

**CURRENT TREATMENT OF
OCCUPATIONAL PENSION RIGHTS
UNDER TUPE TRANSFERS**

**A report of research conducted for the Department of
Trade and Industry**

By IRS Research

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February 2000**

ACKNOWLEDGEMENTS

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Additional technical and legal advice was provided by Colin Sherwood, editor of the journal *Occupational Pensions*; and Roger Walden, joint editor of the *Industrial Relations Law Bulletin*.

IRS RESEARCH

February 2000

Contents

	PAGE
EXECUTIVE SUMMARY	1
INTRODUCTION	4
The current position on TUPE	
The need for research	4
METHODOLOGY	5
Analysis of respondents	6
The pension arrangements: analysis of responses	6
Conditions attached to transfer	
The legal and actuarial position	8
MAIN RESEARCH FINDINGS	12
What happened in practice	12
What transfer value?	13
Eligibility conditions	14
Enhanced pension rights with the new employer?	14
Take up of membership in new scheme	15
Consideration of pensions issues: Timing	15
Policy adopted	16
Consultation	17
Information on the transfer	18
Information to employees	19
Position of pension rights in the transfer	20
If TUPE applied	21
Other comments	22
Conclusions	25

List of Tables

(Tables 1-4 are in a separate document: www.dti.gov.uk/er/emar/tupe2.pdf)

- TABLE 1: RESPONSE RATE: REASONS FOR REFUSAL TO PARTICIPATE
- TABLE 2: RESPONDENTS BY SIZE, INDUSTRY AND TRANSFERS UNDERTAKEN
- TABLE 3: PENSION ARRANGEMENTS BEFORE AND AFTER TRANSFER
- TABLE 4: QUALITATIVE JUDGMENT OF TRANSFER
- TABLE 5: CONDITIONS ATTACHED TO TRANSFERS
- TABLE 6: BASIS USED FOR TRANSFER VALUE
- TABLE 7: ENHANCEMENTS PROVIDED FOR PAST SERVICE
- TABLE 8: CONSIDERATION OF PENSIONS ISSUES: TIMING
- TABLE 9: POLICY ADOPTED TOWARDS PENSION IN TRANSFER
- TABLE 10: WHO DECIDED POLICY
- TABLE 11: UNION CONSULTATION
- TABLE 12: IMPORTANT FACTORS IN POLICY AND APPROACH ADOPTED
- TABLE 13: POLICY CHANGES
- TABLE 14: INFORMATION GIVEN TO POTENTIAL TRANSFERORS AND TRANSFEREES
- TABLE 15: INFORMATION TO EMPLOYEES
- TABLE 16: IMPORTANCE OF PENSION ISSUES
- TABLE 17: EFFECT OF DECISION TO BUY
- TABLE 18: VIEWS OF BRINGING PENSIONS UNDER TUPE

CURRENT TREATMENT OF OCCUPATIONAL PENSION RIGHTS UNDER TUPE TRANSFERS

EXECUTIVE SUMMARY

To summarise the main points of this study:

1. The DTI is at present considering whether to bring continuing occupational pension rights to some extent within the coverage of the revised Regulations. However, there is little information on current practice and so the DTI have commissioned this study to clarify the position.
2. The study consisted of 16 interviews, seven with representatives of employers who had sold businesses and transferred employees out, nine with representatives of employers who had bought businesses and transferred employees in. Because of the short timescale required for the project, and the unwillingness of many of those contacted to participate, **the companies whose practices have been examined are not representative of all companies involved in TUPE transfers**. Overwhelmingly, they were large well known companies.
3. Most transferors and transferees *attempted* to secure what they saw as similar or better terms, and allowing people to join an existing pension scheme was generally seen as the way to do this. However, they did not always succeed. One multiple transferee offered pension provision only to management (except when taking on contracts from the public sector), and one made no pension provision at all.
4. In a final earnings scheme, the legal framework protecting early leavers' benefits is complex. The legal minimum "cash equivalent transfer value" (CETV) is based on the amount needed to provide a deferred pension escalating in line with **prices**: for the pension to be based on **earnings** at retirement a higher amount, commonly known as the past service reserve, is needed. There is a range of ways, above the legal minimum, in which past service can be treated on a transfer.
5. Several of the multiple transferors had laid down pension conditions, more or less firmly, for transferees of their businesses; it was not always possible to keep to these. The multiple transferees found, however, that those selling to them rarely made pension conditions. They were therefore able to implement their own policy, which was (with the exceptions already quoted above) to bring people into their existing schemes.
6. Most of the transferees accepted transfers in (with two exceptions, again). The majority appeared to give year-for-year entitlement, usually provided the employee consented to the transfer of accrued rights within a deadline.
7. Take up of membership in the new scheme was generally high.

8. Of the transferors, the majority gave at least the past service reserve (the amount needed to ensure that year-for year entitlement could be granted), and another one a share of the surplus, ring-fenced for five years.
9. There was no clear answer to the question of when pension issues were dealt with, although several pensions managers expressed the desire to "get in there early," and some of the multiple transferors had developed policy on this as time went on. Policy on how to deal with pensions was usually developed at a high level within the company, with considerable involvement by experts.
10. Arrangements were formally negotiated or discussed with the unions in only a few cases. However, even without such union interest, in most cases, the important factors in the approach taken were objectives of fairness and harmonious industrial relations. "Cost" and "efficiency" were mentioned only by three interviewees, of whom two were the transferees who were not making pension provision for all or most of those transferred.
11. Some transferors were far more open in their approach to giving information to the transferees than others, and there were complaints from transferees about inadequate information and membership data. Costs of providing information were not seen as high, except for actuarial work. Transferors frequently create "pro-formas" or "seller's packs" to provide all the information a transferee needed.
12. Where transferees and/or transferors were concerned about pension provision, they were generally providing information to scheme members, including announcements, group meetings, and access to independent financial advisers. The two companies not providing pensions were not providing information either.
13. The majority did not see the consideration of future pension rights as a significant factor in the transfer, though some would walk away from a deal if their policy could not be followed.
14. The majority of transferees felt that a TUPE requirement to have "broadly comparable" terms, (in the way they understood this term), would not have affected the decision to buy in the instances under discussion, though several saw sizeable administrative problems and effects on price. Of the two transferees not currently providing pensions, one said it would affect what purchases they would make, and the other would "find some way round it". Of the transferors, the majority thought it would not make a difference to the way they handled things, but there were again questions about practicality. Overall, there was opposition to the idea because of these issues. Several people voiced concern for the position of small firms, based partly on the experience of those they had dealt with during the transactions. It should be pointed out that only three of the interviewees had experience of the meaning attached to broad comparability by the Government Actuary.
15. A number of both transferors and transferees commented that the scenario would be different if the Government imposed minimum requirements for pension provision by employers, so that every employer would have some pension arrangement, rather than provision being voluntary on the part of the employer.

