Sackers extra

18 October 2010

At a glance

ACCOUNTING STANDARDS BOARD
- Accounting implications for retirement benefits of the replacement of RPI with CPI

CABINET OFFICE
- PPF, TPR and TPAS all survive Quango cull

DEPARTMENT FOR WORK AND PENSIONS
- Preserving powers to refund surplus - an update from the DWP
- The Occupational and Personal Pension Schemes (Miscellaneous Amendments) Regulations 2011
- DWP encourages people to trace forgotten pensions
- DWP research report: Evaluation of TPAS workplace visits

HM TREASURY
- Pensions Tax Relief Restrictions - Annual Allowance reduced

OFFICE FOR NATIONAL STATISTICS
- Inflation figures announced

THE PENSIONS REGULATOR
- TPR confirms agreement reached on funding EMI Group Pension Scheme

CASES
- The Lehman Brothers Pension Scheme: Reasons of the determinations panel
- Association Belge des Consommateurs Test-Achats ASBL and others

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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)
CPI: Consumer Prices Index
DB: Defined benefit
DC: Defined contribution
DWP: Department for Work and Pensions
ECJ: European Court of Justice
HMRC: HM Revenue & Customs
PPF: Pension Protection Fund
RPI: Retail Prices Index
TPAS: The Pensions Advisory Service
TPR: The Pensions Regulator

ACCOUNTING STANDARDS BOARD (ASB)

Accounting implications for retirement benefits of the replacement of RPI with CPI

In the Budget on 22 June 2010, the Government announced that CPI, rather than RPI, would be used for increases (both in deferment and to pensions in payment) to public sector pensions from April 2011. On 8 July 2010 the change was extended to private sector occupational pension schemes.

In the light of these announcements, the ASB has published a draft Urgent Issues Task Force (UITF) Abstract on the accounting implications of the replacement of RPI with CPI. The key issue for accounting purposes is whether the change gives rise to a different benefit or whether a different assumption is being applied to an unchanged benefit.

Comments on the draft Abstract are requested by 10 November 2010.

CABINET OFFICE

PPF, TPR and TPAS all survive Quango cull

On 14 October 2010, the Minister for the Cabinet Office, Francis Maude, outlined the Government's plans for substantial reform of a large number of public bodies.

The Government proposes to reform 481 Non-Departmental Public Bodies (NDPBs) or quangos (Quasi-autonomous non-government organisations). Of these, 192 will cease to be public bodies and their functions will either be brought back into Government, devolved to local government, moved out of Government or abolished altogether. In addition, 118 bodies will be merged down to 57, while a further 171 will be substantially reformed. After the reforms, it is intended that 648 public bodies will remain - down from the current 901.

The PPF, TPR and TPAS will be retained, on the grounds that they each perform a function which requires impartiality. The PO and the PPFO will merge to form a single tribunal. Although the PO and the PPFO are currently separate statutory offices, they are run as one body with the same person holding both posts.

The Financial Reporting Council (FRC) (the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment) will also be retained, although it will be substantially reformed, with its future reliance on government funding removed.

Cabinet Office Press Release

Full list of reforms to the Government's Public Bodies

PO Press Release

FRC Press Release

DEPARTMENT FOR WORK AND PENSIONS

Preserving powers to refund surplus - an update from the DWP

Prior to the Finance Act 2004, the then Inland Revenue had power under the Income and Corporation Taxes Act 1988 to require exempt approved occupational pension schemes to produce a valuation of their assets and liabilities on a prescribed basis. Where the scheme was more than 105% funded on that basis, the funding level had to be reduced in one or more ways (for example, by way of an employer or member contribution holiday, or a repayment of surplus to the employer, taxable at 35%).

The requirements dealing with excess surplus were removed from 6 April 2006 (A-Day) and, as a result, section 37 of the Pensions Act 1995 ("payment of surplus to employer") was revised to remove the reference to the previous tax legislation. Since A-Day, a return of surplus can be made to an employer from an ongoing scheme only if:

- the scheme rules permit such a payment;
- the power is exercised by the trustees; and
- certain prescribed conditions are satisfied.

Section 251 of the Pensions Act 2004 was introduced specifically to take account of the above changes. It provides trustees with a transitional power to preserve their current power(s) to return surplus and/or to amend such powers. (For more information, see our Alert: "Preserving powers to refund surplus" dated 24 May 2010.)

As section 251 is currently drafted, unless a resolution is passed before 6 April 2011, any such powers will lapse.

