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pensions reform

Trigger Happy TPR?

The Pension Regulator's Code of Practice on scheme funding is at pains to stress that the new statutory funding objective (SFO) is not just "son of MFR", but is scheme specific with the trustees taking the leading role. However, the Regulator's role and attitude in policing compliance will be crucial to the viability of this approach. With this in mind we look at the Regulator's recently published Guidance on "How the Pensions Regulator will regulate the funding of defined benefits".

Scheme Funding

A quick recap

- SFO requires a defined benefit scheme to have "sufficient and appropriate assets to cover its technical provisions" (namely, from the EC Pensions Directive, "the amount required, on an actuarial calculation, to make provision for the scheme's liabilities").
- If SFO is not met the trustees, with actuarial advice, will have to devise a "recovery plan" setting out proposals to make up the shortfall.

Regulator's trigger-based approach

- The Regulator's approach is governed by its statutory objectives of protecting the benefits of members of occupational pension schemes and reducing the risk of calls on the Pension Protection Fund (PPF).
- In order to improve scheme funding to facilitate these twin aims, the Regulator has set a trigger point approach to identify schemes "presenting the greatest risk".

The triggers

- The first trigger (and the Regulator's primary focus) will be whether the scheme's technical provisions have been calculated using methods and assumptions that are prudent "given the scheme's circumstances".
- The second trigger will focus on the recovery plan put in place by the trustees.
- Schemes will also come to the Regulator's attention through other routes such as clearance applications, notifiable events and whistle-blowing.

Technical provisions

Primary trigger

- In making the initial assessment as to the adequacy of the technical provisions, the Regulator will compare these with the range between the PPF levy target for the scheme (the section 179 valuation) and the company's accounting standard (FRS 17 or similar). The trigger point between these two figures will depend on the scheme's maturity and the employer's strength.
- The Regulator's decision to drop the focus on buy-out levels will be welcomed. But the buy-out figures may still be used as a "sense check".

Recovery Plans

Triggers

- The triggers for the Regulator to investigate the scheme will be where the recovery period is:
  - longer than 10 years;
  - back-end loaded (i.e. contributions are higher at the end of the period); or
  - based on assumptions (particularly investment assumptions) which appear inappropriate.
- But the Regulator may also look at a scheme if it believes the deficit can be paid off more quickly (particularly if the employer is weak or weakening).

Recovery Plans

More flexibility

- For companies with a poor or weak covenant, the Regulator has said that it will focus on the "impact any change to the recovery plan may have on the employer's viability, including its ongoing ability to fund the scheme and its [long term] health".
- And there is good news for stronger companies too – unless there is another trigger, the Regulator "does not intend to focus its attention on schemes where the recovery period is set at less than ten years". Originally, it had seemed that these companies might be required to meet the deficit over a shorter period.

Conclusions

- The triggers are (in the Regulator's own words) "primarily a mechanism for the Regulator to focus its resources. They are not and should not be seen as targets for pension schemes".
- But if the Regulator does identify a scheme where the trustees have taken "imprudent or inappropriate" funding decisions, it says that a further assessment will be undertaken.

This edition of Sackers Extra News is part of a series focusing specifically on Pensions Reform to keep you abreast of the key issues throughout this period of change.

SACKER & PARTNERS

Solicitors specialising in pensions law

Sacker & Partners LLP
29 Ludgate Hill
London EC4M 7NX
Tel 020 7329 6699
Fax 020 7248 0552

enquiries@sackers.com
www.sackers.com

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