16. It is difficult to reach firm conclusions from such a small group, but it does seem as if the larger and better employers in the sample aim to treat pensions on the basis of what they see as providing equivalent benefits. The picture might be rather different if smaller and less financially secure companies had been included in the sample. There was little evidence of standardisation, though it was felt that this would assist the transfer process.

INTRODUCTION

THE CURRENT POSITION ON TUPE

The need for research

1. The Government is committed to amending the TUPE Regulations, in order to improve their operation and to implement the revised version of the EC Acquired Rights Directive adopted in 1998. One issue being considered is whether or not to bring continuing occupational pension rights to some extent within the coverage of the Regulations. One factor in reaching the decision will be the potential costs and benefits to business of making the change.
2. However, there is little information available about this at present. This exploratory study, therefore, is aimed at collecting information on how organisations recently involved in TUPE transfers treat continuing occupational pension rights. The DTI's brief for this research asked for the following issues to be addressed;
 - Do transferees generally provide for employees who had occupational pension rights before the transfer to continue to enjoy them after the transfer?
 - If so, is this because the transferors make it a condition of the transfer, or because of other considerations such as harmonious industrial relations and smoothing the transition?
 - Does the question of continuing occupational pension rights affect transferees' willingness to make TUPE acquisitions and/or the price they pay for them, and how does it rate alongside other financial factors?
 - Would bringing occupational pension rights to some extent within the coverage of the regulations (not necessarily on the basis of a requirement for broad comparability) affect the likelihood of transfers taking place, or the way in which they were carried out?
 - Where the transferees provide for transferred employees to continue to have occupational pension rights, is separate provision generally made for them, or are they generally absorbed into existing schemes? What costs are involved? Are there any wider knock-on business, organisational or employee relations effects or consequences?

METHODOLOGY

3. In order to answer these questions, IRS Research drew up a research project based on conducting face-to-face interviews with senior managers in companies that had been involved in TUPE transfers. Sixteen interviews were conducted in all, by three different researchers, all experienced in pensions issues. In the event, last minute commitments on the part of a small number of case study organisations led to the late cancellation of four appointments for face-to-face interviews. In order to meet the time scale for the project the four interviews concerned were instead conducted by telephone. The transcripts from all the interviews, and copies of scheme documentation where available, were analysed for this research report.
4. A short timescale was required for the project, which meant that there was limited scope to ensure representation of the full range of organisations involved in TUPE transfers. The intention was to aim for a mix of sectors and a range of manual and non-manual occupations, with at least half being transferees and the rest transferors, and at least one transferor and one transferee having been involved in a number of transfers over recent years.
5. In the event, much difficulty was experienced with obtaining sufficient responses, as table 1 (see separate document: www.dti.gov.uk/er/emar/tupe2.pdf) illustrates. IRS initially contacted a list of 37 private sector companies, of which 22 were transferees, and 15 were transferors. Of these nine companies agreed to participate. As shown in the table, six transfers turned out to be non-TUPE. A significant number of potential respondents told us that they were "too busy", did not respond to messages, or could not be contacted (as they were away) within the timescale. Among other reasons given, one company said that it would not be "beneficial" to participate. In another case where receivers were selling on behalf of creditors, we were told that "pension considerations were not taken into account at all".
6. In the light of this high refusal rate, IRS drew up a second list of 50 companies (32 transferees and 18 transferors). From this list we obtained a further seven participants. Again a significant number were too busy (4); or did not respond to messages (8). In several cases, we left three or four messages before giving up. A further 19 were not contacted from the second list once we had obtained our sample number.
7. We therefore contacted in total 68 organisations to obtain the sample of 16. This response rate of just under a quarter is lower than we would have expected. Overall we gained the impression that our interviewees - company secretaries and pension fund managers - were under enormous time pressures, and the short timescale within which the interviews had to be completed reduced the willingness to participate.
8. It needs to be stressed that as a result of the somewhat limited selection process, and the high refusal rate, the sample cannot be said to be representative of organisations involved in TUPE transfers. Overwhelmingly, interviewees came from large, healthy, well known companies and indeed those who agreed to be interviewed tended to be people who had views and wanted to share them. Strenuous efforts were made to obtain responses from smaller companies, but with very limited success. It would have been very informative, for example, to include in a sample the company in receivership quoted above. It would also have been interesting to see the issue from the point of view of the smaller companies being acquired by some of the expanding firms in our sample. A study of the pension issues

around takeovers and contracting out in due course, with a larger and more representative sample would make a useful component in the DSS's series of research studies on occupational pensions. It seems unlikely that the picture would have been the same if smaller companies with less of a reputation to lose and a less financially secure position had been in the sample. It would also be useful to question the advisers, especially the actuaries, who were heavily involved in the process (see para 60)

9. Face to face interviews lasted on average just over 1 hour 30 minutes. Telephone interviews were shorter - on average around 40 minutes. Each followed a detailed interview schedule and was taped.

ANALYSIS OF RESPONDENTS

10. Table 2 (at end of document) analyses briefly each of the respondents by size, industry, transfer(s) undertaken, and information provided. As will be seen, in all only four schemes provided booklets, and in no cases were they available for both transferee's and transferor's schemes in a single transaction. One booklet related to Company C's current scheme, which had been improved in a number of ways since the bulk of acquisitions took place. The interview schedule included, in annexes, a set of questions about the schemes, both of transferor and transferee. Completion of these was not comprehensive. In general, the interviewees' own scheme details were provided but not those of the other party(ies) to the transaction. Only in two cases were both sets of details fully completed. In nine, the major points of the other party's scheme were given (type of scheme and accrual rate, for instance) but the detail was not. In seven it was not completed at all.

11. The reasons for this appear to include the following

- in most cases, the interview was referring to past transactions, and whatever material had been provided then was not to hand (in two cases, where transactions were still going through, material was not yet available);
- as explained in para 57, there was considerable reliance on advisers and consultants, to whom the detailed information would probably have been passed;
- as explained in para 63, some people had experienced considerable difficulty in obtaining information from the other party

12. Interviewees varied, understandably, in the amount of research they had done beforehand. Those who were pension managers or in a similar position will have known their own scheme very well, but the opposite parties' schemes much less well, while those from other disciplines would not necessarily have detailed knowledge of their own scheme either. Some of the information provided, therefore, was fairly impressionistic and came from the respondent's memories rather than detailed checks of documents.

