21 August 2003

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Winding-Up Defined Benefit or Hybrid Schemes Opra Update 3

1 BACKGROUND

The Occupational Pension Schemes (Winding-Up Notices and Reports etc) Regulations 2002 gave Opra new powers to monitor and intervene in the winding-up of occupational pension schemes and came into force on 1 April 2002. Based on its experience over the sixteen months or so since, Opra's latest Update discusses its views on some tricky issues which often arise when winding- up either defined benefit (DB) or hybrid occupational pension schemes.

The Update is aimed at trustees, advisers and insolvency practitioners and considers issues which are not straight forward, explaining how Opra expects trustees to address them.

2 THE MAIN POINTS DISCUSSED

Some of the key points emerging from the Update include the following:

- **Commencement of wind-up**

  If there are uncertainties as to whether a scheme has gone into wind-up or not, the trustees should resolve them. Opra Note 10 which was published in August 2002 also considers in some detail the uncertainties surrounding when winding-up is triggered and the need for trustees to lay an accurate paper trail.

- **Investment issues**

  Once winding-up begins, Opra expects trustees "to take immediate advice as to whether their previous investment policy remains appropriate".

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- **Minimum funding requirement (MFR)**

  Opra recognises that the priority for trustees and the scheme actuary following the start of winding-up centres on considering whether there are sufficient assets to secure members' benefits (and, if necessary, recover any debt from the employer(s)). Therefore, Opra will not normally insist on an MFR valuation being prepared every three years provided that Opra is given "appropriate assurances" by the trustees and the scheme actuary that the winding-up is progressing and steps are being taken to secure benefits. Trustees and scheme actuaries are also encouraged to contact Opra's winding-up team to discuss Opra's requirements relating to the specific circumstances of their scheme.

- **Eliminating deficits under section 75 of the Pensions Act 1995**

  Generally speaking, trustees decide at what point during the winding-up ("the applicable time") a calculation should be carried out of the scheme's assets and liabilities to determine whether a debt is owed by the employer(s). Opra suggests that, in deciding to have a debt certified by the actuary, trustees should consider factors such as whether the employer may be willing to pay voluntarily or "whether the likely recovery of any debt from an employer's insolvency outweighs the costs involved in its calculation". Opra also reminds trustees of their duties towards members in pursuing a debt so that as much money is recovered as possible and cautions them against being swayed by any conflict of interest.

- **Cash equivalent transfer values (CETVs)**

  Whilst a scheme's assets and liabilities are being confirmed, Opra will not normally penalise trustees who, acting on the scheme actuary's advice, do not quote CETVs within the statutory deadline (three months but with a long-stop of six months in certain circumstances). However, during this period, trustees should be "actively working towards resolving outstanding issues".

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- **Guaranteed Minimum Pension (GMP) equalisation**

  Always a thorny issue for trustees and their advisers, Update 3 sets out useful examples of approaches taken by other trustees (including, for example, a decision not to equalise). Although Opra stops short of endorsing any particular approach, it makes it clear that trustees who follow any one of the examples given will provide Opra with reassurance that they have acted honestly and reasonably. It remains to be seen what level of comfort trustees will derive from this in practice.

  That said, Opra also comments that the “cost and time involved in devising and implementing a methodology for equalisation may well outweigh the value in terms of benefit to members”. (Interestingly, it also suggests that “there is no clear obligation on trustees to equalise benefits where inequalities arise only from the impact of the contracting-out legislation”.)

- **Employer insolvency and appointing a statutory independent trustee**

  Opra tackles a number of points affecting schemes in these circumstances including the possibility of an independent trustee maintaining links with the previous trustees as they can provide essential background information about a scheme.

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