Sackers extra

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S07

Abbreviations commonly used in 7 Days

Alert/News: Sackers Extra publications (available from the client area of our website or from your usual contact)
DB: Defined benefit
DC: Defined contribution
DWP: Department for Work and Pensions
ECJ: Court of Justice of the European Union
FAS: Financial Assistance Scheme
HMRC: HM Revenue & Customs
NAPF: National Association of Pension Funds
NEST: National Employment Savings Trust
PPF: Pension Protection Fund
TPR: The Pensions Regulator

LEGISLATION

The Taxation of Equitable Life (Payments) Order 2011

Individuals who were adversely affected by maladministration in the regulation of the Equitable Life Assurance Society before December 2001 may be entitled to compensation from the Equitable Life Payments Scheme (the Scheme).

This Order provides that payments from the Scheme will be disregarded for the purpose of tax liability and entitlement to tax credits.

Further information can be found in the Explanatory Memorandum which accompanies the Order.

DEPARTMENT FOR WORK AND PENSIONS

State Pension Reform: Summary of responses to Green Paper

On 27 July 2011, the Government published a summary of responses to its April 2011 consultation[1] on the following options for reforming the state pension system:

- faster flat rating of the State Second Pension (S2P) with S2P remaining separate from the basic State Pension; and
- a single tier pension, combining the basic State Pension and S2P into one.

The summary indicates that the vast majority of respondents are in favour of a single tier State Pension, but consider that the implications for the ending of contracting-out (the inevitable result of the introduction of a single tier pension) need to be carefully managed.

The consultation also considered options for a more automatic mechanism for future changes to SPA. Responses suggest that a review process would be preferred, rather than directly linking SPA to longevity statistics.

No conclusions have been drawn by the Government in the response, but we expect a White Paper and full Impact Assessment to follow.

DWP Press Release

[1] Please see our Alert: "A State Pension for the 21st Century?" (6 April 2011)

Workplace pension reforms evaluation strategy

The DWP has published an "Evaluation Strategy" which is designed to provide a framework for assessing the effects of the workplace pension reforms which will start to come into effect in 2012.

The DWP's evaluation of the reforms will feed into the statutory review of NEST (which is due in 2017) and any subsequent changes in regulations.

Occupational Pension Schemes (Assignment, Forfeiture, Bankruptcy etc.) (Amendment) Regulations 2011

As we reported in 7 Days on 25 July 2011, regulations have been laid before Parliament which allow a member to agree to a surrender of their rights under a pension scheme for the purpose of meeting an annual allowance (AA) charge from their pension benefits (known as "scheme pays").

These regulations were finalised following a consultation which addressed exemptions to the provisions in section 91 of the Pensions Act 1995 that would otherwise prevent schemes from meeting AA charges from scheme benefits. The DWP's response this consultation was published 28 July 2011.

EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY (EIOPA)

Report on Market Developments 2011

EIOPA has published its latest report on Market Developments, which provides a general overview on the development of cross-border pension arrangements.

The report indicates that in the twelve months to June 2011, eleven new cross-border arrangements have been reported, while five schemes ceased cross-border activity during the same period. The UK and the Republic of Ireland continue to lead the way, having registered the greatest number of cross-border arrangements.

DC Project: Risks and risk mitigation mechanisms

The move away from DB pension provision and the increasing importance of DC is a trend which is replicated across Europe. EIOPA is carrying out a project which is designed to map out the risks for members of DC schemes and to ascertain what tools are in place in EU Member States to help members make their best individual decisions.

The project covers the three phases of the life-cycle model (joining, accumulation and payout) and consists of two stages:

- Stage 1 focuses on "pure" DC occupational pension schemes (those where no guarantees are provided) mapping out the risks borne by scheme members.
- Stage 2 presents an analysis of selected risks and the related risk mitigation mechanisms which Member States have in place. This stage takes account of all occupational pension schemes, to gauge the extent to which risk mitigation mechanisms can be used for DC schemes with guarantees, hybrids and DB schemes.

HM TREASURY

Public sector pensions: Government consultation on proposed pension contribution changes

On 28 July 2011, the Cabinet Office, the Department for Education and the National Health Service published consultations on pension contribution increases for civil servants, teachers and NHS staff for the financial year 2012/13.

The proposals form part of a package of reforms to public sector pensions which are currently under consideration. The increases are broadly equivalent to those expected under the "cap and share" arrangements which were agreed with Unions in the 2009 Pre-Budget Report.

Protections for the lowest paid mean that those earning less than £15,000 will see no increase, while those earning between £15,000 and £1,000 will have their increase capped to 0.6% (before tax) in 2012/13. The maximum increase in 2012/13 will be 2.4%.