THE PENSION ARRANGEMENTS: ANALYSIS OF RESPONSES

13. A main objective of the research was to find out what was happening with transfers within the private sector. It should be pointed out here that there is a difference in practice, and terminology, between public and private sectors. In transfers from the public sector, (both sales and transfer of staff as a result of letting contracts) a procedure has been

adopted under which the Government Actuary's Department (GAD) will certify whether the new employer has a "broadly comparable" scheme. To quote the recently published Statement of Practice by the Government Actuary

"Value

- The overall value of the new scheme should be equal to or greater than that of the current scheme.
- There will not be any identifiable group of individuals within the staff being transferred who, overall, are materially worse off.
- Value is assessed by calculating, on consistent assumptions and methods, the underlying employer costs, in excess of the employee's share of the cost, of providing the benefits under the scheme which will accrue over the remaining working life.
- Value is considered as that in the hands of the employee gross of any liability of tax.

Contributions

- Schemes with higher employee contributions will not be deemed broadly comparable because of the implied reduction in net pay (unless a compensating pay rise is proposed).

Benefits

- The range of benefits provided under the new schemes must at least match that provided by the current scheme.
- Benefits must be available from the new scheme in respect of the same events and at the same time as would have arisen in the existing scheme.
- In some cases, the amount of benefit may be lower on a particular contingency than under the current scheme, but this will need to be balanced by better benefits on other contingencies."

14. The GAD's Statement also makes clear that safeguards for the security of benefits (including member representation on trustee bodies) are required, and that money purchase (defined contribution) schemes where the risk is on the employee rather than the employer, cannot be regarded as broadly comparable to final earnings (defined benefit) schemes.¹

15. Thus a term that might seem at first to be fairly general does have a precise meaning in the public sector. The three multiple **transferees** who had taken on staff were familiar with the "broadly comparable" concept and interviewees had dealt with its consequences; where transactions had been wholly in the private sector, interviewees were not familiar with it. On the evidence of these interviews, the same precision does not apply. Interviewees spoke of "no less favourable", "equal value" or "equivalent" pension terms, and we have chosen out of these the term "equivalent". Analysis was not always rigorous. To quote one pensions

¹ Appendix to HM Treasury statement on staff "*Transfers from Central Government. A fair deal for staff pensions*", *Guidance to Departments and Agencies*, June 1999

manager, from multiple transferor Company O, "I would look through the scheme booklets of the transferee and check there was nothing untoward."

16. It had originally been planned to do an analysis of the scheme before and after the transfers along the lines of the Government Actuary's analysis under the public sector's "broad comparability" guidance. However, as explained above (paras 10 - 12), the information provided by interviewees was generally not very detailed, for a variety of reasons. It therefore proved impractical to do this analysis. Only a fairly impressionistic one, based on the details which were available and what the interviewers were told about the policy, could be done.

17. "Broad comparability" in the strict GAD sense can be definitely said to exist in those cases where special schemes or special sections have been set up, and in those where it was a transfer from the public sector. Apart from these cases, the information available from interviewees was not sufficient to assess in general whether the new and old schemes would have fully met the test, so on the basis of a broad brush analysis these have been categorised as "equivalent" (or not). The assessment of scheme quality in Table 3 (see separate document: www.dti.gov.uk/er/emar/tupe2.pdf) has been done in the same broad brush way.

18. In the three cases of single sales, two transferors had arranged for equivalent provision for those transferring, plus in one case a non-equivalent GPP for a small group of staff. The third had seen a GPP (of which full details are unknown) introduced instead of the good quality scheme, representing a worsening.

19. Of the single **transferees**, one gave a choice between an improvement and a worsening, and the other gave either an equivalent scheme or an improvement, depending on which part of the previous scheme those transferred had been in; there was one overall improvement.

20. All four of the multiple **transferors** sought "equivalent" benefits, although in one case some groups were moved into a money purchase scheme of "equivalent value". Of the seven multiple **transferees**, there were three cases where "broadly comparable" arrangement, in the Government Actuary's strict sense, were available for those staff for whom it was a requirement (i.e. when the business or the contract was coming over from the public sector). Overlapping with this, there were examples of "equivalent" benefits being provided, through the new employer's scheme(s), and there were two examples of worsening or continued non-coverage.

21. Table 3 summarises the way in which the pension arrangements differed before and after the transfer.

CONDITIONS ATTACHED TO TRANSFER

The legal and actuarial position

23. Before dealing with the responses on these questions, it is necessary to explain the legal and actuarial position .

24. Anyone leaving an occupational pension scheme before the scheme's "normal retirement date" is considered, under social security legislation as an "early leaver". This includes people taking early **retirement**, for whom the early leaver rules act as a statutory underpinning.

25. "Early leavers" with less than two years in a contracted out salary related pension scheme can have a refund of their own contributions less tax and the contracting out rebate. They receive no credit for those made by the employer, which stay in the fund. With a contracted out money purchase scheme, no refund of the Protected Rights is allowed, so a preserved pension (often very small) must be set up.

26. Schemes can offer deferred pensions to people with less than two years' service, if wished. After more than two years with that employer, the pension must be either preserved (also often described as "frozen" or "deferred") or transferred. The rules vary between pre- and post-1997 pension.

27. There are special rules for pre-1997 services relating to identifying the Guaranteed Minimum Pension. For post-April 1997 service, a final earnings pension is no longer divided into Guaranteed Minimum Pension and excess. Instead, the whole pension is increased by the rise in the Retail Prices Index or 5% compound, whichever is the lower.

28. Almost everyone with a preserved pension has the right to take a transfer out of the scheme, up until a year before retirement. For a final-earnings scheme the minimum requirement is for a "cash equivalent transfer value", calculated broadly as the capital needed to be set aside now in order to provide the pension promised.

29. With a money-purchase value, the transfer value is simply the amount that has built up in the fund at that time, less charges and deductions

30. The individual has the choice of taking the transfer to

- the new employer's scheme - it is at the trustees' discretion whether to accept it, and there is no right to transfer in; or
- a Personal Pension or the older form of "Section 32 buy-out".

31. The minimum cash equivalent transfer value is not normally enough to provide year-for-year service in the new scheme, however, even if the benefit package is the same. This is because the cash equivalent transfer value has been calculated on the basis that the preserved pension will rise in line with **prices** (with a 5% cap and ceiling in the private sector schemes). The pension to be provided at retirement, however, will have increased in line with earnings, which on average increase faster than prices, and in the case of "high flyers", very much faster than that.

32. An example, on a rather simplified basis and assuming no Guaranteed Minimum Pension is payable, may help to illustrate the point.

Mr X leaves scheme A 25 years before his normal retirement date, having had earnings of £15,000, and having built up a pension of £3,000 (20%). His preserved pension at retirement will be £10,159, taking into account 5% compound interest over 25 years. Taking some round (and inaccurate figures) for the purposes of this illustration, the actuary calculates in his case that he will need a "pot" of money of £100,000 at normal retirement date to pay this entitlement, and that to achieve this figure, after investment returns over all that time, £18,000 needs to be set aside now.

