Sackers

Quarterly Briefing
December 2013

Highlighting significant developments in pensions law, covering key areas such as pensions reform, regulatory developments, new legislation and cases.

Quarterly Briefing December 2013

In this issue

On the front cover this quarter: Peter Murphy, Partner.

Abbreviations commonly used in the Quarterly Briefing:

AA: Annual Allowance

Alert: Analysis of topical developments in pensions (available from our website or your usual contact)

AVC: Additional voluntary contribution

CARE: Career averaged revalued earnings

CJEU: Court of Justice of the European Union

CPI: Consumer Prices Index

DA: Defined ambition

DB: Defined benefit

DC: Defined contribution

DCLG: Department for Communities and Local Government

DWP: Department for Work & Pensions

EEA: European Economic Area

EMIR: European Market Infrastructure Regulations

FP12: Fixed Protection 2012

FP14: Fixed Protection 2014

FCA: Financial Conduct Authority

ICAEW: The Institute of Chartered Accountants for England and Wales

IP14: Individual Protection 2014

LGPS: Local Government Pension Scheme

LTA: Lifetime Allowance

NAPF: National Association of Pension Funds

OFT: Office of Fair Trading

PO: Pensions Ombudsman

PPF: Pension Protection Fund

QROPS: Qualifying Recognised Overseas Pension Scheme

TPR: The Pensions Regulator

TUPE: The Transfer of Undertakings (Protection of Employment) Regulations 2006

Current Legal Agenda

The latest developments in DC are set out on pages 2 and 3

DC schemes

As the DC pensions universe expands and more individuals are brought into pension saving as a result of automatic enrolment, the Government, TPR and other pensions industry bodies are working to ensure good member outcomes in DC.

- TPR's new DC code of practice is due to come into force in November 2013 and will apply to the trustees of all occupational DC trust based schemes (including AVCs under occupational DB schemes).
- In September 2013, the OFT published the results of its market study on achieving value for money for members, following which a number of pensions industry bodies have agreed to take action.
- TPR and other bodies are consulting on various strands of DC pension provision. These include a cap on charges in automatic enrolment schemes, a draft assurance framework for master trusts, and quality standards for workplace DC schemes.

For details of the protections available on the reduction in the LTA please see page 5

Pensions tax

From April 2014 onwards:

- the AA (which limits tax relief on pension savings by an individual in a registered pension scheme in any given tax year) will be reduced to £40,000 from its current level of £50,000; and
- the standard LTA (the total amount of tax relieved pension savings that an individual can build up over their lifetime without incurring an additional tax charge) will be reduced from £1.5 million to £1.25 million.

Defined Ambition

The DWP has finally unveiled its plans for "defined ambition" pensions, setting out proposals for alternatives to the traditional DB and DC models of pension provision. The consultation covers various options within the DA sphere, including flexible DB, DC models that offer greater certainty for members by providing a guarantee but without creating a funding liability for the employer, and Dutch-style collective DC.[1]

Draft pensions directive awaited

European Union

A new pensions directive is on the European Commission's agenda. Since the review of the existing pensions directive was first announced, headlines had largely been made by the Commission's proposals to impose insurance style Solvency II funding requirements on DB schemes. Although these plans are on hold (for the time being at least), a draft of the new directive is still expected before the end of 2013. The main focus will be on governance and transparency.

Sackers' October 2013 Investment Briefing available now

Investment matters

EMIR sets out risk mitigation measures in relation to over the counter derivatives (OTCs) within the EEA. At the heart of EMIR is the requirement for central clearing of certain OTCs with newly established central counterparties, but the regulations encompass a range of different measures.

For more details of this and other issues affecting pension scheme investors, please see the latest edition of our **Investment Briefing**.[2]

1 Please see our Alert: The Government redefines its ambition (8 November 2011)

2 Sackers' Investment Briefing (October 2013)

Defined Contribution

DC Developments

DWP publishes long awaited consultation on the reclassification of DC benefits

Reclassifying DC Benefits[3]

The DWP has published a consultation paper on reclassifying DC benefits following the Bridge Trustees case.[4] In that case, the Supreme Court concluded that it was possible for certain benefits to come within the definition of "money purchase benefits", despite there being a potential mismatch between assets and liabilities. The DWP then announced it would legislate retrospectively to reverse the decision.

