Sackers extra

05 March 2012

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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
FSA: Financial Services Authority
GMP: Guaranteed Minimum Pension
HMRC: HM Revenue & Customs
NEST: National Employment Savings Trust
PPF: Pension Protection Fund
TPAS: The Pensions Advisory Service
TPR: The Pensions Regulator

LEGISLATION

Abolition of DC contracting-out: Final regulations published

Contracting-out on a DC basis (protected rights) will be abolished with effect from 6 April 2012. Regulations were laid before Parliament on 29 February 2012. These regulations introduce an easement allowing trustees, by resolution, to remove "all or part of a scheme rule which makes special provision in relation to the protected rights of members", and which no longer reflects a statutory provision. Schemes will have until 5 April 2018 at the latest to make changes and may make amendments retrospective to 6 April 2012. These regulations may assist trustees in making rule amendments to remove references to protected rights.

Currently protected rights are subject to certain statutory restrictions. For example, protected rights have to be separately identified from non-protected rights and annuities derived from protected rights must provide for a survivor's benefit where the member is married or in a civil partnership. However, on 6 April 2012, any protected rights not yet in payment will become ordinary scheme benefits and all the statutory restrictions will fall away.

Schemes which are currently contracted-out on a DC basis will need to consider removing protected rights provisions from their trust deed and rules, as they will not be removed automatically.

Trustees should seek legal advice on whether any changes they require are covered by the regulations. For further information, please see:

- Sackers' Alert: "Abolition of DC contracting-out: final regulations published" (dated 1 March 2012);
- the explanatory memorandum which accompanies the regulations; and
- the DWP's response to consultation on the draft regulations.

PPF levy ceiling and compensation cap

Section 175 of the Pensions Act 2004 requires the PPF to set a levy for DB occupational pension schemes (and the DB element of hybrid schemes) to fund the compensation it will pay to scheme members if their employer becomes insolvent and the scheme has insufficient assets to enable it to provide benefits up to the protected PPF level.

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The Pension Protection Fund and Occupational Pension Schemes (Levy Ceiling and Compensation Cap) Order 2012 (which was laid before Parliament on 29 February 2012) imposes a levy ceiling figure of £918,854,855 on the pension protection levy for the financial year beginning 1 April 2012.

The order also provides for the level of the PPF compensation cap to be increased to £34,049.84 (up from £33,219.36) from 1 April 2012. This figure is based on a 2.5% increase in average earnings over the review period.

When applying the new compensation cap to members whose PPF entitlement is restricted to 90% of benefits (i.e. people below their scheme's normal retirement age), the maximum level of compensation payable to an individual at age 65 will be £30,644.86.

Further information can be found in the explanatory memorandum which accompanies the order.

Changes to pension scheme levy rates

The general levy for occupational and personal pension schemes meets the running costs of TPR, TPAS and the Pensions Ombudsman. The general levy rates have remained unchanged since 2008/09. Regulations will come into force on 1 April 2012 which provide that from 2012/13, the general levy rates will be reduced by at least 12%. This reflects the forecast yearly running costs of the relevant bodies.

These regulations will also provide for a reduction in the PPF administration levy, which meets the running costs of the PPF. The PPF administration levy rates have also remained unchanged since 2008/09 and from 2012/13 will be reduced by at least 25%. This is largely a result of legislative changes which have meant that since April 2011, certain costs which had previously been met from the PPF administration levy are now met out of the main PPF.

Further information can be found in the explanatory memorandum which accompanies the regulations.

Personal Pensions: Trivial commutation rules

Regulations have been laid before Parliament which amend the Registered Pension Schemes (Authorised Payments) Regulations 2009 by adding a further category of payment to the types of authorised payments which can be made by registered pension schemes that are not public service pension schemes or occupational pension schemes.

Currently, members of occupational pension schemes (who are aged 60 or over) already have the option of 'commuting' small pension pots of £2,000 or less as a lump sum. This right in relation to 'small pots' can be exercised in addition to the general rules on trivial commutation, under which members may take all of their pension savings as a lump sum if their aggregate pension savings are less than £18,000.

With effect from 6 April 2012, the ability to commute small pension pots of £2,000 or less will also be permitted from personal pension schemes. To prevent the abuse of this easement, an individual will only be able to take two such lump payments in their lifetime. However, it will be possible to make these payments regardless of the value of the individual's total pension savings and in addition to any trivial commutation lump sum payments or small pots paid from occupational pension schemes.

