Sackers extra

07 January 2013

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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
ECJ	European Court of Justice
FAS:	Financial Assistance Scheme
GMP:	Guaranteed Minimum Pension
HMRC:	HM Revenue & Customs
NEST:	National Employment Savings Trust
PPF:	Pension Protection Fund
TPR:	The Pensions Regulator

ASSOCIATION OF CONSULTING ACTUARIES (ACA)

Survey of pension trends in smaller firms

The final report of the ACA 2012 Smaller Firm's Pensions Survey will be published shortly.

On 2 January 2013, the ACA issued a press release with some details of their findings. For example, the survey demonstrates that contributions into smaller schemes run by smaller firms' – where these are present at all – are flatlining. Average combined pension contributions by employers and employees into DC schemes have remained static since the last survey in 2010 at 9% of earnings into trust-based schemes and just over 7.5% into contract-based schemes.

The ACA gathered responses from 344 smaller employers with 250 or fewer employees.

CABINET OFFICE

Mid-term Review

The Government has today, 7 January 2013, published its Mid-term Review. On pensions, the document says:

"Ensuring that our pensions system is fair and affordable, and provides dignity for our citizens in their old age is a priority for the Government. That means working towards a better, simple, single basic pension, protecting pensioners against erosions in the value of their pensions and introducing a new system which will encourage young people to put aside enough money for their old age."

The Review lists achievements such as the triple lock guarantee on the basic state pension and makes the following pledges on pensions:

- We will continue to roll out automatic enrolment into workplace pensions to help people make proper provision for their retirement, while ensuring that small businesses (with fewer than 50 employees) are not required to start enrolling employees until 2015.

- We will take forward legislation to put public sector pensions on a fair and affordable footing.

- We will put in place a new mechanism to ensure that the state pension age reflects future changes in life expectancy so that the state pension system continues to be sustainable and affordable.

- We will continue to protect the state pension through the operation of the triple lock guarantee for the duration of this Parliament.

- We will continue to keep our Coalition Agreement commitment to protect key benefits for older people throughout this Parliament.

- We will make it easier for people to use their pension savings by increasing the ‘drawdown limit’ to 120 per cent.

DEPARTMENT FOR BUSINESS, INNOVATION AND SKILLS

Government plans to update employment legislation

On 18 December 2012, Employment Relations Minister, Jo Swinson announced changes to collective redundancies rules which are aimed at helping employees and businesses.

The Government plans to:

- reduce the current 90 day minimum period, before very large scale redundancies can take place, to 45 days;

- legislate to make clear that fixed term contracts which have reached the end of their natural life are excluded from obligations for collective redundancies consultation; and

- introduce new non-statutory Acas guidance to address a number of key issues affecting collective redundancies consultation.

The changes will be made by secondary legislation. Draft regulations will be laid early in 2013 with the changes expected to be made by 6 April 2013.

DEPARTMENT FOR WORK AND PENSIONS

Automatic transfers and treatment of micro pots

On 15 December 2011, the DWP issued a consultation seeking views on proposals to improve transfers and deal with small pension pots.[1] In the response to the consultation,2 the Government confirmed that it would abolish DC short service refunds at the "earliest legislative opportunity" and would explore continuing to allow "micro pot" refunds.

[1] See our Alert: "Government consults on transfers and small pension pots" dated 19 December 2011

[2] See our Alert: "Improving transfers and dealing with small pension pots" dated 26 July 2012

The DWP has now written an open letter to the Society of Pension Consultants with its conclusion on micro pots.

The Government considers that, in practice, refunding a micro pot is more complex than first appears. In both trust-based occupational pension schemes and contract-based arrangements, any pot will have to be separated into employer contributions, employee contributions and tax relief granted by HMRC on those contributions. Once this has been done, the contributions will be treated differently according to the nature of the scheme, with employer contributions absorbed into the general fund, in the case of trust-based schemes, or refunded to the employer, in the case of contract-based schemes.

Furthermore, the DWP's analysis of the amounts which will have been paid by low, median and high earners in the three months following enrolment shows that even within such a short period of active membership people can build up pots which, although small, could well be worth transferring to future pension schemes.

The Government has therefore decided not to legislate for micro pot refunds; automatic transfer should be the norm, for pots of any size. However, the situation will be monitored as automatic enrolment rolls out and action may be taken later, if problems develop.