Whether benefits are classified as DB or DC makes important differences to:

- the protection offered by legislation on a wind-up;
- whether the scheme funding and employer debt requirements apply; and
- the availability of the PPF.

Provisions in the Pensions Act 2011 will introduce a new definition of "money purchase benefits" to provide that a benefit is only DC if:

Trustees should consider their benefit structures to establish whether any benefits previously considered DC will be regarded as DB

- before it comes into payment, its rate or amount is calculated solely by reference to assets which (because of the nature of the calculation) must necessarily suffice for the purposes of its provision to or in respect of the member; and
- once in payment, the pension is secured by an annuity or an insurance policy with an insurance company and, at all times before coming into payment, the member's benefits met the test outlined above.

This definition is designed to ensure that benefits cannot be regarded as DC if it is possible for a funding deficit to arise in respect of them.

The DWP's consultation deals with the potential retrospective application of the change in the definition to January 1997, and the range of pension protection measures affected.

Charges

The level of charges levied by DC schemes is an important current focus for the pensions industry.

Legislation to ban consultancy charges in DC automatic enrolment schemes came into force on 14 September 2013. The new rules mean that an employer cannot receive advice under an agreement with a third party, other than a trustee, provider or pension scheme manager, and pay for that advice out of the members' pension pots or contributions.

The Government has proposed a cap on pension scheme charges

The Government is also consulting[5] on three options for capping charges for default funds in DC schemes used for automatic enrolment:

- a charge cap of 1% of funds under management;
- a lower charge cap of 0.75%; and
- a two-tier "comply or explain cap", that would comprise a standard cap of 0.75%, which could be increased to 1% for employers who can explain to TPR the reason for charges in excess of the standard cap.

3 Please see our Alert: Reclassifying DC benefits following Bridge Trustees (31 October 2013)

4 *Houldsworth and another v Bridge Trustees Limited and another and Secretary of State for Work and Pensions* (SC, July 2011)

5 Please see our Alert: Charges cap proposed for DC schemes (30 October 2013)

Defined Contribution (continued)

OFT finds pensions market uncompetitive

OFT Market Study

The OFT has reached agreement with business and TPR on a set of reforms to the market for workplace DC pensions after its recent study[6] identified that some savers do not get value for money. Issues to be addressed include:

- an audit of old and high charging contract and bundled trust schemes;
- improved governance, to be overseen by independent committees; and
- the provision of higher quality information on costs and charges.

Draft assurance framework published

Master trusts

As occupational trust based DC schemes, master trusts can manage the pension investments of many individual companies and their employees within a single entity. They are proving a popular vehicle for automatic enrolment. In partnership with TPR, the ICAEW is consulting on a draft master trust assurance framework.[7]

The draft framework aims to help trustees of DC master trusts demonstrate that their scheme is being run to a high standard. TPR will encourage employers to select master trusts that have obtained this assurance.

Compliance and enforcement for trust based DC schemes

TPR issued a call for evidence on its compliance and enforcement policy for occupational DC trust based schemes, together with its overall strategy for regulating all DC schemes.[8]

Among other things, the draft policy explains how TPR will identify and assess risk in DC and how this forms the basis for TPR's operational activity. It also sets out TPR's approach to monitoring DC schemes and its available enforcement options.

Default funds under the spotlight

Default funds

The NAPF has published research which indicates that DC default funds are reviewing and overhauling their design and governance, with a view to delivering better retirement outcomes for members.[9] Design trends for default funds include:

- a strong focus on driving value for money;
- stripping out investment volatility; and
- "white labelling" to facilitate future changes of funds.

The NAPF has also consulted on default fund criteria for the Pension Quality Mark, its benchmark for quality DC pension provision.

