Sackers extra

06 December 2010

At a glance

DEPARTMENT FOR WORK AND PENSIONS

- **Abolition of DC contracting-out: Consultation response published**
- **Working Paper No. 91: Pension scheme administration costs**

HM REVENUE & CUSTOMS

- **Consultation: Options to meet high annual allowance charges from pension benefits**
- **HMRC guidance on the reduced AA**
- **HMRC filing deadline**

NATIONAL ASSOCIATION OF PENSION FUNDS

- **NAPF Guidance: Stewardship Code**
- **Corporate Governance Policy and Voting Guidelines 2010**

THE PENSIONS REGULATOR

- **Employer covenant guidance finalised**

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
HMRC: HM Revenue & Customs
PPF: Pension Protection Fund
TPR: The Pensions Regulator

DEPARTMENT FOR WORK AND PENSIONS

Abolition of DC contracting-out: Consultation response published

The Pensions Acts of 2007 and 2008 paved the way for the abolition of contracting-out on a DC basis.

This year, between 28 July and 19 October 2010, the Government consulted on draft regulations which are designed to implement certain consequential amendments to give effect to the abolition provisions contained in those Acts, with effect from 6 April 2012. The consultation included four sets of draft regulations which are intended to amend or repeal references in legislation to contracted-out money purchase schemes (COMPS) and appropriate personal pensions (APPs).

On 30 November 2010, the DWP published its response to this consultation, setting out its comments in relation to the responses received. While the regulations predominantly deal with the consequential changes needed to give full effect to the abolition of DC contracting-out, key points arising from the Government's response include:

- *Transfers*

  The consultation proposed the removal of all references relating to transfers between contracted-out DB and contracted-out DC schemes. This was on the basis that contracted-out DC benefits would no longer exist from 6 April 2012 and, as a result, such transfers would no longer be possible.

  Transfers are currently permitted from a contracted-out salary related-scheme to another contracted-out salary-related scheme, to a COMP or to an APP.

  Responding to the consultation, Sackers and others raised the point that, post-abolition, members of schemes which are contracted-out on a salary-related basis would have fewer transfer options if the regulations were adopted as originally drafted. The inability to transfer contracted-out benefits to a DC scheme would have been a potential issue for any employers contemplating the option of de-risking by making available enhanced transfer values to members who transfer their benefits out of the scheme as well as for individuals wishing to transfer their benefits to another scheme.

  In its response, the Government states that "restricting transfers to the contracted-out environment beyond the abolition date would be inconsistent in policy and run counter to our overall pension simplification agenda. It would restrict the choice and flexibility that members currently have as to how they manage their pension provision." It also acknowledged the potential risk of creating an artificial transfer market in the run-up to April 2012.

As a result, the Government has decided to allow transfers from DB contracted-out schemes to non-contracted-out schemes post abolition and has amended the legislation accordingly. The DWP's response notes that the Government has introduced a number of safeguards "to ensure that members are aware of the implications of transferring, in particular that there will no longer be a requirement to provide for survivor benefit after transferring."

- *Switching the basis for contracting-out*

  In connection with DB schemes which are currently contracted-out on a DC basis, such schemes will be permitted to switch from DC to DB contracting-out provided they meet the requirements for contracting-out on a DB basis (in other words, that they can satisfy the reference scheme test). The response notes that they will need to take the necessary administrative steps with HMRC to obtain a new certificate confirming that it will be contracted-out on a DB basis, as the DC certificate will be invalid. There will be no transitional provisions.

- *Entrenched protected rights provisions*

  Sackers and others also raised the point that where a scheme contracts-out, the trustees are required to ensure that their rules incorporate appropriate contracting-out provisions. As a result, contracted-out DC schemes have generally included protected rights provisions in their rules. For such schemes, the removal of protected rights provisions from legislation will not automatically lead to their removal from particular scheme rules and they will need to take active steps to achieve this.

  While the draft regulations propose amendments to the requirements for alterations to the rules of contracted-out schemes under regulation 42 of the Occupational Pension Schemes (Contracting-out) Regulations 1996, they do not address the restrictions in section 67 of the Pensions Act 1995, which could cause difficulties for trustees and employers in connection with the removal of protected rights restrictions where they have been drafted into scheme rules. Similarly, schemes in this situation may encounter difficulties removing protected rights provisions from their rules if their amendment power prevents them from doing so.

  In its response, the DWP states the Government is not currently introducing a 'statutory override' in relation to the subsisting rights provisions of the Pensions Act 1995, "as that would not form part form part of the consequential amendments required by abolition". However, the DWP says that it intends to "look into this issue during 2011 to consider whether a statutory override is appropriate".

For more background information, please see our Alert: Abolition of DC contracting-out: consultation on implementing legislation dated 30 July 2010, and Sackers' response to the consultation.

Working Paper No. 91: Pension scheme administration costs

On 30 November 2010, the DWP published Working Paper 91, which presents the findings from research exploring the administrative costs of running occupational pension schemes.

The research was commissioned by the DWP and carried out by Ipsos MORI. The aims of the research were to inform the DWP about the range and scale of costs that private sector employers and pension schemes face, looking in particular at: internal costs; administrative costs; expenditure on professional services; managing funds; and the costs associated with having trustees.

Key findings from the research included:

- trustee boards of schemes with between 12 and 999 members tended to face higher running costs per member than trustee boards with more than 1,000 members;
- the annual cost of employing professionals was highest for investment managers at a mean cost per member per year of £63 and lowest for independent financial advisers (for members) at less than £1 per member per year; and
- the most commonly cited priority for deregulation was reducing the levies, followed by reducing scheme valuation/audit requirements. Respondents considered both the general and PPF levy to be a significant cost.