It is estimated that approximately 2.5 million public service workers will be affected.

It is expected that further proposals, resulting from scheme specific talks, will be published by the end of October 2011, as to how savings of £2.3 billion in 2013/14 and £2.8 billion in 2014/15 can be achieved.

HM Treasury Press Release

NATIONAL ASSOCIATION OF PENSION FUNDS

Revised table of pension sharing charges

The NAPF provides a recommended scale of charges for private sector occupational pension schemes to use when providing information on pension sharing orders.

Updated guidance, which includes a flowchart illustrating the circumstances in which charges can be made, was published on 22 July 2011.

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT (OECD)

Pension Markets in Focus

The OECD has published the latest issue of "Pension Markets in Focus".

The key findings in this edition include:

- in 2010, pension funds experienced an average positive net return on investment of 2.7% in real terms;
- pension fund assets in most OECD countries have climbed back above the level managed at the end of 2007; and
- bonds remain the dominant asset class in most OECD countries, accounting for 50% of total assets on average.

THE PENSIONS ADVISORY SERVICE

Annual Review 2010/11

TPAS has published its annual review for the year 2010/11, covering the main areas of work for TPAS and highlighting typical issues dealt with by staff and volunteers.

The most popular questions concern the state pension system. However, TPAS also dealt with a variety of questions about private pension arrangements, from individuals wanting to gain a better understanding of their rights and entitlements, to those trying to trace old pension schemes.

TPAS Press Release

THE PENSIONS REGULATOR

TPR Statement: Identifying your statutory employer

DB scheme trustees need to identify their scheme's statutory employer in order to assess the nature and extent of the employer's legal obligations towards the scheme. These include, for example, meeting the scheme specific funding requirements, paying a section 75 debt and triggering entry to the PPF assessment period on insolvency.

Given the importance of this exercise, TPR published a statement on 28 July 2011 which is designed to help trustees with this.

From November 2011, TPR's Scheme Return forms will include a requirement that trustees identify the statutory employer for their scheme.

TPR Press Release

Automatic enrolment: online tools

On 28 July 2011, TPR released new online interactive tools to help smaller businesses to begin preparing for automatic enrolment.

TPR notes that by filling in basic information, such as their PAYE reference, the number of people they employ and salary information, employers can find out more detail about:

- when automatic enrolment will affect them;
- which staff need to be automatically enrolled into a pension scheme;
- how to automatically enrol staff; and
- how much they will need to contribute to their staff's pension.

The interactive tools are similar in style and format to TPR's existing online financial and budgeting tools.

TPR Press Release

WORKPLACE RETIREMENT INCOME COMMISSION (WRIC)

Report published: Building a strong, stable and transparent pensions system

Lead by Lord McFall, WRIC is an independent commission set up in early 2011 to look at the future of workplace retirement savings and how people use workplace retirement savings as income during retirement, to provide a review of retirement saving. WRIC's final report was published today (1 August 2011).

WRIC considers that an urgent review of the UK's pension system is required. The report notes that while the introduction of automatic enrolment (from October 2012) will be an important step forward, an estimated 5-9 million people (representing a third of the workforce) could still end up missing out.

The WRIC report therefore sets out 16 recommendations for reform, with seven key areas for the Government, employers, individuals and the pensions industry to focus on:

- *Adequacy:* Many people are not saving enough, and the 8% of salary minimum contribution set for automatic enrolment will be insufficient for many people. The Government should therefore work with employers to pilot ways of encouraging increased saving.
- *Charges:* Fee structures are currently too opaque, with high charges having a big impact on savings. New structures should be developed to allow bigger, low-cost pension schemes to operate.
- *Annuities:* These should be more flexible to ensure they meet changing spending patterns in old age.
- *Risk:* The Government should work with the industry to develop new products that help mitigate risk, and employers must be incentivised to take on a share of pension risk.
- *Small pension pots:* The Government should consider defaulting small pension pots into places where they can be managed efficiently. This includes NEST, which is currently banned from accepting transfers.
- *Cultural change:* Savings products must become more accessible. Employers need to be engaged through tax incentives and the creation of 'safe harbours' that allow them to discuss pensions more thoroughly with staff without falling into the territory of giving financial advice.
- *Stability:* A permanent, independent pensions commission should be established "to take the politics out of pensions".

WRIC Press Release

CASES

Houldsworth and another v Bridge Trustees Limited and another and Secretary of State for Work and Pensions (Supreme Court)

The Supreme Court's decision in this case was handed down on 27 July 2011. It addresses the dividing line between DB and DC benefits. How the benefit is classified makes a difference to the protections afforded by legislation. For this reason, the Government intervened in the case, sponsoring the appeal first to the Court of Appeal and then to the Supreme Court.