Governance

A common theme in all the developments relating to DC pensions is good governance, seen by TPR as an important means of improving member outcomes.

For details of the various ways in which Sackers can help with your governance issues, please see our latest Governance Briefing.[10]

6 Office of Fair Trading: Defined contribution workplace pension market study (19 September 2013)

7 Please see our Alert: Master trust draft assurance framework published (18 October 2013)

8 Please see our Alert: Consultation on TPR's DC compliance and enforcement policy (8 October 2013) and Sackers' response to the call for evidence (31 October 2013)

9 NAPF report on default fund design and governance in DC pensions (10 September 2013)

10 Sackers' Governance Briefing: Gaining trust through preparation: key issues for pension scheme trustees (September 2013)

Latest developments

Technical changes[11]

Automatic enrolment reached its one year anniversary in October 2013. Responding to concerns relating to certain provisions, the DWP:

DWP seeks to streamline automatic enrolment processes

- has revised the definition of pay reference periods for automatic enrolment to align them with tax periods;
- has extended the two month deadline for deducting contributions at the outset of automatic enrolment to all jobholders, irrespective of whether their employer uses "statutory" or "contractual" enrolment;
- will extend the joining window from one month to six weeks. As a result, the registration deadline will also be extended from one month to two; and
- has made minor technical changes to the quality requirements that DB pension schemes have to meet if they are used for automatic enrolment.

While the majority of the changes came into force on 1 November 2013, changes to the joining window and registration deadlines are due to come into force on 1 April 2014.

A number of issues will be the subject of further consultation, including the appropriateness of excluding certain categories of worker from the automatic enrolment duty.

DWP guidance

Certification guidance updated

The DWP has updated its detailed guidance for employers and actuaries on certifying workplace pension schemes for automatic enrolment.[12] The guidance (originally published in July 2012) covers DC schemes, as well as DB and hybrid arrangements, and sets out how employers can confirm that their schemes can be used as qualifying schemes for automatic enrolment.

The changes generally either clarify the guidance or make technical amendments. However, certain significant changes are summarised in an annex to each guidance document.

Opt-out rates[13]

Research and analysis by the DWP, looking at some of the largest employers to which automatic enrolment applied in the first year (those with between 6,000 and 120,000 employees), indicates lower than expected opt-out rates. Across all the public and private sector employers in the study, the average opt-out rate was 9%. Overall participation in workplace schemes increased from 61% to 83%, representing an increase from around 1.2 million workers to 1.6 million workers.

11 Please see our Alert: Technical changes to automatic enrolment (15 October 2013)

12 Automatic enrolment: Guidance for employers and actuaries (25 September 2013)

13 Automatic enrolment opt-out rates: findings from research with large employers (August 2013)

Pensions Tax

LTA protections

LTA to be reduced from April 2014

From the tax year 2014/15 onwards, the standard LTA (the total amount of tax relieved pension savings that an individual can build up over their lifetime without incurring an additional tax charge) will be reduced from £1.5 million to £1.25 million.

Fixed Protection 2014

Using the framework of the fixed protection regime introduced from April 2012, FP14 will allow an individual to maintain an LTA of the greater of £1.5 million and the standard LTA. As with FP12, FP14 can be lost in certain circumstances, including new contributions to a DC arrangement or DB accrual in excess of the relevant percentage[14] at any time during a tax year.

Applications for fixed protection must be received by HMRC by 5 April 2014. It is possible to apply for this tax protection online.[15]

Individual Protection

New transitional protections available

In addition, the Government has been consulting[16] on a new form of protection, IP14, which would entitle individuals to an LTA of the greater of the value of their pension rights on 5 April 2014 (up to an overall maximum of £1.5 million) or the standard LTA. In contrast to fixed protection, it is envisaged that individuals with IP14 would not be subject to restrictions on future contributions or accrual. The outcome of the Government's consultation is awaited.