DWP Press Release

HM REVENUE & CUSTOMS

Consultation: Options to meet high annual allowance charges from pension benefits

On 14 October 2010, the Government published its plans for restricting pensions tax relief. These included its decision to reduce the Annual Allowance (AA) from £255,000 to £50,000 (for more information, please see our Alert: Restricting pensions tax relief: the verdict dated 14 October 2010).

The Government anticipates that most individuals and employers will want to adapt their pension saving behaviour and remuneration terms to ensure that their pension contributions remain below the AA. However, some individuals may still exceed the AA, particularly if they are long-serving members of a DB scheme with a generous accrual rate. The Government notes that in some cases, it is feasible that the charges will not be able to be met from current income. To address this, the Government is consulting on options to enable individuals to meet the charge out of their pension benefits. A joint consultation was published by HMRC and HM Treasury on 30 November 2010.

The consultation sets out two broad options for meeting AA charges from pension benefits, which would permit either:

- meeting a specific year's liability in real time, while pension benefits are still accruing; or
- rolling up the liability, deferring payment of AA charges until the point that the individual's pension benefits crystallise.

In both scenarios, the individual would be required to account for the charge on their Self Assessment tax return.

Other aspects of this approach being considered as part of the consultation include:

- the threshold above which an individual will be permitted to meet the AA from their pension benefits - the consultation suggests a level in the region of £2,000 - £6,000;
- whether individuals in DC schemes would have need of and/or make use of a facility to meet AA charges from pension benefits; and
- the treatment of individuals who are members of more than one pension scheme - the consultation proposes that individuals be permitted to elect a single scheme to pay the charge.

The consultation closes on 7 January 2011.

HM Treasury Press Release

HMRC guidance on the reduced AA

Alongside the Government's plans for restricting pensions tax relief, on 14 October 2010 HMRC published draft legislation for implementation of the reduced AA and draft guidance to help individuals and the pensions industry to understand the announced changes.

As HMRC has since received a number of queries and comments on the draft legislation and guidance, it has provided some clarification on a number of the issues which have been raised.

HMRC's latest guidance provides further information on:

- the carry forward provisions which allow individuals to set-off excess contributions due to one-off spikes in accrual against unused allowance from up to the three previous tax years; and
- the ability for schemes to align their pension input period to the tax year.

HMRC filing deadline

HMRC has issued a reminder to schemes who need to submit a Registered Pension Scheme return or an Event Report for tax year ending 5 April 2010. This needs to be done online before 31 January 2011.

NATIONAL ASSOCIATION OF PENSION FUNDS

NAPF Guidance: Stewardship Code

Launched on 2 July 2010, the UK Stewardship Code was published by the Financial Reporting Council and builds on the established Institutional Shareholders' Committee's Statement of Principles on the responsibilities of shareholders and agents. It is designed to set out the responsibilities of institutional investors as shareholders and provide guidance on how those responsibilities may be met. (For more information on the Stewardship Code, please see 7 Days dated 5 July 2010.)

Pension fund trustees and other investors are "strongly encouraged" to report if and how they have complied with the code.

The NAPF has now published guidance to assist investors, particularly pension funds, to meet their obligations under the code. In its guide, the NAPF encourages all pension funds to disclose publicly:

- whether they support the Code's Principles and to explain if they do not;
- whether reference is made to the Code in their Statement of Investment Principles and Investment Management Agreements;
- their process and frequency for reviewing, for example, their investment consultants and managers; and
- the investment managers used by the scheme and whether they apply the Code.

In addition, as the NAPF notes, in March 2011, the Financial Reporting Council will issue a report which includes a review of the policy statements disclosed by the investors who have signed up to the Code.

NAPF Press Release

Corporate Governance Policy and Voting Guidelines 2010

The NAPF has also published (on 30 November 2010) an updated version of its Corporate Governance Policy and Voting Guidelines to take account of the publication of the UK Corporate Governance Code (for more information see 7 Days dated 31 May 2010).

The main purpose of the NAPF's Corporate Governance Policy and Voting Guidelines is to assist investors in their interpretation of the provisions of the UK Corporate Governance Code when assessing a company's compliance with it.

THE PENSIONS REGULATOR

Employer covenant guidance finalised

On 30 November 2010, TPR published its finalised guidance on "Monitoring employer support: Covenant, contingent assets and other security" (the Guidance) together with its consultation response.

The Guidance is aimed at trustees and managers of all pension schemes with a DB element, and sets out the practice which it expects trustees to follow in assessing, monitoring and taking action on the employer covenant.

While the Guidance has not changed significantly since the draft was published for consultation in June, TPR has made some helpful changes in the light of responses to the consultation. (For more information on TPR's consultation, please see our Alert: "Employer covenant - first set of guidance issued" dated 18 June 2010.)

This guidance can also be read in conjunction with TPR's recently finalised guidance on DB multi-employer schemes and employer departures, on which we reported in 7 Days on 29 November 2010.

For more information, please see our Alert: "Employer Covenant: Final Guidance" dated 2 December 2010.

TPR Press Release

© Sacker & Partners LLP 2010

Nothing stated in this document should be treated as an authoritative statement of the law in any particular aspect or in any specific case. Action should not be taken on the basis of this document alone. For specific advice on any particular aspect you should consult the usual Solicitor with whom you deal. © Sacker & Partners LLP December 2010