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Draft HMRC guidance on the commutation of small personal pension pots was published in December 2011. Final guidance is due to be published by HMRC once the regulations are in force.

Further information can be found in the explanatory memorandum which accompanies the regulations.

DEPARTMENT FOR BUSINESS INNOVATION AND SKILLS

Kay Review of equity investment: Interim Report published

On 29 February 2012, Professor John Kay published the Interim Report of his Independent Review to examine investment in UK equity market and its impact on the long-term performance and governance of UK quoted companies.

The Interim Report summarises the responses of the Review's call for evidence and presents a broad discussion of the issues raised, including:

- the purpose of equity markets, both economically and in facilitating stewardship and corporate governance;
- the company and the board, including Directors' duties, takeovers, voting rights and executive pay;
- performance measurement and the effect of financial reporting; and
- asset management, including the role of regulation in driving investment behaviour and the Stewardship Code.

The comments and proposals discussed signal areas of interest for the final report but do not represent its provisional conclusions - no recommendations are made at this stage. Professor Kay is due to present his final report, including recommendations for action, to the Secretary of State for Business in the summer.

Those wishing to submit further evidence in connection with the Review are invited to do so before 27 April 2012.

BIS Press Release

EUROPEAN UNION

Review of the EU Pensions Directive

On 1 March 2012, a public hearing was held on the proposed review of the EU Pensions (or "IORP") Directive.[1]

Addressing the hearing, Michel Barnier (European Commissioner for Internal Market and Services) outlined a number of reasons why a review of the Directive would help EU Member States benefit from a "more modern legislative framework better adapted to current socio-economic requirements".

[1] Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision

These included:

- sustainability of Member States' public finances;
- taking "better account of the specific characteristics of pension funds"; and
- maintaining a level playing field for regulatory competition between pension funds and insurance companies.

Barnier commented that although the Commission intends to draw on the approach of Solvency II, "there is no question of 'copying and pasting' this approach to the pension funds sector".

However, the review of the Directive continues to come under fire from those in the pensions industry. NAPF Chairman, Mark Hyde Harrison (who also spoke at the hearing), said that "The European Commission has completely failed to make the case for a new IORP Directive". And as a joint press statement published by the European Federation for Retirement Provision (EFRP) notes, these sentiments are echoed elsewhere in Europe: "it is dangerous to apply legislation made for insurance companies to IORPs. There are fundamental differences between them. Any effort to harmonise the regulatory regime is based on flawed logic and could have unintended consequences on pension plan members, IORPs and the economy as a whole by impeding growth and job creation."

European Commission Press Release

EFRP Press Release

NAPF Press Release

FINANCIAL SERVICES AUTHORITY

Consultation on proposed changes to pension transfer analysis

For FSA purposes, a "pension transfer" occurs when a pension is moved from a DB scheme to a personal pension scheme. On retirement, retirees can convert a personal pension fund into an annuity or draw money from the fund, known as income drawdown, to provide regular payments.

Current FSA rules set out how to calculate the benefits of a transfer that will be given up when members transfer to a personal pension – this process is known as the transfer value analysis (TVA). The TVA process compares the pension benefits from the DB scheme with those that could be provided by the personal pension scheme. The FSA considers the TVA to be a complex process and requires the full facts to be presented to the member before any action is taken. The starting point is always that such a transfer will not be in the client's best interests.

The FSA is consulting on changes to the TVA process to ensure that the assumptions used by advisers for the comparison are applied consistently by all firms, take account of recent UK and EU legislation, and use reasonable growth rates for illustrating the results of the comparison to the member.

The consultation closes on 27 March 2012.

FSA Press Release

HOUSE OF COMMONS

MPs vote against a return to RPI

In the Coalition Government's first Budget in June 2010, it announced it intended to use the Consumer Prices Index (CPI)[2] rather than the Retail Prices Index (RPI) as the measure for applying increases (both for deferred pensions and pensions in payment) to public sector pensions from April 2011. The switch was also later extended to private sector occupational pension schemes.

A proposal seeking to get MPs to force the Government to return to the RPI based calculation (which, historically, has generally been higher than CPI) was introduced to Parliament by John McDonnell (the Labour MP for Hayes and Harlington) and debated in the House of Commons on 1 March 2012. The debate came about after an e-petition on the switch from RPI to CPI received over 109,000 signatures (100,000 signatures are needed for an issue to be discussed in the Commons).

Following the debate, only 33 MPs voted to call on the UK Government to re-introduce RPI, with 232 voting against the proposal.