Updated guidance

Ahead of the April 2014 changes to the AA and LTA, HMRC has published guidance for individuals which outlines details of the new protections, as well as the new QROPS rules (see below) and other developments in pensions taxation.[17] HMRC has also launched a new online tool for pension scheme members to check whether they need to calculate an AA tax liability and complete a self-assessment tax return.[18]

Overseas pensions

Changes to the QROPS regime

QROPS rules tightened up

New rules aimed at further strengthening the QROPS regime[19] make a number of changes to the rules on tax-free transfers of UK tax relieved pension savings to pension schemes overseas that meet the QROPS requirements. The changes include a new renewal system, under which QROPS will need to notify HMRC of their status every five years, and new reporting requirements for funds transferred from UK schemes.

New HMRC forms are available for QROPS to report certain information.[20]

14 The "relevant percentage" will normally be either the annual rate of revaluation specified in the scheme rules as of 11 December 2012 or CPI (if no rate is specified), although certain statutory increases will be excluded from this test

15 Visit HMRC's website to access the online application form

16 Please see our Alert: Lifetime Allowance – the Government consults on "individual protection" (13 June 2013)

17 HMRC pension schemes newsletters: No.58 (August 2013) and No.59 (October 2013)

18 The Annual Allowance checking tool is available on HMRC's website

19 The Registered Pension Schemes and Overseas Pension Schemes (Miscellaneous Amendments) Regulations 2013

20 New QROPS forms APSS 251 and APSS 253 are available on the HMRC website

Public Sector Pensions

Reform of public sector pensions

The Fair Deal

Continuing membership of public sector schemes to be allowed for outsourced employees

The Fair Deal is a non-statutory policy applying to pensions for public sector staff. Until now, it has required that where staff are compulsorily transferred out of central government to an external provider, such as on a public sector outsourcing, the new employer must provide a broadly comparable pension scheme.

Following consultation, the Government confirmed that the overall approach would be retained, but may be delivered by offering access to public sector schemes for staff transferred under TUPE. New guidance sets out how the policy will operate.

Governance overview

TPR to take over regulation of public sector schemes

TPR has published its first report on the governance and administration of public sector pension schemes.[21] The report is intended to provide a portrait of the current state of such schemes.

TPR's role was expanded by the Public Service Pensions Act 2013, in the wake of the Hutton Report.[22] TPR sees providing educational information on the areas that it regulates as an important element of its risk based regulatory approach. It will make clear the standards required in terms of governance and administration of public sector schemes, and will monitor and report on the progress made by schemes in achieving them.

Local Government Pension Scheme

LGPS Regulations 2013

LGPS switches to CARE in April 2014

Regulations[23] made in September 2013 implement recommendations of the Public Service Pensions Commission[24] and set up a new legal regime for the LGPS that will come into force on 1 April 2014.

The new regime will provide for benefits to accrue on a CARE basis (rather than pure DB as currently), and for the normal retirement age at which a member can draw benefits without actuarial reduction to be the same as the age at which the person is entitled to draw the state retirement pension.

Pooling arrangements

The DCLG is consulting on proposals for pooling arrangements within the LGPS.[25] A pool is a mechanism for two or more employers to share actuarial assumptions and risks relating to participation in the scheme as an employer. The consultation is aimed at academies and local authorities.

21 Public service pension schemes: A summary of governance and administration (6 September 2013)

22 Final report of the Independent Public Service Pensions Commission (10 March 2011)

23 The Local Government Pension Scheme Regulations 2013

24 Please see our Alert: Hutton recommends new career average scheme (10 March 2011)

25 Pooling arrangements for Academies within the LGPS (7 October 2013)

Regulatory

HM Revenue & Customs

Pension liberation high on HMRC's agenda

Pension liberation processes revised [26]

HMRC has made a number of changes (with effect from 21 September 2013) to strengthen existing processes with a view to deterring pension liberation and to safeguarding pension savings. These include:

- registering a pension scheme: scheme registration will no longer be confirmed automatically, to allow HMRC time to first conduct a detailed risk assessment;
- transfers: HMRC will respond to requests for confirmation of a scheme's registration status without seeking consent from the receiving scheme as it did previously.

