

# THE QUARTERLY

MARCH 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](http://www.sackers.com) or from your usual contact.

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## PENSIONS REFORM

### Consultations on new legislation

#### ***The Occupational, Personal and Stakeholder Pensions (Miscellaneous Amendments) Regulations 2009<sup>1</sup>***

These draft regulations propose amendments to no less than 24 separate sets of regulations. A number of these are designed to implement minor policy changes and make some outstanding consequential amendments. However, there are some more substantive changes, including:

- a power to enable trustees to modify scheme rules by resolution to reflect the new lower cap on revaluation of deferred defined benefit pensions. This will be of assistance to schemes where the change will not apply automatically (due to the way the scheme rules are drafted);
- a similar “statutory override” provision relating to indexation of pensions in payment;
- a new power for the Pensions Regulator (TPR) to impose civil penalties on employers who fail to consult with affected members over changes which are “listed” under the consultation regulations<sup>2</sup>; and
- the removal of certain transitional provisions in relation to employer-related investments.

#### ***New statutory overrides***

Consultation on these regulations closed on 30 January 2009.

#### ***Flexible retirement and pension provision - Government response to consultation***

The Department for Work and Pensions (DWP) has finally published its response to the consultation on Flexible Retirement and Pension Provision (originally issued back in October 2007), together with a new consultation on alternative sets of draft regulations. These draft regulations set out two distinct options for a further exemption to the age discrimination legislation to cater for flexible retirement.<sup>3</sup>

#### ***Further flexible retirement consultation***

Many employers decided to defer their decision on a flexible retirement policy until more guidance was available and industry standards had emerged. However, the responses to the consultation generally illustrate a continued lack of consensus on the issue of flexible retirement and age discrimination.

The consultation (to which Sackers are responding) closes on 10 March 2009.

#### ***Guaranteed Minimum Pensions (GMP) conversion - Government response to consultation<sup>4</sup>***

Amendments made to the Pension Schemes Act 1993 by the Pensions Act 2007 included a facility to allow contracted-out occupational pension schemes to convert members’ GMPs into ordinary scheme benefits.

#### ***Converting GMPs into scheme benefits***

Draft amending regulations to effect this were published for consultation in September 2008 and the DWP has now published its response to the

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<sup>1</sup> For more details, please see our Alert: “When draft regulations are born!” dated 10 December 2008

<sup>2</sup> The Occupational and Personal Pension Schemes (Consultation by Employers and Miscellaneous Amendment) Regulations 2006

<sup>3</sup> For more details, please see our Sackers Extra Alert: “Flexible Retirement - What the Dickens?” dated 22 December 2008

<sup>4</sup> For more details, please see our Alert: “GMP Conversion - the facts” dated 9 September 2008, together with our response to the consultation, both of which are available from the client area of our website

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consultation. We can expect the final version of the Occupational Pension Schemes (Contracting-out) (Amendment) Regulations 2009 to be laid before Parliament “shortly” and “to come into force in April or May 2009”.

## LEGISLATION

### Pensions Act 2008

#### *Royal Assent*

Having received Royal Assent on 26 November 2008, the Pensions Act 2008 (the Act) will come into force in stages between now and 2012.<sup>5</sup>

Although the main purpose of the Act is to establish a framework for the new personal accounts regime, it also contains a number of important measures for existing occupational pension schemes, including:

- *Anti-Avoidance*<sup>6</sup>: Inspired by Government concern over the introduction of “business models that look to sever the link between the employer and scheme” (seen as potentially undermining the traditional employer/trustee relationship to the possible detriment of members) TPR has been given a number of new anti-avoidance powers. These include a new power to impose contribution notices based on a “material detriment test”. (TPR has recently consulted on a draft code of practice which outlines the circumstances in which it expects to issue contribution notices based on this test.<sup>7</sup>)
- *Reduction in cap on revaluation*: From 6 April 2009, the statutory cap on revaluing defined benefit pensions in deferment will be reduced from 5% to 2.5%. Whether or not this change will apply automatically for future service will depend on the drafting of a scheme’s rules.
- *Scheme funding*: since 26 January 2009, TPR has had the power to intervene in funding decisions if it considers that the trustees have failed to comply with prescribed requirements.
- *Appointment of trustees*: also from 26 January 2009, TPR has the power to appoint trustees to schemes where it considers it “reasonable” to do so (previously the test was whether the appointment was “necessary”).
- *Abolition of safeguarded rights*: the legislative requirements relating to “safeguarded rights” (pension credit benefits derived from contracted-out rights) will be abolished with effect from 6 April 2009.