However, Mr X's pay increases with the new employer in fact average 7% a year, so his earnings are now around £81,000 and 20% is £16,260. Again, using an inaccurate 10-1

ratio, there should be £160,000 set aside by the time he retires. That would mean having £28,000 available when he left.

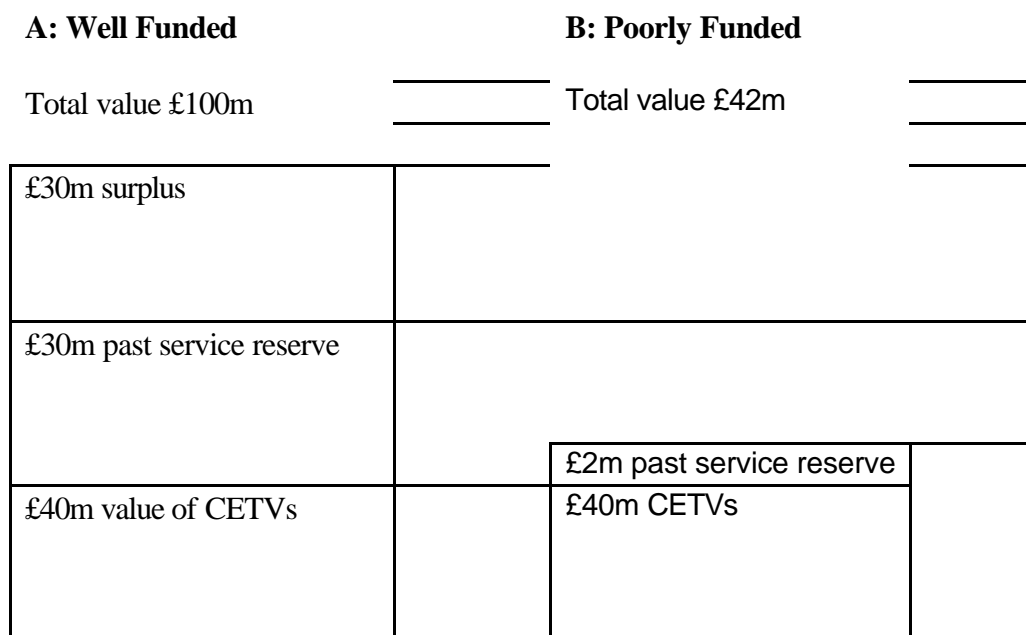
Thus if Mr X takes his transfer value estimate to scheme B's pension manager when he joins the company, he will be offered fewer additional years' service than he had in scheme A. Indeed, it is rare today with an "ordinary" transfer to be offered additional years of service at all, because the trustees are unwilling to take on the risk that the final earnings pension at the end will be higher than the amount calculated by the actuary many years previously.

For Mr X to be offered a year-for-year transfer credit, extra money has to come from somewhere - **either** Scheme A has to agree to pass over the past service reserve **or** Scheme B has to agree extra funding with the employer. (If the pension scheme is the core public services, there is a transfer "club" in which, within certain conditions, year-for-year transfers are available. The funding calculations reflect this, and there is also an assumption that, broadly speaking, flows between schemes will cancel each other out over time - rather like the insurance companies' "knock or knock" arrangements.)

33. In valuing the liabilities of a final earnings pension fund, the actuary will assume that all, or the bulk of scheme members, will be drawing pensions based on the earnings at retirement, and so has to build in a figure for **earnings** increase. (What allowance is made for early leavers and just how it is calculated, depends on the actuarial method used.) The total of the fund set aside for service already completed is generally **more**, therefore than the aggregate value of the cash equivalent transfer values. The amount that is being held to cover the expected rise in earnings is often referred to as the "past service reserve". In addition a well funded scheme may have a "surplus" above that - that is, assets greater than are needed, in the actuary's view, to provide the benefits promised. A poorly funded scheme, while still above the Minimum Funding Requirement required under the Pensions Act 1995, may have little or nothing above the cash equivalent transfer values, and an even worse funded scheme may not even be able to pay those cash equivalent transfer values in full.

To illustrate this diagrammatically:

Diagram 1



34. An additional factor is that safeguards have been introduced in recent years for individuals in cases of "compulsory transfers" (that is, where the trustees decided to transfer the liability, and hence the assets, to another scheme without the members' consent). Before a transfer can take place, an actuary must certify to the trustees or managers of the transferring scheme that:

- the transfer credits to be acquired for each member under the receiving scheme are, broadly, no less favourable than the rights to be transferred
- if the receiving scheme were wound up immediately after the transfers, the rights would not be likely to be materially less secure than they would be if the transferring scheme were wound up immediately before the transfer
- where it is the established custom for discretionary benefits or increases in benefits to be awarded under the transferring scheme, there is good cause to believe that the award of discretionary benefits or increases in benefits under the receiving scheme will (making allowance for any amount by which transfer credits under the receiving scheme are more favourable than the rights to be transferred) be broadly no less favourable.²

35. Actuaries are understandably wary of giving such a wide ranging certificate, so compulsory transfers are not common; it is far more usual to ask for consent. If that consent is not forthcoming, the individual will retain a preserved pension in their former scheme (or could transfer elsewhere) but it is perfectly possible for them to start as a new entrant in the new employer's scheme, without any accrued rights coming with them.

36. So the treatment of **future** service and **past** service should be seen as separate issues.

² Under the Preservation of Benefits Regulations (SI 1991/167) these have recently been amended so the reference is to the position at the time these transfers take place.

MAIN RESEARCH FINDINGS

WHAT HAPPENED IN PRACTICE

37. Interviewers asked both transferors and transferees

- whether any pension conditions, such as providing equivalent pension benefits, were attached to the transfers;
- whether the acceptance of transfers in of the accrued pension rights of employees being transferred was made a condition of the TUPE transfer;
- whether eligibility conditions were required to be relaxed; and
- the reasons that any conditions had been applied by the transferor?

Table 5 gives the results.

38. Six **transferors** attached conditions (including the one who attempted to do so but where the transferee failed to comply), the reasons were essentially company policy, along with trustees' wishes in one case. More specifically, the transferor in the financial services industry commented on general expectations in the sector, so that any transferee would expect the same; three others commented that it was "good business practice". Another made the point, echoed in rather different words by others, that "We want existing employees to know that we will protect them if any business is divested. If they didn't and they found out that we were selling companies without these safeguards for a particular sale, we would have industrial relations problems." In one case of a multiple sale, policy was pragmatic; if for some reason such as the size of the purchasing company, an equivalent scheme could not be set up, then an adjustment to pay or to other non-pension benefits was expected to make up the difference. In the one case where no conditions were attached the interviewee said that there was an "understanding that pensions were very important."

