of benefits already acquired. However, whether the AVC has to be maintained for future contributions is dependent on scheme rules. In Clayton Brewery's case, the scheme rules allowed it to close the scheme for future contributions.

How are the additional benefits secured?

The benefits secured from additional employee funding depend on the scheme's provisions. At Clayton Brewery, as with most schemes, contributions accumulate on a defined contribution (DC) basis and the amount of pension depends on the same factors as any other DC arrangement.

Note that a very few schemes (mostly in the public sector) allow members to secure additional service on a DB basis by paying AVCs.

What are the trustees' responsibilities?

Trustees have as much responsibility for these arrangements as they do for the main scheme, and as much responsibility as trustees of DC schemes have for their schemes. For the trustees of Clayton Brewery's DB scheme, these DC arrangements are the only contact they have with DC funding.

Case study: Insured liabilities

In the Clayton Brewery's scheme, insurance policies provide for certain benefits.

Why are some liabilities insured?

In DB schemes most benefits are not insured. However it is quite common for schemes to have insurance policies to provide for certain benefits. This is particularly the case for small schemes where there is limited scope for spreading the risk over the membership. Compared to individual cover, this type of group cover is usually available at beneficial rates.

Death in service benefits

Death in service lump sums are the most commonly insured benefits. These benefits are often large (eg 3 x salary) and can be well in excess of the amount of assets held within the fund for a particular member (especially if a young member with short service dies). Although the chance of death is small, the impact on the funding position of the scheme could be significant. This is why insurance cover is particularly appropriate.

Other insured benefits

In addition to death in service lump sums, smaller schemes sometimes also insure spouses' pensions and ill health benefits. In larger schemes these benefits tend not to be insured.