Following representations from many in the industry (including Sackers), on 14 October 2010, the DWP wrote to those who had contacted the department acknowledging the uncertainty about the scope and application of section 251. The DWP notes that while an amendment to clarify the position would require primary legislation, they "intend to amend the provision when a suitable opportunity arises, in order to ensure that it operates in a sensible and proportionate way. In particular [they] intend to make it clear that the provision does not apply to payments that would not themselves be subject to the overriding provision of section 37 of the Pensions Act 1995, and [they] also propose to extend the deadline for action by trustees by five years, to 6 April 2016." The DWP has yet to confirm in which Bill this amendment will be included.

Schemes need to be aware that there is a small risk that the DWP will not take action before the power to pass a resolution under section 251 lapses next April. (Likewise, the DWP's concession may conceivably depend upon the Coalition Government staying in power!)

However, we believe that it is reasonable for trustees to rely on the DWP's statement. In practice, those schemes with rules incorporating a section 37 power could pass a resolution as they will be caught even by a modified section 251. Indeed where such schemes have already begun the section 251 process by issuing a notice to members and the employer, there is no reason not to continue the process to its conclusion.

On the basis of the DWP's statement, we are satisfied that schemes which do not have section 37 powers can drop the issue.

We will be producing an Alert on the DWP's latest statement.

The Occupational and Personal Pension Schemes (Miscellaneous Amendments) Regulations 2011

The DWP has today (18 October 2010), launched a consultation on draft regulations which it intends will come into force on 6 April 2011.

The consultation proposes a number of minor amendments to regulations governing occupational and personal pension schemes, including:

- a change to the notification requirements where a "listed change" is proposed in a multi-employer scheme that would only affect members who work for that proposing employer - the draft regulations exempt the proposing employer from having to notify the other employers in the scheme of the proposed listed change;
- an increase, with effect from 31 March 2011, in the maximum fraud compensation levy on occupational pension schemes that can be raised by the Board of the PPF in respect of each financial year. The draft regulations propose an increase from 23p per scheme member (the rate set in 1997) to 75p per scheme member. The fraud compensation levy has been charged twice before - in 1997 and 2005. The increase is deemed necessary to allow the Board of the PPF to continue to manage the Fraud Compensation Fund effectively;
- an amendment to the Occupational Pension Schemes (Preservation of Benefit) Regulations 1991 to reflect the replacement of actuarial guidance note GN16 (transfers without consent) with principles based guidance; and
- an amendment to reflect the replacement of GN28 (adequacy of benefits for contracting-out) with principles-based guidance as the guidance which the Board for Actuarial Standards provides for actuaries needing to certify that a scheme meets the reference scheme test.

The consultation closes on 10 January 2011.

DWP encourages people to trace forgotten pensions

The DWP issued a press release on 12 October 2010, urging people who have lost contact with workplace pension schemes from previous employers, or personal schemes, to trace their pensions.

The Pension Tracing Service (part of the DWP's Pension Service) helps individuals to find occupational and personal pensions that they have lost track of. It uses a database with information on more than 200,000 pension schemes. The service provides contact details of the potential scheme administrator to enable customers to make subsequent enquiries.

A DWP survey of users of the Service indicates that around one in five customers found a forgotten pension after using the service. 68% of those who responded to the survey cited moving on from an employer as the reason for losing track of a pension.

DWP research report: Evaluation of TPAS workplace visits

TPAS is an independent, non-profit organisation, grant-aid funded by the DWP, which provides free information and guidance on UK pensions, including both state and workplace arrangements.

Alongside the TPAS website, leaflets, helpline and advisory services, TPAS also offers to visit organisations, where they deliver talks to groups in the workplace. The main aim of these talks is to explain to individuals how best they can plan for their retirement. The DWP's latest research report (published on 14 October 2010) presents the findings from an evaluation of these workplace visits.

The main findings of the research were that:

- TPAS workplace visits have a balanced and useful content and are well delivered. In particular the independence and personalised content and delivery offered by TPAS were valued by both the hosts and attendees;
- the workplace visits meet the aim of explaining to individuals how best to plan for their retirement, and appear to be inspiring people to do more, for example to budgeting for retirement;
- the cost efficiency of the visits is favourable when compared with that estimated for the workplace visits provided under the discontinued Pensions Education Fund. The research notes that this will improve further if TPAS meet their objective of maintaining the number of visits in 2010/11 while reducing their costs, mainly through increased use of volunteers; and
- visits should focus on where they can deliver most value for money, with improved targeting, and extending the scope of the visits to engage with harder to reach groups.