Pension Protection Fund

Increase in the PPF levy

Consultation on the pension protection levy

The PPF has been consulting on the Pension Protection Levy Determination for 2014/15.[27] It intends that the levy parameters will remain unchanged, meaning the total levy will be £695 million (representing an increase of 10%).

While changes are to be kept to a minimum, the PPF has proposed procedural improvements to the recertification of contingent assets, and a revised form of wording for the certification of Type A contingent assets (parent or group company guarantees).

Levy deadlines

Data deadlines for 2014

The consultation document sets out provisional deadlines for the 2014/15 levy year. Key dates to watch out for are:

- **31 March 2014:** Deadline for submission of Scheme Return to TPR. Information from the Scheme Return is used in the calculation of the levies.
- **31 March 2014**: Deadline for certification of new contingent assets and recertification of existing contingent assets.
- **30 April 2014:** Deadline for submission of deficit reduction contribution certificates for contributions made up to and including 31 March 2014.
- **30 June 2014:** Deadline for submission of full block transfer certificates.

Schemes wishing to put in place or recertify PPF contingent assets are advised to start this process in good time to ensure these deadlines can be met.

Levy invoicing

The PPF began invoicing for the pension protection levy in September 2013. Ahead of this, it updated the information provided on its levy invoicing pages.[28]

26 Please see our Alert: Pension liberation: Latest news (22 October 2013)

27 Published on 5 September 2013. Please see also Sackers' response to the consultation (23 October 2013)

28 Further information is available on the levy invoicing pages of the PPF website

The Pensions Regulator

Scheme funding

A consultation on revisions to TPR's code of practice on scheme funding is awaited.[29] TPR has indicated that this will include:

- changes made as a result of TPR's new statutory objective "to support scheme funding arrangements that are compatible with sustainable growth for the sponsoring employer and fully consistent with the 2004 funding legislation";
- a new focus on integrated risk management – addressing covenant, investment and funding risks; and
- TPR's regulatory approach and how it will assess risk, including the new triggers for involvement with schemes.

Draft revised scheme funding code awaited

TPR statement on double counting

In the meantime, TPR has issued a statement on double counting in scheme funding for DB schemes,[30] in which it states that it considers payments under a schedule of contributions cannot also be payments towards "section 75 debts" or vice versa.

Kodak restructuring

TPR issued a statement[31] on the completion of the acquisition from Eastman Kodak Company of the Personalised Imaging and Document Imaging businesses. TPR gave clearance in April 2013 for the acquisition of the two companies and the establishment of a new pension plan.

This is another example of the type of deal that may be reached with a view to obtaining the best possible outcomes for both scheme members and the PPF. In this case, the restructuring avoids the insolvency of the Kodak group and allows pension scheme members to benefit from the cash flows and growth potential of the two groups. TPR is still working on some connected issues with the trustees and the PPF, including monitoring and governance arrangements. Once these have been addressed, TPR intends to publish a full report outlining how it approached the Kodak case.

Reporting late payment of contributions[32]

Revised codes of practice in force

TPR's revised codes of practice on reporting the late payment of contributions to occupational and personal schemes came into force on 20 September 2013.[33] The codes set out how occupational pension scheme trustees and the managers of personal pension schemes should:

- monitor the payment of contributions due under the payment schedule / direct payment arrangement (as appropriate);
- provide sufficient information to enable members to check contributions; and
- report material payment failures to TPR and members within a reasonable period.

29 Announced in TPR's annual funding statement (May 2013)

30 Double counting: Section 75 debts/scheme funding obligations (October 2013)

31 On 4 September 2013

32 Please see our Alert: Revised codes and guidance on late payment of contributions (12 June 2013)

33 Codes of Practice No.5 and No.6 on the reporting of late payment of contributions

Cases

Court of Justice of the European Union

Age related contributions can be objectively justified

HK Danmark v Experian A/S

Contributions to the Experian scheme are payable on a sliding scale, increasing with age. Ms Kristensen alleged this was unlawful age discrimination.

