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sackers extra

THE QUARTERLY

JUNE 2009

Introduction

Welcome to our Sackers Extra "Quarterly", designed to highlight significant developments in pensions law over the last quarter. The Quarterly is published in March, June, September and December. Each edition covers key areas such as pensions reform, regulatory developments, new legislation and cases.

Copies of our Sackers Extra publications referred to in this "Quarterly" are available from the client area of our website www.sackers.com or from your usual contact.

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PENSIONS REFORM

Budget 2009[1]

Restriction on pensions tax relief

This year's Budget on 22 April 2009 delivered a heavy blow to high earning pension savers, with the announcement of a reduction in tax relief on pension contributions for those earning £150,000 or more. From April 2011, relief will be tapered away so that for those earning £180,000 or over it will be worth just 20% (i.e. the same as for a basic rate tax payer). The Government is to consult on these measures.

Tax relief restricted on pension contributions for high earners

Transitional provisions

In order to prevent those at whom the Budget measure is aimed from making extraordinary contributions in the run-up to 2011, the Finance Bill 2009 introduces interim measures which will be effective from 22 April 2009. Generally speaking, a 20% charge ("the special annual allowance charge") will be levied on individuals who:

Special annual allowance

- have an income of £150,000 or more;
- change the pattern of their normal, regular, ongoing pension savings; and
- whose overall pension savings exceed £20,000 (the "special annual allowance").

Other Budget announcements

These pension tax relief measures come on top of an increase in higher rate tax (to 50%) for taxable income above £150,000 from 2010. The Government also intends to introduce minor changes relating to the tax treatment of pension benefits in the Finance Bill 2009, including legislation that will allow lump sum payments from the Financial Assistance Scheme to be given broadly the same tax treatment as if they had been received from the original pension scheme.

Consultations on new legislation

Personal accounts scheme order and rules

The Pensions Act 2008 enables the personal accounts scheme to be established under secondary legislation.[2] On 28 April 2009, the Personal Accounts Delivery Authority issued a joint consultation document, together with the Department for Work and Pensions (DWP), which sets out proposals on the legal framework for the personal accounts scheme (the "scheme order and rules").

First draft of personal accounts rules published

The scheme order is intended to be the equivalent of the trust deed for a typical trust-based pension scheme and outlines the main parameters of the scheme, including eligibility criteria, and the criteria for member and employer participation. The scheme rules set out more of the detail, such as general administrative provisions, provision for employer and member contributions, the annual contribution limit and the application of benefits on retirement.

The consultation closes on 20 July 2009.

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[1] For more information, please see our Alert: "Budget 2009: Building Britain's future" dated 23 April 2009

[2] For more information, please see our Alert: "Pensions Act 2008: the Road to 2012" dated 5 December 2008

Automatic Enrolment

The DWP is also consulting on two sets of draft regulations relating to the personal accounts provisions of the Pensions Act 2008.

Employer automatic enrolment duties

The draft Automatic Enrolment Regulations[3] set out the practical arrangements for automatic enrolment of eligible employees (defined as "jobholders" under the Act) into qualifying pension arrangements, including the procedure for opting out. They are currently scheduled to come into force in 2012.

The draft Delegation of Powers Regulations[4] will enable the Pensions Regulator to delegate certain specified compliance powers in relation to the personal accounts regime to external public and private bodies. They are intended to come into force in the autumn of 2009.

Review of Disclosure of Information Requirements applying to Occupational, Personal and Stakeholder Pension Schemes

New approach to disclosure regulation?

The 2007 Deregulatory Review[5] recommended that the DWP explore a "principles-based" approach to regulation, suggesting that the legislation governing disclosure in occupational and personal pension arrangements could be used as a pilot. Since then, the Government has considered the proposal and commissioned a working group to look into the issues further.

This consultation sets out the results of a review of the existing disclosure requirements and puts forward proposals for reform.[6] The intention is to streamline and, where possible, simplify the disclosure requirements.