DWP Press Release

HM TREASURY

Pensions Tax Relief Restrictions - Annual Allowance reduced

On 14 October 2010, the Government published its final plans for the restriction of pensions tax relief.

Key points emerging from the Government's response to its July 2010 consultation include:

- the reduction of the Annual Allowance (AA) to £50,000, from its current level of £255,000. This figure is, however, higher than the £30,000 - £45,000 range originally proposed by the Coalition and, as such, represents a significant improvement, both on the previous Government's plans and the Coalition's original proposals[1];
- in what the Government recognises is a "stretching timetable", the new AA will apply from the tax year 2011/12 (when the existing anti-forestalling provisions will fall away);
- the LTA will also be reduced, to £1.5 million, but from April 2012 to allow a transitional period;

[1] For more information, see our Alert: "Restricting pensions tax relief: The Coalition's alternative approach" dated 29 July 2010

- individuals will continue to receive relief at their marginal rate (up to the AA), not at 40% as proposed in the July consultation;
- the factor used to measure "deemed contributions" will be increased from 10 to 16 from April 2011. Although this represents a big jump, it is at the lower end of the Government's proposed range of 15-20.

Provisions to enact the reduced AA and LTA will be included in the Finance Bill 2011.

For more information, please see our Alert: "Restricting pensions tax relief: the verdict", and follow the links below:

Written Ministerial Statement

HMRC Guidance

GAD technical bulletin

GAD report on setting the valuation factor

Draft legislation and explanatory note

OFFICE FOR NATIONAL STATISTICS (ONS)

Inflation figures announced

As noted above, in the Budget on 22 June 2010 the Government announced that CPI, rather than RPI, would be used for increases (both in deferment and to pensions in payment) to public sector pensions from April 2011. This change was subsequently extended to private sector occupational pension schemes.

The ONS has now announced that the rise in CPI for the year to September was 3.1%, whereas the rise in RPI was 4.6%. This figure is used for the Revaluation Order normally published in December. The Revaluation Order is used for public sector pension increases and certain increases in deferment. It is also used by some occupational pension schemes for increases to pensions in payment.

THE PENSIONS REGULATOR

TPR confirms agreement reached on funding EMI Group Pension Scheme

The Trustee of the EMI Group Pension Fund has reached agreement with the EMI Group regarding the long term funding of the scheme, the Regulator confirmed in a statement issued today, 18 October 2010.

Sacker & Partners LLP (Sackers) advised the Trustee during the negotiations - our press release can be read here.

CASES

The Lehman Brothers Pension Scheme: Reasons of the determinations panel of the Pensions Regulator in relation its determination to issue a financial support direction

Background

On 15 September 2008 Lehman Brothers Holdings Inc. filed for Chapter 11 bankruptcy protection in the United States. On the same date, the UK company Lehman Brothers Limited (LBL), went into administration. As at 1 January 2007, the buy-out deficit in the UK DB scheme, the Lehman Brothers Pension Scheme (the Scheme), was approximately £150m.

On 24 May 2010, TPR issued a warning notice of a financial support direction (FSD) against a number of companies in the Lehman Brothers group (the Targets) requiring support of the Scheme. TPR relied on the statutory ground that the principal employer of the Scheme, LBL, was "insufficiently resourced" on 15 September 2008.

Timing

For various reasons, the FSD warning notice was not served until 1 June 2010 on most of the Targets, and even later in some cases. The warning notice had a reply date of 21 June 2010. This was subsequently extended to 30 July 2010.

The solicitors for the Targets who were represented at the Determination Panel (DP) hearing in relation to the FSD (not all Targets were represented), applied for judicial review of TPR's actions. Immediately before the judicial review hearing, TPR handed over the matter to the DP. The DP set a new timetable – skeleton arguments were due by 31 August and the hearing was set for 8 and 9 September 2010.

Although this was not a significant extension, the timetable for issuing the FSD was acknowledged to be tight. Under the Pensions Act 2004 (and relevant regulations) TPR has to issue an FSD within 24 months of the date on which it alleges the companies were either service companies or insufficiently resourced. As TPR had set this date as 15 September 2008, that gave the DP only until 14 September 2010 to decide it was reasonable to issue the FSD.

The DP concluded that, despite the timing issues, the hearing had been fair "but only just". This was based on two key points – first, two firms of solicitors had in fact managed to put in substantial responses to the warning notices; and secondly, that the majority of facts were not disputed.

Decision

There were numerous Targets. In considering whether it is reasonable to impose an FSD to each Target, the key statutory test is whether the Target in question had received any benefit directly or indirectly from LBL.