39. Of the **transferees**, those who had taken on businesses from the public sector, covered by their requirements (explained above) had accepted that they must provide broadly comparable benefits in these cases. Apart from this, the picture was patchy but the setting of conditions by transferors appeared to be rare, and it was up to the new owners to set up what arrangements they liked. The exception was Company I, the IT services company, which found that conditions were generally applied to both public and private sector purchases.

Table 5: Conditions attached to transfers

	Attached conditions	Transferring in conditions
Transferors		
Yes	5	6
Attempted	1	0
No	1 ("understanding")	1
Transferees		
Yes	3	2
Sometimes	1 (one out of several transfers)	1 (normally)
No	5	6

40. The question on acceptance of transfer in of pension rights did not differentiate between transfers without the members' consent, and those with. However, for the reason explained

above, transfers of accrued rights without consent are very rare, and so almost certainly what was in question was whether members were **offered** the possibility of transferring in their rights, with the alternative being to leave a preserved pension with the old scheme (or, if the scheme was being wound up altogether, the purchase of an annuity).

41. In general, **transferees'** preferences were most often to bring people into their own pension scheme(s), sometimes with specific conditions. The most frequent reasons cited were ease of administration, and a desire for parity with existing employees. Company I commented that setting up a public sector type scheme was expensive and time consuming, but once it was there, "pensions was not an issue". One company, however, would decline to take over businesses where pension rights were to be maintained, mainly because of cost factors, and another had no pension scheme to accept such transfers.

WHAT TRANSFER VALUE?

42. Where transfers-in of accrued pension rights were accepted by transferees, they were asked on what basis transfer values had been accepted, whether they were enhanced to facilitate the transfer, and whether there was any sort of "package deal" of generous transfer value terms

43. As explained above, for a final salary scheme the minimum transfer value legally required, the **Cash Equivalent Transfer Value** (CETV), is not enough to buy the equivalent of full past service in the new scheme. For that, **the past service reserve** is required. In a money purchase scheme, the options would be for the full fund held in the member's name, or their fund with administration costs and the cost of death benefit deducted.

44. Of the **transferors**, five gave at least the past service reserve. One also included a share of surplus in what they passed on, but had ring-fenced it to ensure that it could only be used for the benefit of transferring employees for the next five years. In one case, less was being offered where there was a funding problem with the small schemes being transferred out. CETVs figured only where they would give a better benefit (in one case) or where the transfer was to a money-purchase scheme (in another case).

Table 6: Basis used for transfer value

Transferees	Amount transferred
Past service reserve	3 ³
Share of surplus	1
Cash equivalent	3
Not known	1
Not relevant	2
Transferors	
Past service reserve	2
Past service plus surplus	2
Past service reserve or CETV	1
Past service reserve with some exceptions	2
Money purchase full fund	1

(More than one answer in some cases)

³ One interviewee referred to "full money purchase fund" but analysis of the rest of his answers make clear that he meant the past service reserve (and a share of surplus in some cases).

ELIGIBILITY CONDITIONS

45. Respondents were asked whether eligibility conditions were required to be waived or relaxed.

46. All but one replied that they had, and the one negative came from a company where the details of the new owner's new pension scheme were still being worked out. It would indeed be a nonsense to offer special terms in a new scheme and then require people to wait, say, a year before joining it, so the waiver really follows on logically from the previous points. In one case, quoted as a typical example by Company M, the new employer re-opened a closed final salary scheme to allow in members transferred across.

ENHANCED PENSION RIGHTS WITH THE NEW EMPLOYER?

47. All but two of the nine **transferees** accepted transfer values, but the terms varied considerably. From the employees' point of view, the ideal is to have a "seamless" transfer, with year-for-year service in the previous scheme, and if possible extra credits if a surplus is shown. One scheme had it as policy that they would aim for a share of the surplus and give employees a part of this. Of the rest, it appears that one gave whatever the money purchase fund would buy, one gave only the values people would have had if they were early leavers from the previous, and the rest probably did give year-for-year service. Of the two that did **not** accept transfers, one had a policy of never accepting, and the other had no scheme to receive the accrued rights.

48. One **transferee** would threaten to walk away from negotiations if they did not get sufficient in the transfer value, (the past service reserve) to allow them to do this. They commented that their "whole stock in trade is the acquisition of people from other people. Having built up a good reputation as being fairly safe people to go and join, [if] suddenly a group of people end up being treated rather more shabbily... then that puts a dent in our reputation." The one company that would not take on accrued rights took the view that "we do not wish to take over any liabilities in relation to employee pension rights".

49. One multiple **transferee** had had a bad experience with a transferor who had sought to impose conditions on the accrued rights. "The vendor dictated how the credit would be calculated, as part of the terms of their sale. But their administration was not very good, so we're still waiting for their figures - and that's two years ago." They now had a problem, with people retiring and not enough information about what they should be given. The aim in the selling company had been to safeguard the members, the interviewee said. "As far as the trustees are concerned, they can say they've done what they should do - it just didn't work very well in practice." The vendors had, in effect, handed the problem over to them. Another had the experience of a vendor reneging on a deal to give a past service reserve, and providing CETVs instead.

50. Only three of the **transferors** answered "yes" to the questions of whether transfer values were enhanced or a package deal of generous transfer value terms offered. However, this probably reflects a lack of clarity in the question. From the evidence elsewhere in the interviews, and from the information about the level of transfer values paid, it seems likely that several others will also have given "year-for-year" transfers in the final salary schemes, provided the transfer is done within a deadline. Here again there was one example of a

transferee reneging, and having promised a new scheme and obtaining the past service reserve on that basis, setting up a GPP instead.

51. Only three interviewees answered the question of whether the effect of setting conditions was to lower the price for the business sold. None thought they did, though one said that it certainly narrowed the field of transferees, as there were "a number of people out there who are not prepared to meet the conditions, for instance when the lawyers tell them there is no need to".

Table 7: Enhancements provided for past service

Transferees	
Yes	3
Sometimes	1
No	2
Not known	1
Transferors	
Yes with deadline	3
Surplus ring fenced	1
No / not clear	3

TAKE UP OF MEMBERSHIP IN NEW SCHEME

52. Take up of membership in the new scheme, where one was available (a total of seven of the nine **transferee** companies), was generally high, reaching 100% in two schemes and over 90% in two more. One interviewee commented that their 60-80% take up was not only because the benefits were better but because the new pensions manager would go round and talk to people and make them aware of the scheme. Of the other two schemes, in one only 16 out of the 60 left in employment within a few months (out of 500) had joined, which may have been as much for employee relations reasons as for pensions reasons. In the other, only management were eligible and no figures were available for them.