Government to introduce further protection for savers under automatic enrolment

On 19 December 2012, the Government announced that it intends to ensure that transitional arrangements designed for companies with DB or hybrid pension schemes are only used for workers that have access to defined benefits.

Current rules allow companies with DB or hybrid schemes to defer automatically enrolling existing staff until 2017. This is because the funding requirements for these types of schemes mean employers cannot take advantage of phasing-in of contributions, as can employers using a DC scheme.

The Government is acting to put beyond doubt its intention that people with access solely to a DC pension do not have their automatic enrolment deferred, even if they are in a hybrid scheme.

An amendment to the Pensions Act 2008 (which will be retrospective to the date of this announcement) will tighten the rules, ensuring that only employers offering DB to a jobholder, whether in a DB or hybrid scheme, will be able to defer automatic enrolment until 2017. Under the change, all eligible jobholders who do not have access to defined benefits must be automatically enrolled from their staging date.

Any firm that issues a notice to an employee with a DC pension to defer automatic enrolment will have to backdate employer contributions and give the employee the choice to pay back contributions if they would like.

Consultation: The Pension Protection Fund and Occupational Pension Schemes (Miscellaneous Amendments) Regulations 2013

This consultation seeks views on draft regulations which would make a number of technical and drafting changes to legislation governing the PPF as well as:

- make changes to the time limit for making an application for a review decision;
- give members the option to take their compensation early or late;
- clarify how assets are valued when amounts are owed to a scheme;
- allow the PPF, in certain circumstances, to discharge money purchase benefits to members aged 60 or over where those benefits are worth £2,000 or less; and
- make consequential changes to existing secondary legislation to reflect the introduction of funding determinations without valuations and requests for reconsideration without a protected benefits quotation.

The regulations also clarify the Pension Ombudsman's jurisdiction.

The intention is that the regulations will come into force on 1 April 2013.

The consultation closes on 29 January 2013.

FINANCIAL REPORTING COUNCIL (FRC)

Actuarial Standard TM1 updated

Following consultation, the FRC has published a revised version of actuarial standard TM1 (AS TM1) which sets out the assumptions to be used in annual statutory money purchase pension illustrations (SMPIs).

Changes have been made to:

- remove the cap of 7% per annum on the rate at which pension scheme investments are assumed to build up. Insurance companies and other providers will have to make justifiable assumptions about the investment returns that can be achieved taking account of the nature of members' investments. The FRC will monitor the assumptions used in SMPIs to assess the impact of the removal of the cap;
- require insurance companies and other providers to make justifiable assumptions about the investment returns that can be achieved, taking into account the nature of members' investments; and
- document the rationale used to determine the accumulation rate and provide this to members on request.

The FRC will also monitor the assumptions used in SMPIs to assess the impact of the removal of the cap. The new version of AS TM1 applies from 6 April 2013 with a transitional arrangement allowing compliance with the earlier version for illustrations with effective dates before 6 April 2014.

Positive uptake of UK Corporate Governance and Stewardship Codes in 2012

One of the conclusions in the FRC's annual report on its monitoring of developments in corporate governance was that the Stewardship Code has been a catalyst for greater engagement between companies and their shareholders in 2012.

The UK Stewardship Code was published in July 2010. It aims to enhance the quality of engagement between institutional investors and companies to help improve long term returns to shareholders and the efficient exercise of governance responsibilities by setting out good practice on engagement with investee companies to which the FRC believes institutional investors should aspire. There are now over 250 signatories to the Code, including most major institutional investors.

The FRC also found strong take-up by companies of the recommendations introduced to the UK Corporate Governance Code in 2010. Ninety-six per cent of FTSE 350 companies now put all directors up for re-election every year, and the majority of those companies will have the effectiveness of their board independently reviewed at least every three years. Overall compliance with the Code among listed companies of all sizes remains high.

Press release

HM REVENUE & CUSTOMS

FATCA: Update on implementation of the UK-US Agreement

Background

US provisions commonly known as the Foreign Account Tax Compliance Act ("FATCA") aim to combat tax evasion by US persons with non-US accounts. As the US tax system is based on citizenship, US persons do not need to be resident in the US.