The DP held that it was reasonable to impose an FSD on:

- the parent company;
- certain UK operating companies; and
- the parent companies of LBL.

The DP concluded it was not reasonable to impose an FSD on a number of other Targets as there was a "lack of particularised evidence".

Nevertheless, it remains unclear what proportion of the total deficit each Target will be liable for. The DP side-stepped this issue, concluding that "when considering whether to impose an FSD we need only to be concerned with the imposition of an FSD *simpliciter*, and need not make a direction giving specific figures or proportions."

Comment

In making its decision on Lehman Brothers, interestingly the DP specifically stated it is an executive committee of a regulatory body "not a judge or court".

No doubt with this in mind, the DP stood firm on preserving the flexible nature of the rules governing its conduct. In particular, it held back from offering hard and fast rules on disclosure of documents. Although the DP acknowledged the general rule is that the targets are entitled to anything on which the DP might rely on when making a determination, they did not want to be seen as "shackling" TPR's discretion in matters of disclosure. For instance, although the case will normally be "entirely contained" within the Warning Notice and supporting evidence, the DP did not see "in principle" that no further evidence should be admitted provided any target has a reasonable time to respond.

Association Belge des Consommateurs Test-Achats ASBL and others

The Advocate General (AG), Ms Kokott, delivered her opinion in this Belgian case on 30 September 2010. It addresses anew the question of whether it is unlawful to allow the sex of the insured person to be taken into account as a risk factor in the formulation of insurance contracts. This practice is expressly permitted in the UK under the Equality Act 2010.

Background

The European Gender Directive (2004/113/EC) (the Directive) was designed to provide a framework for combating discrimination based on sex in access to and supply of goods and services, with a view to putting into effect in the Member States the principle of equal treatment between men and women.

Article 5 of the Directive requires Member States to ensure that, in all new contracts concluded after 21 December 2007, the use of sex as a factor in the calculation of premiums and benefits for the purposes of insurance and related financial services shall not result in differences in individuals' premiums and benefits. However, under Article 5(2), Member States may permit proportionate differences in individuals' premiums and benefits where the use of sex is a determining factor in the assessment of risk based on relevant and accurate actuarial and statistical data.

The Belgian Government had taken advantage of the derogation provided by Article 5(2) in respect of life assurance contracts. Test-Achats (a non-profit making consumer organisation) brought an action for the annulment of that law before the Constitutional Court of the Kingdom of Belgium. It argued that the law was incompatible with the principle of equal treatment for men and women.

Questions referred to the European Court of Justice

As the law in dispute relies on an exemption set out in the Directive, the Constitutional Court decided it was necessary to refer the questions below to the ECJ for a preliminary ruling. This is because the ECJ alone has jurisdiction to determine the validity of its legislation.

- Is Article 5(2) of the Directive compatible with the fundamental principle of equal treatment and non-discrimination?

- If the answer to the first question is no, is Article 5(2) of the Directive also incompatible with fundamental rights if its application is restricted to life assurance contracts?

Opinion of the Advocate General

The AG considered that the use of actuarial factors based on sex is incompatible with the principle of equal treatment for men and women and that Article 5(2) of the Directive is therefore invalid. She was also satisfied that there is no reason to treat life assurance as a special case.

In reaching her conclusions, the AG explained that direct discrimination on grounds of sex is only permissible if it can be established with certainty that there are relevant differences between men and women which necessitate such discrimination. This is not the case where insurance premiums and benefits are calculated solely or essentially on the basis of statistics in respect of men and women. This practice involves a sweeping assumption that, for example, different life expectancies and different propensities to take risks when driving are essentially due to sex. In practice, many factors other than sex play an important role in the evaluation of insurance risks. For example, life expectancy is strongly influenced by economic and social conditions as well as the habits of each individual. Furthermore, as it is not lawful for a person's race and ethnic origin to be used as a ground for differentiation in insurance, it is equally inappropriate to allow such differentiation on the grounds of sex.

However, the AG was of the view that Article 5(2) should only be declared invalid for the future as, conceivably, millions of insurance contracts based on sex-specific risk assessments have been concluded since the Directive came into force. She also suggested that there should be a transitional period of three years to allow Member States to decide what action to take in respect of their domestic law and to give insurance companies time to adjust to the new legal framework conditions. Following such a transitional period, all insurance premiums and benefits would have to be neutral in terms of sex.

Comment

Although the ECJ is not bound to follow the Advocate General's opinion, it is unusual for it not to do so. Should the ECJ declare the Directive invalid in this respect, the effect on the purchase of annuities could be considerable.

The ECJ's decision is expected in 2011.