As currently drafted, the consultation puts forward an overarching disclosure principle, complemented by obligations for specific circumstances. The consultation also provides for information to be provided "within a reasonable period", rather than within specific time limits.

The DWP plans to introduce the new disclosure requirements in 2010.

Financial Assistance Scheme (FAS)

Consultation on draft actuarial guidance

Funding FAS extensions

In December 2007, the Government announced substantial reforms to FAS, including its extension so that those eligible for help would receive 90% of their promised benefits (subject to a cap), and the inclusion of certain schemes with solvent employers.[7] This extension was to be funded, in part, by transferring into Government the residual assets of FAS qualifying schemes that have yet to complete winding-up.

On 2 April 2009, the DWP issued a consultation on draft guidance relating to the method and assumptions that will apply when actuaries undertake valuations in respect of FAS qualifying schemes to facilitate such transfers. This is ahead of further consultation on regulations that will enable such transfers to take place (which is intended to be published over the summer). This consultation (aimed primarily at pension scheme actuaries) closed on 15 May 2009.

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[3] The Pensions (Automatic Enrolment) Regulations 2009

[4] The Pensions Regulator (Delegation of Powers) Regulations 2009

[5] For more information, please see our Alert: "Deregulatory review – the simple life?" dated 27 July 2007

[6] For more information, please see our Alert: "Fresh approach to disclosure regulation" dated 16 March 2009 and Sackers' response to the consultation dated 6 May 2009

[7] For more information, see our Alert: "FAS is for life, not just for Christmas" dated 18 December 2007

LEGISLATION

Government Equalities Office

Equality Bill 2009

Consolidation of existing equality legislation

This is designed to bring together and re-state a number of anti-discrimination laws which will be familiar to those who operate in the world of occupational pension provision, including:

- The Equal Pay Act 1970;
- The Sex Discrimination Act 1975;
- The Disability Discrimination Act 1995; and
- The Employment Equality (Age) Regulations 2006.

The Bill seeks to harmonise existing legislative provisions, giving a single approach where appropriate. It is anticipated that the Bill will become law during 2010.

HM Revenue & Customs (HMRC)

The Registered Pension Schemes (Authorised Payments) Regulations 2009

New authorised payments

Regulations which add to the list of categories of authorised payments that can be made by registered pension schemes without attracting a tax charge have been published in final form, almost one year after their publication in draft.[8]

HMRC received many comments on the draft regulations and made changes in the light of these. The regulations will now come into force on 1 June 2009.

Since the authorised payments rules were introduced on A-Day (6 April 2006), the Government has become aware of a number of circumstances in which the authorised payment rules catch payments that it considers it would be fairer to treat as authorised. These include:

- lump sums representing commutation of certain small pension pots;
- certain payments made in error; and
- arrears of pension due after the death of the member.

The regulations set out the requirements to be met for payments to be treated as authorised (and taxed as such). Changes from the original draft regulations include further instances in which it is possible to commute small pension pots, as well as allowing certain lump sums paid in error to be treated as authorised.

The regulations will apply retrospectively (from 6 April 2006) to those payments which relate to lump sum or pension errors, while the provisions authorising new commutation payments will apply to payments made on or after 1 December 2009.

[8] For more information, please see our Alert: “Trivial Commutation Regulations published!” dated 18 May 2009

Department for Work and Pensions (DWP)

The Occupational Pension Schemes (Contracting-out) (Amendment) Regulations 2009

Converting GMPs into scheme benefits

On 6 April 2009, it became possible for trustees to convert Guaranteed Minimum Pensions (GMPs) into scheme benefits.[9] The framework for GMP conversion is contained in the Pensions Act 2007[10], which sets out five conditions which need to be met before conversion can take place. These regulations detail how the GMP element is to be converted, on an actuarially equivalent basis, and outline the circumstances in which a survivor's benefit must be payable from the converted benefits.