Background

When the winding-up of the Imperial Décor Pension Scheme (the Scheme) began in October 2003 it had a £40 million deficit. Originally a DB scheme, changes over the years had resulted in a varied and complex benefit structure. The original application to the Court was brought by the Scheme's trustees to determine how the statutory priority order on winding-up should be applied to the Scheme. (The case concerned the pre-2005 statutory order of priority on winding up - see our summary table for more information.)

The priority order establishes priority for payment where a scheme winds up in deficit. Where DB assets are insufficient to satisfy all the liabilities in a particular class they are applied across the whole class and any lower ranking class remains unsatisfied. Under the relevant legislation, "money purchase benefits" fall outside the statutory priority order.

The two benefits at issue in the appeal to the Supreme Court were not obviously DB or DC. They were:

- a money purchase benefit with a guaranteed investment return; and
- a pension benefit purchased in the scheme with a money purchase "pot" (known as an internal annuity).

In both cases a deficit could arise in the Scheme as a result of the provision of these benefits. The Government considered both these benefits to be DB in nature – its view being that a money purchase benefit can have no mismatch between assets and liabilities.

Decision

The Supreme Court disagreed. It concluded that:

- DC benefits with a guaranteed investment return could be "money purchase benefits" for the purposes of pensions legislation.
- DC internal annuities may also be characterised as DC not DB, both the investment and longevity risk being retained within the Scheme.

Comment

The DWP has issued a statement which explains that it intends to introduce retrospective legislation (at least to the date of the judgment) which will ensure that benefits which may create a funding deficit may not be classified as "money purchase". It is particularly concerned that members with these types of benefits may not have the advantage of protective legislation, such that relating to scheme funding, employer debt, the PPF and FAS.

Please see our Alert: "Bridge too far: DWP set to legislate" dated 28 July 2011.

Fuchs & Köhler v Land Hessen (Court of Justice of the European Communities)

The ECJ held that a compulsory retirement age of 65 for prosecutors was capable of objective justification.

Background

German Federal law requires that "Permanent civil servants shall retire on reaching the retirement age". The retirement age is determined by the individual States and is set at 65 in Hessen, subject to certain limited exceptions. (The law also allows retirement to be postponed for periods of no more than a year if this is "in the interests of the service", subject to an overall retirement age limit of 68.)

Mr Fuchs and Mr Köhler, state prosecutors, brought actions disputing the retirement age when their applications to work beyond age 65 were rejected.

Decision of the ECJ

The ECJ was asked to consider whether the retirement age for prosecutors was incompatible with, in particular, Article 6 of the Equal Treatment Directive[2] (age discrimination).

The ECJ concluded that a compulsory retirement age could be objectively justified as a proportionate means of meeting a legitimate aim. In particular:

- its aim of establishing a balanced age structure in order to encourage the recruitment and promotion of young people, to improve personnel management and thereby to prevent possible disputes concerning employees' fitness to work beyond a certain age was legitimate; and

- the setting of a compulsory retirement age did not go beyond what was appropriate and necessary to achieve the aim. Broadly, this was because a retirement age was the only means of ensuring that employment was distributed fairly among the generations (prosecutors are appointed permanently and rarely resign voluntarily and prematurely). Further, prosecutors are able to retire at 65 on a pension equivalent to 72% of their salary and are not precluded from finding alternative employment.

Can cost savings be a legitimate aim?

The German government asked whether an aim of "achieving budgetary savings" would be regarded as a legitimate aim for the purposes of establishing objective justification. The ECJ considered that such savings could underpin the chosen social policy of a Member State and influence the nature or extent of the measures it wished to adopt but that such considerations could not *in themselves* constitute a legitimate aim for the purposes of the Directive.

Comment

The case will be remitted to the German courts for a decision on the facts.

This decision provides useful guidance for UK employers on potential legitimate aims for justifying the use of compulsory retirement ages and seems to support some of those argued in the case of *Seldon v Clarkson Wright & Jakes* last year.

2 Directive 2000/78/EC

It would appear from its comments on cost as a legitimate aim for the purposes of establishing objective justification, that the ECJ still considers that such an aim would be insufficient on its own. This fits with current UK case law on the issue (see *Cross v British Airways*), and suggests that *Woodcock v Cumbria Primary Care Trust*[3] (in which cost alone was sufficient to prove objective justification) is confined to its own facts.

[3] [2010] UK EAT 0489_09_1211 (12 November 2010)