FATCA requires financial institutions outside the US to report information on US account holders to the US Internal Revenue Service. If financial institutions fail to report the required information, 30% US tax would be withheld on all US payments to them.

Consultation

As part of its commitment to tackling tax evasion and increasing international tax transparency, the UK Government has signed an Intergovernmental Agreement to Improve Tax Compliance and to Implement FATCA (the "Agreement"). The Agreement represents a commitment by both governments to increase the scope of information that is automatically exchanged.

The Agreement exempts most UK occupational pension arrangements from the new reporting requirements.

In September 2012, HMRC published a consultation,[3] on how to implement the Agreement and sought views on its proposed approach.

[3] See 7days dated 1 October 2012

A response to the consultation, draft regulations and guidance were published on 18 December 2012. Comments on the draft regulations and guidance are requested by 13 February 2013.

VAT notice 700/17 Funded pension schemes

On 28 December 2012, HMRC published a notice to provide guidance on claiming input tax on funded pension scheme expenditure for both employers and trustees.

A funded pension scheme is one in which the employer and employees' contributions are vested in separate trustees who may be individuals or corporate bodies. It is normally separate and distinct from the employer's business.

This notice replaces the November 2012 edition. It has been amended to include guidance on the recovery of VAT on management costs by professional trustees who are appointed to run a pension scheme.

Pensions Industry Business Update

On 4 January 2013, HMRC published the fourth edition of its pensions industry business update. Among other matters it includes information on:

- how to find forms;
- current issues in relation to scheme cessation;
- auto-enrolment; and
- contracted-out salary related schemes and the effects of the abolition of DC contracting-out.

LOCAL GOVERNMENT PENSION SCHEME

Consultation on draft regulations on membership, contributions and benefits

This consultation seeks responses on draft regulations for the new Local Government Pension Scheme to come into force in April 2014. It covers the core elements of the new scheme, in particular the provisions relating to membership, contributions and benefits.

A second consultation exercise covering the remainder of the new scheme is due to follow shortly.

The consultation closes on 8 February 2013.

PENSION PROTECTION FUND

Levy determination for 2013/14

Following a consultation launched in September 2012,[4] the PPF has confirmed that the 2013/14 pension protection levy estimate will be £630 million, as originally proposed.

It has also published the 2013/14 Levy Determination which sets out the Levy Rules.

The PPF will reduce the levy scaling factor from 0.89 to 0.73, and the scheme based levy multiplier from 0.000085 to 0.000056, to raise this amount. This means that fewer schemes will have their levy capped.

The other rules used to set the levy will remain the same, except for a relaxation in the requirements for a guarantee from a bank, or from a custodian, so that in future an A-credit rating will be sufficient.

Alongside the Levy Rules, the PPF has updated guidance for putting in place contingent assets following informal consultation with stakeholders, to give a better steer to schemes on what to consider when planning to use guarantees as contingent assets. We will publish a newsletter on this shortly.

The key dates and deadlines for the 2013/14 levy year are as follows

- Information from scheme returns submitted by 5pm on 28 March 2013 will be used to calculate individual levies. TPR's Exchange system will continue to be the sole point of data submission for the purposes of the PPF levy and submissions can now be made.
- Insolvency risk will be measured using the average annual Failure Score of each sponsoring employer measured on the last working day of each month, from 30 April 2012 to 28 March 2013.
- The deadline for certification and/or re-certification of contingent assets will be 5pm on 28 March 2013.
- Deficit reduction contributions that have been made up to and including 31 March 2013 must be certified by 5pm on 30 April 2013.
- Full block transfers that have taken place up to and including 31 March 2013 must be certified by 5pm on 28 June 2013.
- The PPF will use market data over five years to smooth funding levels. For levy year 2013/14, it will use market data for each week day in the five-year period up to 31 March 2013.
- The date to which the PPF will transform section 179 valuations is 31 March 2013. These transformed values will be subject to smoothing and stressing.

[4] See our Alert: 2013/14 PPF Levy consultation dated 20 November 2012

THE PENSIONS REGULATOR

Larger schemes more likely to display DC quality features

On 3 January 2013, TPR published research which indicates that large DC schemes are more likely to display the quality features necessary for good outcomes for retirement savers than smaller schemes.