The Occupational, Personal and Stakeholder Pensions (Miscellaneous Amendments) Regulations 2009[11]

These regulations seek to make a number of (unconnected) amendments to regulations governing occupational, personal and stakeholder pensions. They:

Statutory override provisions in force from 6 April 2009

- enable trustees to take advantage more easily of the reductions in the statutory caps applicable to increases on pensions in payment and revaluation of deferred benefits, by allowing trustees to amend their rules (with employer consent) by resolution;
- update the investment regulations (to remove transitional measures, in line with the EU Pensions Directive), although certain provisions which would have affected employer-related investments in Collective Investment Schemes have been removed from the final draft (the Government is to look at this issue further);
- provide a power for the Pensions Regulator to impose a financial penalty, or to issue an improvement notice, on a person who fails to consult when making certain future changes to pension provision;
- make it easier for members of occupational pension schemes with benefits payable as a result of a pension sharing order to take a pension before normal benefit age in line with other scheme benefits; and
- tidy up some out of date legislation.

Other than the investment provisions (which generally come into force on 23 September 2010), these regulations came into force on 6 April 2009.

The Pensions Regulator (Miscellaneous Amendment) Regulations 2009

Extended "look back" period for FSDs

Where a sponsoring employer is a service company or is "insufficiently resourced", the Pensions Regulator can impose a financial support direction (FSD) on anyone who is connected or associated with that employer. When assessing which persons met this test, the Regulator could previously only "look back" for a period of 12 months, ending on the date on which the determination to issue the FSD was made. This period has now been extended to 24 months, although implementation will be phased in until 6 April 2010 (when the full 24 months will apply).

Changes to notifiable events regime

The regulations also make changes to the notifiable events regime from 6 April 2009. The following three events will no longer need to be notified to the

[9] For more information, please see our Alert: "GMPs: Trying for a Conversion?" dated 5 March 2009

[10] The Pensions Act 2007 amends the Pension Schemes Act 1993 for this purpose

[11] For more information, please see our Alert: "When draft regulations are born!" dated 10 December 2008

Regulator:

- two or more changes in the holders of any key scheme post within the previous 12 months;
- any change in the employer's credit rating, or the employer ceasing to have a credit rating; and
- two or more changes in the holders of any key employer posts within the previous 12 months.

The Financial Assistance Scheme and Incapacity Benefit (Miscellaneous Amendments) Regulations 2009

These regulations (in force from 27 March 2009) make a further extension to FAS by providing for early unreduced payment of assistance to certain qualifying members who are aged 55 or over and who are not terminally ill, but have a significantly shortened life expectancy.

Further extensions to FAS

REGULATORY

Department for Work and Pensions (DWP)

Updated guidance on employer consultation

The DWP has published an updated version of its guidance on the requirement for employers to consult affected members when making certain future changes to pension provision.

Employer consultation guidance updated

The key changes from the March 2006 version of the guidance are that:

- the DWP considers that, providing the employer's contribution rate does not change and that members' contributions do not increase, changing a group personal pension provider is not a listed change and consultation by the employer is not required;
- the "Sanctions" section of the guidance has been updated to reflect the new power for the Pensions Regulator to impose a fine on employers who (without reasonable excuse) do not comply with the statutory consultation requirements.

Financial Services Authority (FSA)

Changes to simplify the Financial Services Compensation Scheme (FSCS)

The FSA has announced that it will go ahead with proposed changes to compensation limits for insurance, investment and home finance advice business in the event of a firm failing. This is designed to achieve "greater simplicity and consistency" in the FSCS.

FSCS compensation

Currently, the FSCS provides protection for non-compulsory insurance at a rate of 100% for the first £2,000 of a claim and 90% of the remainder (with no upper limit). This protection, which may be relevant to schemes which have, or are considering, buy-in or buy-out policies, will change with effect from 1 January 2010, so that protection is provided at a rate of 90% across the whole claim (with no upper limit).