CONSIDERATION OF PENSIONS ISSUES: TIMING

53. **Transferees** were asked at what stage in the discussions/ negotiations on the TUPE transfers pensions issues were considered. As Table 8 demonstrates, there was no clear answer, with some going in at the beginning, one "somewhere in the middle", others rather late on. Probably this partly reflects the fact that it is not the pensions managers who are in control of the pace of negotiations. One cry from the heart was a wish to be involved from the start of acquisitions "rather than being asked to pick up the pieces later." But his company, the respondent said, does not plan like this. Only two transferees, Company H and Company L, did not consider pensions at all.

54. The multiple **transferors'** answers tended to reflect a learning curve, with early poor experience of leaving the issue until later leading to pressure to deal with it early in later deals. At Company O, when a company was sold the management supplied a database of information including pensions, so it was seen at the same time as everything else. "I would try to get pensions sorted early because nobody wants it to surface later in the negotiations", the pensions manager commented. Another explained that there had been "horrendous" experiences early on. "The pensions department worked all night to get things sorted. Now we have wised up and have a fixed policy and deal with pensions early on". Three multiple

transferors had pro-formas or other standard documents setting out the pensions conditions so that they were available to prospective transferees from the beginning and one transferee commented that having such "seller's packs" was now common practice.

Table 8: Consideration of pensions issues: timing

Timing	Transferees	Transferors
Early	3	5
In the general process	2	2
Late	2	
Not specified	0	
Not at all	2	

POLICY ADOPTED

55. Respondents were asked what policy and approach they adopted. As can be seen from the table, most **transferees** wanted to bring people into their existing company schemes, but one was driven by the desire to keep costs down, and one by a policy of closing down schemes taken over. Out of the seven **transferors**, as table 9 shows, five used terms such as “equivalent” or “no less favourable”, while one spoke of ensuring that benefits were maintained. However, as company O put it, this was “if possible, with hard bargaining if necessary, but not at all costs.” Company B’s attitude was the firmest, saying that providing equivalent benefits was the “industry norm”. The seventh transferor spoke specifically of past service benefits, rather than future benefits. All these terms would have been used in a “broad brush” way, rather than with the Government Actuary’s more precise approach.

Table 9: Policy adopted towards pension in transfer

Policy	Transferees	Transferors
As far as possible ensure benefits maintained		1
Past service rights must be secure in transferee’s scheme or elsewhere		1
Equivalent/ no less favourable benefits		4
Equivalent benefits but not at all costs		1
Ensure equivalent benefits		
Keeping costs down	1	
Bring people into schemes	7	
Close schemes down	1	

56. Policy was determined in all but one case by the company as opposed to the trustees, and in general at quite a high level. The division between company and trustees is not clear-cut, though, since senior people in the company are very likely to be trustees. And as one interviewee commented, in the end the trustees' responsibilities are onerous, because they have to agree with the company's arrangements, or disagree and ask for more money.

57. There could be a difference of view between different departments of a company. The Company O pensions manager commented for instance that he wanted to get the best deal for staff, while others wanted to protect the deal." The role of outside advisers was clearly

important, especially lawyers and actuaries, and it is likely that they were consulted (without deciding on policy) in other instances also.

Table 10: Who decided policy

	Transferor	Transferee
Finance director/ corporate finance	2	1
Consultant/advisers	4	4
Trustees	3	3
Lawyers	2	2
Chief executive/managing director	1	1
Company secretary	1	1
Board level	2	5
Human resources function	1	2
Pensions manager	1	2

(most cited more than one)

CONSULTATION

58. Comparatively few companies in the sample were unionised, as was seen in Table 11.

59. This means that, in general, arrangements for future pension rights were not negotiated with unions. Among **transferees**, none had done so, though Company E thought there had been negotiations on the transferors' side. Among the **transferors**, Company B consulted the unions at every stage, and in some of the Company N businesses there had been "consultation rather than negotiation", while in Company P "their views would have been factored in".

Table 11: Union consultation

	Transferees	Transferors
Yes	-	1
Partly	1 (possibly by transferor)	1 consultation, 1 "factored in"
No	8	4

FACTORS IN POLICY AND APPROACH

60. Respondents were asked about the most important factors in the policy and approach adopted. Examples given by interviewees were legal advice, cost, trade union agreement, harmonious industrial relations, fairness.

61. Fairness and harmonious industrial relations, and wanting to be seen as a good employer, figured highly in the responses, however competitiveness and costs were mentioned as most important only by one **transferee** and one **transferor** (though these two, Company H and Company M, actually had very different policies). One company, Company B, made the point that it would not be a good thing to have a company in their own industry providing lower benefits. The company without a pension scheme said that the most important factor was "efficiency".

Table 12: Important factors in policy and approach adopted

	Transferees	Transferors
Fairness	2	
Harmonious industrial relations	2	
Cost/competitiveness	1	1
Efficiency	1	
Company policy	1	1
Parity with current employees	1	
Ease of administration	1	
Fair transfer value of benefits from past service	1	
Seen as good employer		3
Not going to let transferee undercut		1

(some cited more than one reason)

62. Interviewees with multiple sales or purchases were asked whether policy had changed during the process of sales. Some said it had, but mainly in terms of getting the pensions discussion in earlier. Company K commented that trustees had become increasingly involved as they became more aware of their responsibilities.

Table 13: Policy changes

	Multiple transferee	Multiple transferor
Trustees more involved	1	
Doing it earlier	1	2
No	4	1

INFORMATION ON THE TRANSFER

63. Questions were asked about information provided to prospective transferors and transferees before the transfer, and about further information requested. Some **transferors** appeared to be very open with financial and other information, while others were secretive. At times there was a very combative spirit. Three transferors refused access to the actuarial valuation - "a bit like showing someone your hand in poker" - as one said. However, the valuation is not a secret document and any scheme member can see it on request. On the other hand, one **transferee** pointed out that valuations were not important to them since most acquisitions are of parts of businesses rather than whole companies and pension funds. One multiple transferee stressed the difficulties that could be encountered with both public and private sector transferors. "With some people at the moment, who had previous service with [another organisation] the information is held by the state and we can't get access to it. In some cases we are having to make decisions about people, and we don't actually know [their service]." In the private sector "we've just signed a contract with [an organisation] and they wouldn't give us information about any of the staff until we'd signed the contract [age, sex, length of service, medical history]." Another transferee found that the transferor could not supply even a list of members. Because they were no longer its employees the transferor "did not seem interested", it reported. Company L, the multiple transferee who closed down schemes after its purchases, asked for no information (which does raise the question of how they act if there turns out to be a deficit in any scheme, though this was not pursued).

64. **Transferors** were asked whether the information was to hand, or had had to be specially prepared, and if there were any significant costs associated with the collating of

information or advice provided, for instance by consultants. The three who had found it expensive commented that the main cost was the actuarial work. Otherwise, as one manager commented, it was "mostly just a big photocopying job."