While the CJEU agreed that linking contributions to age represented a difference in treatment on the grounds of age, the sliding scale was justified as it was intended to:

- enable older workers who enter its employment at a later stage in their working life to build up reasonable savings over a relatively short contribution period; and
- include young workers in the same pension scheme at an early stage, while enabling them to have a larger proportion of their wages at their disposal.

These aims were legitimate, as they took account of the interests of all employees. It is now up to the Danish courts to determine whether the age related contributions are an appropriate and necessary measure to achieve the legitimate aim.

High Court

Court confirms arrangements are occupational pension schemes

Pi Consulting and Dalriada Trustees v TPR and others[34]

The High Court has ruled that nine schemes under investigation as potential pension liberation vehicles are occupational pension schemes and therefore subject to the jurisdiction of TPR.

The case followed police raids in May 2013 on organisations accused of involvement in pension liberation. It was brought by the independent trustees appointed by TPR to administer the schemes, who asked the Court to determine the legal status of the schemes. As the Court found that all nine schemes were occupational pension schemes under the Pension Schemes Act 1993, the appointments by TPR of Pi and Dalriada as independent trustees to the schemes were valid. It is now open to TPR to argue that the schemes are in fact a mere sham.

Pensions Ombudsman

Investment fund choices must be clearly and accurately described

Mr F White[35]

Mr White had invested in an AVC fund initially described by Standard Life as offering “the highest level of unit price stability” and invested in “bank/building society deposits and other short term sterling assets”. Subsequent literature stated that the “cash investments” in the fund were “not guaranteed” and that the fund value may fall “in extreme circumstances”. Following the collapse in the housing markets in 2008, the fund’s price fell by 4.8% as around half of the funds under management had been invested in mortgaged backed securities.

Standard Life was fined by the FCA[36] in 2010 for the production of misleading marketing material. The PO upheld Mr White’s claim that the fund had been misleadingly promoted and had caused him financial loss. As the literature relied on came initially from Standard Life, a complaint against the trustees was dismissed.

This case underlines the importance of clear and accurate member communications, particularly in relation to DC investment choices.

34 Please see our Alert: Pension liberation: Latest news (22 October 2013)

35 PO-350, 30 August 2013. Please see our summary of the determination

36 The Financial Services Authority as it was then

Sackers seminars:

Dates for your diary

We have an extensive programme of workshops and lecture style seminars. In addition to the Quarterly Legal Updates, seminars take the form of a focused discussion led by experts in the particular area. The workshop format gives clients the opportunity to share their own experiences.

Pensions for New Trustees – Workshop	19/11/13	**Breakfast seminar (9:00am-12:30pm)** Getting up to speed with Trustee Knowledge and Understanding. Followed by lunch and further discussion.
Joint Seminar with the Law Commission – Fiduciary duties	12/12/13	**Breakfast seminar (09:00am-10:30am)** In this session our presenters will examine the Law Commission's current consultation on the application of the law of fiduciary duties to investment intermediaries.
Quarterly Legal Update – Seminar	06/02/14	**Breakfast seminar (09:00am-10:30am)** The latest legal and regulatory developments in the pensions world.
Quarterly Legal Update – Seminar	08/05/14	**Breakfast seminar (09:00am-10:30am)** The latest legal and regulatory developments in the pensions world.
Quarterly Legal Update – Seminar	10/07/14	**Breakfast seminar (09:00am-10:30am)** The latest legal and regulatory developments in the pensions world.

If you would like to attend any of our seminars, please contact our marketing team at marketing@sackers.com.

Our Quarterly video distils content from the Quarterly Legal Update Seminar into a bite size chunk, highlighting some of the current key issues. You can access the Quarterly video and our series of spotlights on specific pensions issues, by scanning the code with your smartphone or tablet.

Sacker & Partners LLP
20 Gresham Street
London EC2V 7JE
T +44 (0)20 7329 6699
F +44 (0)20 7248 0552
E enquiries@sackers.com
www.sackers.com

Sackers

Nothing stated in this document should be treated as an authoritative statement of the law on 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 November 2013