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Government Actuary's Department (GAD)

Changes to revaluation in deferment and validity of certificates of broad comparability

Changes to revaluation may affect certificates of broad comparability

Following changes introduced by the Pensions Act 2008, the statutory cap on revaluing final salary deferred pensions reduced from 5% to 2.5% in respect of benefits accruing from 6 April 2009.

GAD has reminded contractors and contracting authorities that where changes are made to the contractor's pension scheme before a certificate of broad comparability expires, a new certificate may be required for employees who are still public servants at the time of the change. GAD has advised that, if a contractor cuts the cap on revaluation of deferred benefits below the level described in their current passport certificate, then that passport certificate would be withdrawn pending a reassessment of the broad comparability of the benefit package as a whole. In practice, GAD expects that it will be difficult for contractors to come up with a sufficiently valuable benefit structure in other areas to compensate for a reduction in the cap to 2.5%.

HM Revenue and Customs (HMRC)

Notional Earnings Cap for 2009/10

Confirmation of notional earnings cap

The Registered Pension Schemes (Modification of the Rules of Existing Schemes) Regulations 2006 set out transitional provisions for schemes in place at A-Day (6 April 2006). Under one of the transitional provisions, HMRC agreed to publish details of a notional earnings cap each year until 2011.

The notional earnings cap for 2009/10 is £123,600.

Tax repayment requests for a registered pension scheme

Guidance on tax reclaims

When a registered pension scheme has paid UK income tax at source on the income from its investments or deposits held for the purposes of the scheme, a repayment request can be submitted to HMRC.

HMRC has published guidance for registered pension schemes on claims made during the course of a tax year for the repayment of tax paid on investment income. The guidance (which will be incorporated into the Registered Pension Schemes Manual later this year) details changes to the process which will be effective from 1 August 2009.

Anti-avoidance spotlights: Pensions schemes artificial surplus

Anti-avoidance activities attract tax charges

HMRC has published "spotlights" on a number of anti-avoidance activities of which it has become aware, including the creation of artificial pension fund surpluses. HMRC states that it is aware of "schemes that purport to enable a member of a registered pension scheme to remove funds from the scheme tax-free". These arrangements may entail members surrendering benefits and creating funding surplus.

Payments made by a scheme in these circumstances will be regarded as an unauthorised payment in respect of the member, and will attract tax charges on the member on the amount paid out of the scheme.

Parliamentary Ombudsman

Equitable Life: Parliamentary Ombudsman publishes further report

Government's response disappointing

The Parliamentary Ombudsman, Ann Abraham, has laid before both Houses of Parliament a further report concerning the failure of the Equitable Life Assurance Society. This follows an initial report in July 2008[12] and the Government's response in January 2009.

The Ombudsman found the Government's response to be "deeply disappointing" as it provided insufficient support for the rejection of her findings of maladministration and injustice. She also commented on the Government's appointment of Sir John Chadwick to advise on an alternative ex gratia scheme for members who lost out as a result of Equitable Life's failure, expressing concern over, among other things, the lack of clarity on the intended timetable for this work.

Pension Protection Fund (PPF)

PPF Compensation Cap

PPF compensation cap - annual increase

Under the Pensions Act 2004, each year the Secretary of State is required to specify the amount of the PPF compensation cap. The level of the compensation cap was increased to £31,936.32 (up from £30,856.35) from 1 April 2009.

PPF Levy Ceiling

PPF levy ceiling increased

The Board of the PPF imposes the pension protection levy on schemes. This levy is restricted in accordance with the levy ceiling, which is determined by the Secretary of State. The levy ceiling for the financial year beginning on 1 April 2009 is £863,412,967.

Consultation on PPF powers to amend contract terms

No automatic termination of contracts on transfer to PPF?

Under the Pensions Act 2004 and regulations made under it, when the PPF assumes responsibility for a scheme it has the power to disapply any term of a contract entered into by that scheme, or to substitute a reasonable term or condition in its place, if it considers that term to be "onerous".