TPR tested for quality features in more than 300 trust-based occupational DC schemes in areas including investment, governance standards, value for money and communications to members by carrying out both quantitative and qualitative research. The findings show mixed standards across the trust-based DC landscape.

75% of large schemes have at least 15 of the 21 features tested present, compared with 51% of medium schemes and 18% of small schemes.

The findings are consistent with those of TPR's governance surveys, which show that small schemes with between 12 and 99 members and medium schemes with between 100 and 999 members generally display poorer governance than their large counterparts with 1000-plus members.

Later this month, TPR intends to publish for consultation its regulatory approach to trust-based occupational DC schemes, including a code of practice and supporting guidance for the governance and administration of trust-based schemes. This research has been used to inform its work on the code of practice and guidance.

CASES

IBM United Kingdom Pensions Trust Limited V IBM United Kingdom Holdings Limited; IBM United Kingdom Limited and Metcalfe

In a judgment delivered in October 2012, Mr Justice Warren found that the IBM Pension Plan's (the Plan) Trust Deed and Rules should be rectified to provide an entitlement for active members to retire between the ages of 60 and 63 without employer consent.[5]

The rectification did not extend to deferred members as the judge concluded their benefits were accurately reflected in the deed. This was despite the fact that, as rectified, the deed would not have complied with pre-Pensions Act 2004 preservation requirements.

In this connected case, the trustees claimed that the employer's failure to consent to an amendment to reflect the preservation requirements as they stood before 6 April 2004, in respect of pre-6 April 2005 service, was a breach of its duty of trust and confidence.

Preservation

The preservation requirements protect the rights of early leavers from pension schemes and ensure that, subject to a minimum service requirement, a deferred member receives a fair proportion (called "short service benefit" (SSB)) of what he or she would have received had he stayed in the scheme until retirement (called "long service benefit" (LSB)).

[5] See 7 Days dated 29 October 2012

Schemes must not contain any provisions that treat members less favourably for the purposes of SSB than they would otherwise be treated for the corresponding purpose for LSB.

Since 6 April 2005, the legislation has required SSB to be payable from an age no greater than 65, or normal pension age if later. Until then, SSB had to be payable from normal pension age or, if later, age 60. As the April 2005 change contained no transitional provisions, in the October IBM decision Warren J concluded that the Plan only needed to satisfy the requirements as they now stand, even where a deferred member's service includes service prior to the date the legislation changed.

Duty of Trust and Confidence

Warren J requested further written submissions on the duty of trust and confidence in his October 2012 judgement on this case.

Despite the fact that Warren J did not give a full judgment on what comprises an employer's duty of trust and confidence he did make four key observations:

- the employer's exercise of a discretion requires a "genuine and rational as opposed to an empty or irrational, exercise of the discretion";
- the correct test is not one of fairness. "Assessing whether a decision is irrational or perverse is not to be equated with the application of an objective standard of reasonableness";
- whatever the test is, it is a "severe" one. The conduct must be such to destroy or seriously damage the [employment] relationship; and
- the test is objective.

By way of an example, he explained that IBM would have been in breach of the duty had it simply refused to consent to a proposed amendment without even giving it due consideration.

Decision

The conclusion of Warren J's October 2012 decision was that the intention of both the employer and the trustees was to allow for payment of an unreduced deferred pension from age 63.

After these additional submissions, Warren J concluded that IBM was not in breach of its duty of trust and confidence in relation to its failure to consent to an amendment to the Trust Deed and Rules to reflect the pre 2005 preservation requirement for deferred members, as such an amendment would provide more than that which:

- it originally intended should be provided;
- the trustees originally intended should be provided; and

- the members were told consistently would be provided.

Warren J said:

> "The fact that, in the past, legislative provisions would have required provision of more, does not mean that more must now be provided when neither statute nor contract requires it."

Interestingly, he noted that, had an amendment been requested prior to the date the preservation legislation changed, it was "arguable" that IBM could have been compelled to consent: "IBM would then have been under an obligation (whether contractual or pursuant to its [duty of trust and confidence]) to bring about compliance with the preservation requirements as they <u>then</u> stood" (his emphasis).

Comment

Warren J's summary of the employer's duty of trust and confidence is useful while we wait for a more thorough examination of the issue in the next instalment of the IBM litigation. We understand that this case will reach the courts in February 2013.