Table 14: Information given to potential transferors and transferees

	Transferees given	Transferors provided
Scheme details	4	7
Membership profile	4	7
Funding details (valuation)	2	4
Scheme accounts (SSAP24)	1	2
None	2	

	Unable to obtain	Refused
Funding (valuation)		3
Accounts		1
Membership details	3	

(Most cited more than one item)

INFORMATION TO EMPLOYEES

65. Interviewees were asked about the information provided to employees, and in particular whether they arranged for them to receive advice on their pension rights and options. All **transferees** had provided some information, and five transferees had held group meetings and seminars. Four had facilities for people to consult Independent Financial Advisors (IFAs) at no cost to themselves, though in one case no-one took up the offer. One pensions manager commented that he spent considerable time going around telling people about the scheme at some point during the transfer process. There were usually a couple of individuals with particular problems in each acquisition. In some circumstances the outside administrators of the pension scheme could provide advice through their IFA arm, at no cost to the employee, "but there is a gentleman's agreement that I don't abuse that." Another transferee illustrated the difficulties that could arise; their average workplace, he explained, had 15 staff, so that any meeting of more than four people would involve closing the site for the duration. Company L, the transferee who set about closing down pension schemes where they existed, provided no information to employees (though there are legal disclosure requirements on a scheme wind-up, which presumably they met when they reached that stage).

66. Three of the **transferors** were aware that the transferee had provided or probably would provide advice to employees. Two transferors said that it was up to transferees to provide information and one of these commented that he would never give that sort of advice, he only advised on the mechanism for transferring into new scheme. He would encourage but not press, the transferor to get an IFA to give advice. In the other cases, it appears to have been the transferor who was providing the advice. In four cases, IFA access was available, in one case through a hotline; in one further case it may be in future, and in one the transferees may have provided it. Such advice will probably have been limited to the topic of the transfer between schemes: **occupational** pensions do not have the same status under the Financial Services Act as personal pensions which require a full "fact find" before a sale is made.

Table 15: Information to employees

	Transferees	Transferors
Basic information	8	7
Group meetings	5	3
IFA available	4	4 (3 cases provided by transferee)
Advice only on transfer mechanism/ leaving		2
Too early to say		1
None	1	

POSITION OF PENSION RIGHTS IN THE TRANSFER

67. Interviewees were asked how important was the consideration of future pension rights in the overall transfer. Was it more or less important than pay and other considerations, other financial factors in the transfer, or market prospects? They were also asked whether pensions considerations were a significant factor in the transferee's willingness to acquire the business, and if so in what way. Finally in this section, they were asked about their own general attitude to the future pension rights of employees acquired (though in response to this, some transferors spoke instead of the transferees' attitude).

68. For three of the **transferors**, pensions were a "take it for granted" issue, while others gave it a degree of importance. Company O "tried to negotiate it out of the way early on in a vacuum, so that pensions seldom reached the negotiations proper". Company M said that pensions were more important than pay (though not of primary importance), while Company N said that in employees' minds, pensions came after pay and job security.

69. Although pensions were an integral part of the package in Company A, they became a significant factor only because of the funding deficit in two small schemes, which could be perceived as raising the purchase price of the business. However, the transferee did not see them as a significant problem since it was a major group with its own pension scheme. In Company O, some transferees were reluctant to provide equivalent benefits though they did so in the end. Only one transferor (Company N) specifically said that pensions provision was a condition of the sale, although one other commented that he could not say what would have happened without agreement on this issue being reached.

70. As for **transferees**, for most pensions were of marginal importance, however in the minority of cases they were significant enough to affect decisions on transfer. One (Company L) said pensions were not at all important. The very few employees taken on had raised no demur, being "just very glad to have a job". Another (Company H) would walk away from a potential acquisition where the transferor insisted on them taking on potential liabilities, and was willing to make provision only for those eligible to join its existing scheme (essentially management level staff), on the argument that to do so for others would push up costs. Company I, on the other hand, said that they might refuse to acquire if they could not get companies to transfer employees into their scheme on appropriate terms. For the rest, pensions mattered but were not an overwhelming consideration in deciding whether to acquire, with one commenting that cost was considered, but only as a marginal factor. Of those who rated the importance of the issue, two said that it was not as important as pay and conditions, one that it was less important than "other factors".

71. **Transferees** were also asked whether there had been more recent changes since the purchase(s). One had pension increases under discussion, while another had created a new scheme consolidating previous ones (though certain sections for acquired members remained outside this). Others had made no change.

Table 16: Importance of pension issues

	Transferees	Transferors
Not an issue - expected to provide/condition of sale		4 (+1 - some transferees not an issue, some demurred)
More than pay but not primary importance		1
Concentrated on securing accrued rights		1
Not significant in decision to acquire	4	
Significant	1	
Not at all (closed schemes down after acquisitions)	1	
Very important, could stop us acquiring	2	
Not considered because standard policy well known	1	

IF TUPE APPLIED

72. Interviewees were then asked what difference it would have made if TUPE had applied, either on a basis of "broadly comparable" benefits, or on some less stringent and more flexible basis. "Broadly comparable" is of course the term used by the Government Actuary's Department under their precise definition, as explained in para 13. However, only three of the interviewees had experience of a transfer from the public sector and so knew about its usage in this sense. For the rest, it is apparent from their answers that they are understanding "broadly comparable" in what one might call a layman's sense, more or less synonymous with "equivalent". With hindsight, it might have been helpful if we had provided details to the interviewees of what the Government Actuary's definition entails, before asking for a response to the question.

73. Of the **transferees**, broadly comparable terms (in the way they understood this term) would not have changed the decision to *buy* in five cases, but it would have had other effects. Two of the five commented that it would make administration more difficult ("a nightmare" in the case of one scheme with which they had been concerned, where employees had protected rights under a former nationalised industry scheme), and three thought the price paid might change. In addition, one organisation, Company L said that they would carry on acquiring, and would "have to find a way round it." They would probably need more information from consultants. Whether the requirement was "broad comparability" or a "less stringent" basis was not felt to make much difference, though this reflects the usage of the term as understood by the respondents.

74. The two **transferees** who thought differently in terms of the decision to buy included one (Company H), who said they were unlikely to accept transfers on this basis, unless equivalent requirements were imposed on their competitors - often small local companies without pension provision. The less stringent basis was, this interviewee thought, effectively what existed already. "We have complete discretion and that suits us well." The other interviewee who thought it might make a difference made the point that while terms currently affected by TUPE are short-term, pensions are much longer term.