According to the Board of the PPF, industry concern that existing contracts might be disclaimed when a scheme transfers to the PPF has led some fund managers to insert an additional trigger event into termination clauses in their contracts. Such clauses would automatically trigger early termination of the contract on the transfer of a scheme to the PPF.

Given that such early termination will generally not be in the interests of either trustees or fund managers, the Board is seeking to address this by providing standard wording for agreements between trustees and counterparties. The proposed wording provides that the Board of the PPF will notify affected fund managers, before a scheme transfers to the PPF, as to whether or not it proposes to exercise its power. If such wording is adopted, a transfer would not constitute an automatic trigger for early termination of the contract, provided the PPF Board has notified fund managers affected by the transfer.

The PPF has published an open letter consulting on its proposed solution and will publish written guidance on its website when the consultation is complete.

[12] Equitable Life: A Decade of Regulatory Failure (http://www.ombudsman.org.uk/improving_services/special_reports/pca/equitable_life/index.html)

The Pensions Regulator (TPR)

TPR issues an "Alert to risks in the economic downturn"

TPR comments again on the economic downturn

TPR has issued a statement to the pensions industry "to explain how they can work in partnership through the economic downturn". This Alert follows two earlier statements (issued in October 2008 and February 2009[13] to trustees of work based pension schemes and to UK employers of defined benefit schemes respectively) on the impact of the prevailing economic conditions for those involved in the running of occupational pension schemes.

The statement focuses on behaviour which has the potential to increase risks to members' benefits and the PPF, for example dishonesty and fraud, and highlights TPR's powers to sanction behaviour and protect schemes. It also reminds those involved in running both occupational and personal pension schemes of the duty to report materially significant breaches of any legislation or rule of law concerning the administration of pension schemes.

Material Detriment Code revisited[14]

Following a consultation which closed in February 2009, TPR has published a revised code of practice which is expected to come into effect in the summer of 2009.

Final "material detriment test" code published

In response to fears that TPR's anti-avoidance powers were insufficient to tackle risks posed to members' benefits by "new business models", the Pensions Act 2008 introduced a new power to impose contribution notices in certain circumstances, where a party's action or failure to act has a materially detrimental effect on the likelihood of members receiving their benefits (known as the "material detriment test").

TPR's latest code of practice is one of a number of safeguards on the use of this new power, as it is required to set out the circumstances in which it expects to use it. The new power will apply retrospectively to 14 April 2008 (the date on which it was first announced).

Personal Accounts Delivery Authority (PADA)

Investment discussion paper launched

PADA has launched a discussion paper on designing an investment approach for the new personal accounts scheme. It aims to draw on good practice and expertise from the pension and investment industries in deciding the most appropriate investment approach for personal accounts.

Investment options for personal accounts scheme

The discussion paper covers a range of investment issues, including:

- the investment objective and design of the default fund (which is where PADA expects most members to invest);
- the investment approach as members near retirement;
- achievement of high quality corporate governance;
- responsible investment and its role within the scheme; and
- the number and types of fund choice that should be made available.

The consultation closes on 7 August 2009.

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[13] For more information, please see our Alert: "TPR – your flexible friend" dated 18 February 2009

[14] For more information, please see our Alert: "Material Detriment Code revisited" dated 7 May 2009

CASES

European Court of Justice (ECJ)

The Incorporated Trustees of the National Council on Ageing (Age Concern England) v Secretary of State for Business, Enterprise and Regulatory Reform (Heyday)[15]

The ECJ published its judgment in the Heyday case on 5 March 2009.

Default retirement age justifiable in principle

The case challenged provisions under the Employment Equality (Age) Regulations 2006 which allow employers to dismiss workers aged 65 or over, provided the reason for dismissal is retirement. The arguments centred on whether the UK has properly implemented the age discrimination requirements of the European Framework Directive, and whether the so-called default retirement age of 65 is, of itself, discriminatory.