Meanwhile, the judgment of the Court of Appeal is awaited in a judicial review case brought by certain public sector unions on the Government's decision to switch from CPI. The application for judicial review was dismissed by the High Court in December 2011.

THE PENSIONS REGULATOR

TPR publishes strategy for auto-enrolment

Ahead of the introduction of automatic enrolment in October 2012, TPR has published its strategy for "maximising employer compliance" with the new duty.

In the strategy document, TPR sets out its approach to the regulation of employers and schemes, as well as how it intends to support the Government's pension reforms by "aiming to ensure that as many employers as possible comply, and encouraging those providing workplace pension schemes to provide safe, durable and value for money vehicles". TPR intends to maximise compliance by:

- providing employers, intermediaries and advisers with the information, tools and support they need to get to grips with the new duties;
- establishing a pro-compliance culture so that employers understand that the law is being applied fairly, that employers around them are complying, and that wilful or persistent non-compliance will result in a fine; and
- ensuring that effective systems are in place for detecting and tackling non-compliance.

TPR will also encourage the pensions sector to deliver schemes that encompass TPR’s six principles for good design and governance of DC schemes.

TPR Press Release

[2] CPI measures the change in a fixed basket of products and services. RPI is based on a fixed basket of retail goods, including some housing costs – particularly mortgage payments

TPR report on Uniq plc Pension Scheme

On 2 March 2012, TPR published a report setting how it worked with the trustee of the Uniq plc Pension Scheme (the Scheme), the Uniq Group and the PPF to address the scheme's funding problems while avoiding employer insolvency and PPF entry.

Background

The Scheme is an occupational pension scheme with approximately 20,000 DB members.

As at 31 March 2010, the Scheme had a deficit estimated at £431 million. It was clear to all parties that the Uniq Group would be unable to address the Scheme's deficit. TPR took the view that the employer covenant was extremely weak.

TPR's key principles

TPR's objective is to help employers and trustees identify whether a scheme is viable without a strong enough employer covenant to cope with the risk of the scheme's adverse funding performance.

A range of potential solutions was identified and considered, with TPR applying certain principles to test the merits of the different options in the context of this case. TPR considered whether:

- the scheme members and the PPF are significantly better off than if insolvency takes place;
- the scheme members and the PPF get a sufficient stake in the surviving business to ensure no exploitation of them post-restructuring. Where gain is available, the scheme members and the PPF get no less than a proportionate amount of this gain;
- the risks to the PPF are acceptable in the context of the TPR's broader duties to members as well as the PPF;
- the option demonstrates that proper account has been taken of the members' interests, especially where the risks have increased, and appropriate ongoing arrangements are in place to manage those risks; and
- costs are proportionate and fairly shared.

TPR's report notes that these principles reflect its thinking about how the legislative framework should operate and that they will guide its decision making in this area.

Regulatory action

Having considered the circumstances of the Scheme and the Uniq Group, TPR concluded that it could not use its powers under the Pensions Act 2004 to issue a contribution notice or financial support direction, as the key transactions and corporate events affecting the size of the Uniq Group had occurred before those powers were in place.

As a result, the trustee concluded that no viable scheme funding solution could be found and that the Scheme could never realistically expect to pay the full benefits promised to its membership without successful execution of an inappropriately risky investment strategy. TPR agreed and terms for a restructuring were negotiated.

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Early in 2011, TPR issued a clearance statement to facilitate the restructuring and gave approval for a Regulated Apportionment Arrangement (RAA). Under the RAA, the Scheme, via a special purpose vehicle, received the value of 90.2% of the equity in Uniq plc (then listed on the Alternative Investment Market) and also received a significant cash sum. The arrangement was backed by the Group's shareholders who considered that ownership of the remaining 9.8% of equity was better than receiving no value in the event of the Scheme's deficit bringing about insolvency.

Outcome

A cash offer of £113 million was made for the entire issued share capital of Uniq plc, which resulted in £100.8 million flowing to the Scheme. The trustee entered into a buy-in contract in December 2011, to ensure that members would ultimately receive benefits at least equal to PPF compensation levels from an FSA regulated insurance company.

As the value of the Scheme's assets at the PPF assessment Date (24 March 2011) exceeded its liabilities on the PPF funding basis, the trustee will now seek to secure member benefits above PPF compensation levels.

The Scheme will formally remain in an assessment period for the next six months, during which time the trustee must determine whether the scheme can wind-up outside the PPF.

TPR Press Release

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