75. Of the **transferors**, five thought that applying TUPE terms would not have made a difference to the way they had handled things, though one of these thought it would have made the exercise more expensive. In contrast, one of the other transferors thought it would have been a deal breaker that would have reduced the price paid for the business, and could have been critical even on the less stringent basis. The other answer appeared to assume that this would mean a requirement to take on past service liabilities as well as make a future commitment. Again, as with the transferees, there were questions about whether the TUPE approach was the right one. One respondent (Company B) said that while it was a good thing in principle, it would be very difficult in practice, for instance if people were to go from a non contributory final salary to a company with a contributory money-purchase scheme. "It isn't going to work to try and force the transferee to set up a new final salary scheme". This same respondent wondered what on earth a "less stringent" method could mean, other than saying that a minimum level of provision must be made. Another made the point (explored further in the next section) that the way to deal with the issue was by dealing with the total remuneration package.

Table 17: Effect on decision to buy

	Transferees	Transferors
Broadly comparable terms would not have affected decision to buy	5 (2 make administration more difficult, 3 price might change)	5
Would have affected decision	2	1
Would find some way round it	1	
Broadly comparable would have affected, less stringent would be alright	1	1

OTHER COMMENTS

76. Respondents were asked what other pension considerations were relevant to the TUPE transfers they had done. A number of points were raised.

- Company B spoke about the position of unfunded schemes, and also said that on their outsourcing transfers, the companies buying these had not been prepared to match benefits, since they were non-pension companies. In the one case where there was no pension scheme - with caretakers - this employer had arranged personal pensions on staff terms, with virtually no charges and a pay increase before transferring to allow for contributions. They also provided independent financial advice.
- Another respondent described how he had been able to put pressure on a particular employer to provide the right sort of benefit by threatening to cut the transfer value and tell the members.
- Another pointed out that the "residual" schemes for former nationalised industries worked well. By this, he meant schemes such as the Coal Industry scheme and the Railway Pensions Scheme, where companies which have taken over parts of the industry belong to "industry-wide" arrangements providing pensions for those previously employed by British Coal and British Rail.
- Another, however, found the fact that they had members in these schemes an irritation, as it put pensions for some employees beyond their control. One pointed to the role of pensions committees and trustees.

- The smallest company in the study pointed out that because of the company's size, it would not make sense for it to run any elaborate pension scheme.

77. When asked whether they had other points to make on the specific issue of bringing pensions within TUPE regulations, there were many comments, some of them voluminous. Some were strongly opposed to any further regulation in this area, either on principle or for practical reasons.

- Company L were "appalled" by the idea that pension arrangements of employees taken on under TUPE would have to be transferred even if they were to be made redundant immediately. They, and another transferee, commented that they would "find a way round it".
- Several comments raised the question of the effect on small firms, which they speculated would effectively be shut out of the acquisition market, with businesses closing as a result. (Although these comments, coming as they do from representatives of larger firms, **are** speculative, it should be remembered that interviewees and their employers had had considerable dealings with smaller firms, either as transferees or transferors of businesses.)
- Two raised the question of the extra cost, in an outsourcing market where margins were small and the principals were chiefly concerned to save money. Others felt it was a logical step, though still worried about practicality.

78. One **transferor** commented that although pension schemes are designed with similar ends, within the trust deeds themselves the benefits are so inherently different it would be almost impossible to set up mirror image schemes. The interviewee had sympathy with people whose pension rights are changed mid-employment, but pointed out that there was no legal requirement at the moment for companies to provide pension benefits anyway. The burden of expense of having, say, 25 different pension schemes in the same company would probably encourage companies not to have pension arrangements at all, because of the cost of administration.

79. The point was made by four people that if the Government were to impose a minimum standard on everyone, or require employers to provide schemes, this would change the picture. One person floated the possibility of stakeholder pensions acting effectively in this way. Those involved with outsourcing felt that it would be useful to have a "level playing field", since at present those who made no provision could undercut those who did provide pensions.

80. One comment suggested a different solution - indexing deferred pensions to earnings, (rather than prices with a ceiling), and offering transfer values on that basis; another also thought that there should be legislation to ensure that more than the bare minimum was offered as a transfer value.

Table 18: Views of bringing pensions under TUPE

	Transferees	Transferors
Would seem logical/ make no difference to us	1	3
Exact equivalence impractical, broad comparability OK	1	1

Strongly opposed	3	
Would be a problem for small companies	1	3
No comments	2	
Tie in with basic provision like stakeholder/ if employers required to provide pensions, otherwise impractical	1	3

(several gave more than one answer)

81. The final question was about other points to be made on the more general issue of dealing with accrued and future pension rights in business transfers. Particular comments made here included the difficulty of obtaining proper disclosure without standard requirements, legal problems about position of retirement age in the contract, need for simpler regulations and administration, and the need for general guidance to start companies off in doing a transfer. One transferee made the point strongly that the Government needed to standardise its own approach. "Currently each public sector transfer to a private sector scheme is dealt with on an unique basis.

CONCLUSIONS

82. As pointed out above, this research study is based on a small sample which must not be regarded as representative. Certain conclusions can be drawn, but should not be applied too widely;

— Out of the 16 companies studied, the large majority (14) felt they did their best to provide equivalent benefits or better when purchasing or selling companies. With **transferees**, this was generally through inclusion in their own scheme, while for **transferors** it was through a wider variety of means. This was generally because they had a concern about their employees and wanted to be seen to be acting fairly. One company provided a "broadly comparable" scheme when required in taking on a public service contract, but not otherwise, and made no provision for the vast majority of its staff, and one systematically closed down pension schemes and left those (very few) people taken on to make their own provision with a matching contribution. Only three interviewees had experience of the Government Actuary's "broad comparability" approach.

— A difference between the transferors and transferees is that transferors generally **did** impose pension conditions on sales, whereas transferees found that few of those whose businesses they had acquired did so. This probably reflects size as much as anything else: the transferors in the study were large companies pursuing an organised programme of disposals, while the transferees in the study were large companies buying up a series of small businesses.

— Three interviewees had not succeeded in making the provision they had intended for transferring employees, in two cases because the other party reneged on a deal they had made. Such actions would presumably be outlawed if legal standards were introduced.

• There is little standardisation of approach, whether on what is given on transfer values, what information is passed between transferees and transferors, or what information and advice employees are given.

— If TUPE had been extended to pensions, most companies in the sample felt they would probably have coped in recent transactions, however reluctantly, though two would "find a way round it". There were concerns about practicality especially if a mirror image approach was adopted. There was also feeling that it might "freeze" the acquisitions market.

— There are other changes which will affect this area. In one case the majority of manual staff were not eligible to join the new owner's scheme because they were part-timers and low paid, and therefore whatever happens on TUPE, the position will change for them once the Part Time Workers' Directive comes into force. The forthcoming requirement on employers to give access to stakeholder pensions will also be important.

— A number of respondents suggested that the scenario would be very different if pension provision was made compulsory, and one very experienced pensions

manager felt that the solution lay in improving the early leaver requirements (so that deferred pension increases were based on earnings not prices).