The ECJ essentially reached a similar conclusion to the opinion of the Advocate General in September 2008, finding that the UK's default retirement age could be objectively justified as a matter of national law. It ruled that the Directive "gives Member States the option to provide…for certain kinds of differences in treatment on grounds of age if they are 'objectively and reasonably' justified by a legitimate aim, such as employment policy, or [the] labour market…, and if the means of achieving that aim are appropriate and necessary".

However, the Directive imposes on Member States a burden of establishing "to a high standard of proof" the legitimacy of the aim relied on as justification. It is now up to the UK High Court to determine whether the default retirement age can be objectively justified.

Pensions Ombudsman (PO)

Warwick v Trustees of the Rangers Pension Scheme

Mrs R was both a trustee and potential beneficiary of the Rangers Scheme. Her husband (from whom she was separated but still married to), had been cohabiting with Mrs W at the time of his death. On his death, a lump sum and dependant's pension became payable at the trustees' discretion.

Possibility of bias did not invalidate decision

Mrs R and Mrs W were the only potential beneficiaries under the rules. As trustee, Mrs R, together with the other trustee (an independent trustee) had to consider how to award the death benefits. They decided to award 70% of the lump sum to Mrs W and to split the pension (which was payable to an individual who was "wholly or partially financially dependent" on the member) 50/50 between the two women. Mrs W challenged the trustees' decision on the grounds that Mrs R had a conflict of interest.

The PO recognised that Mrs R had a potential conflict of interest but noted that the scheme rules expressly permitted a trustee who was also a beneficiary, or potential beneficiary, to exercise a discretionary power in these circumstances.

The PO considered that while there had been a difference of opinion between Mrs R and the independent trustee as to the appropriate split of the lump sum benefit, the independent trustee, being a professional organisation, could be taken to have known what its responsibilities (and those of Mrs R) were. Therefore, even though there was a potential conflict due to Mrs R's position, the PO did not find any tainting of her thinking by irrelevant matters. In

[15] For more information, please see our Alert: "Heyday: The ECJ Decides" dated 6 March 2009

addition, given “the special position of the independent trustee”, the possibility of bias had not invalidated the decision made by the trustees jointly.

The PO also found that a request by the trustees for further information from Mrs W to establish dependency was not unreasonable, and that her refusal to provide the information requested could properly be taken into account. As a result, the PO did not uphold the complaint.

Deputy Pension Protection Fund Ombudsman (DPPFO)

Trustees of the Hoval Limited Pension Plan (Hoval Plan)

The DPPFO has rejected a challenge mounted by trustees against the Dun & Bradstreet (D&B) methodology (used by the PPF in determining its levies).

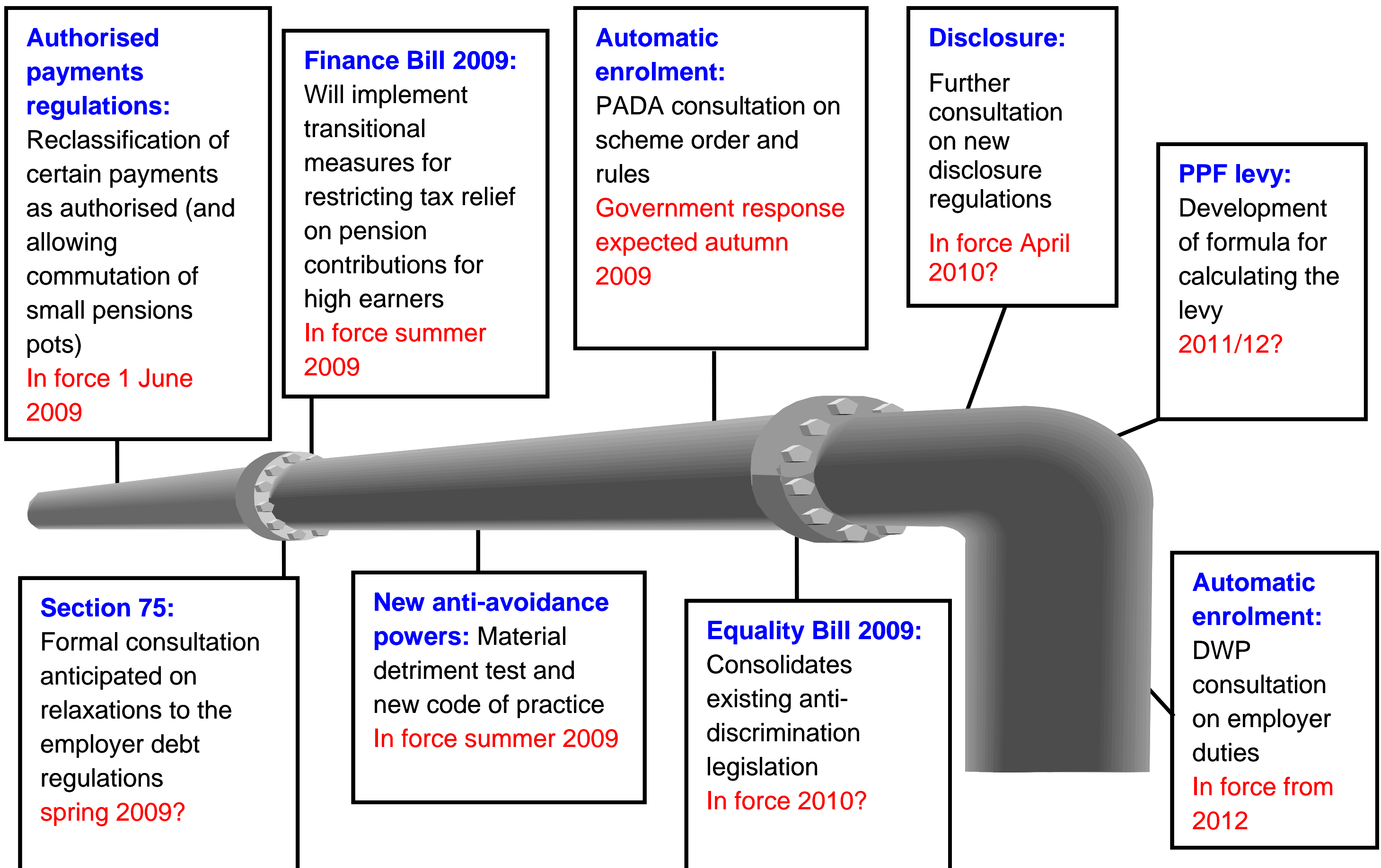
Appeal against D&B failure score rejected

The trustees of the Hoval Plan opposed the amount of their 2007/08 levy on the basis that the PPF Board had improperly assessed the likelihood of an insolvency event (by not taking account of the notes to the accounts on post balance sheet events) and had therefore treated the Plan unfairly. The trustees argued that if this information had been taken into account, the employer’s improved financial position after the year end would have merited a lower PPF levy.

Under the Pensions Act 2004, the Board is required, before the beginning of each financial year, to determine a number of factors in respect of that year, including the factors by reference to which the pension protection levies are to be assessed, and the rate of the levies. As part of that process (and in accordance with the Board’s determination), D&B provide to the Board normal failure scores for each scheme employer (i.e. the likelihood of an insolvency event occurring in respect of that employer). D&B’s process for assessing an employer’s failure score involves “using information extracted from accounts filed at Companies House”.

The DPPFO held that the Board had calculated the Plan levy in accordance with the 2007/08 PPF levy Determination. He considered that “for [D&B] to review notes to accounts and directors’ reports, would be costly and would introduce a degree of subjectivity.”

IN THE PIPELINE



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