*Material detriment test*

*Lower statutory cap on revaluation*

### HM Revenue & Customs (HMRC)

#### *The Taxation of Pension Schemes (Transitional Provisions) (Amendment) Order 2008*

##### *Bridging pensions*

The Finance Act 2004 includes rules about what qualifies as a “scheme pension” (and therefore an authorised payment). As part of these rules, once in payment a scheme pension cannot generally be reduced (and remain

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<sup>5</sup> For more details, please see our Alert: “Pensions Act 2008 - the Road to 2012” dated 5 December 2008

<sup>6</sup> For more details, please refer to our Alerts: “Proposed extension of anti-avoidance powers” (16 April 2008) and “Anti-avoidance powers - update” (22 October 2008)

<sup>7</sup> The consultation period ran from 15 December 2008 until 6 February 2009

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“authorised” for tax purposes), except in specified circumstances (for example, arrangements for “bridging pensions”).

For some schemes, the reduction which could be made to bridging pensions under scheme rules before A-Day (6 April 2006) was greater than can currently be paid as an authorised payment. This exposes schemes (and members) which continue to make such reductions to additional tax charges (or to the potential financial burden of having to pay a larger pension than intended under the scheme’s rules).

*Bridging pension reductions are authorised payments*

This Order allows pensions in payment before 3 July 2007 (to individuals who were members of the scheme on 5 April 2006) to be reduced in accordance with their pension scheme’s pre-A-Day rules, without causing future pension payments to be treated as unauthorised.

### ***The Pension Schemes (Reduction in Pension Rates) (Amendment) Regulations 2009***

As a further exception to the general rule that pensions should not generally reduce once in payment, all scheme pensions being paid can be reduced at the same rate. However, where a scheme is winding-up in deficit, only some members’ benefits (not all) may need to be cut back. Affected individuals may then find that their future pension payments are subject to unauthorised payments charges.

*Reductions on winding-up*

The draft regulations will address this issue by permitting pensions which are reduced in these circumstances to continue to be paid as authorised scheme pensions under the Finance Act. This will apply to schemes with 20 or more members when the winding-up began.

## **Department for Work and Pensions (DWP)**

### ***The Financial Assistance Scheme (Amendment) Regulations 2008***

These regulations (which came into force on 23 December 2008) will permit a small number of occupational pension schemes which could not previously qualify either for the Financial Assistance Scheme (FAS) or for the Pension Protection Fund (PPF), to qualify for assistance from FAS.

*Qualifying criteria expanded*

Schemes will qualify if:

- they started winding-up between 6 April 2005 and 22 December 2008;
- an insolvency event has occurred in relation to the scheme employer in the period before 6 April 2005; and
- there has not been a subsequent insolvency event in relation to the scheme employer which would be a qualifying insolvency event for the PPF if the scheme were an eligible scheme.

## **REGULATORY**

### **HM Revenue & Customs (HMRC)**

#### ***Lifetime Allowance (LA) protection - notification guidance and deadlines***

The deadline for registering for either primary or enhanced protection is looming. Although the deadline is technically 5 April 2009, because this is a Sunday, HMRC are allowing individuals until midnight (the end of the day) on 6 April 2009 to submit their forms.

*Register by 6 April 2009*

HMRC has published guidance on notification for LA protection purposes. If the

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deadline is missed without reasonable excuse, an individual will not be able to benefit from protection against the LA tax charge (55% if taken as a lump sum, or 25% if taken as a pension).

## HM Treasury

### ***Pre-Budget Report 2008***

Announced on 24 November 2008, the Pre-Budget Report proposed the freezing of both the LA and the annual allowance at £1.8 million and £255,000 respectively from 2010/11 until the end of the tax year 2015/16.

*Lifetime and annual allowances frozen*

Other pension proposals include:

- an increase in the level of a full State Pension to £95.25 a week (from the current level of £90.70) from April 2009; and
- an increase in the weekly rate of voluntary Class 3 National Insurance Contributions (NICs) for the 2009/10 tax year to £12.05 per week (from £8.10). (This supports a provision in the Pensions Act 2008 which relaxes the time limits for the payment of voluntary NICs by individuals approaching State Pension ages).

The Chancellor is due to make his Budget statement on 22 April 2009.

### ***Equitable Life – Government response to the Report of the Parliamentary Ombudsman’s investigation***

In January 2009, the Government published its response to the Parliamentary Ombudsman’s report into the collapse of Equitable Life.

The Ombudsman made ten determinations of maladministration against the former Department of Trade and Industry, the Government Actuary’s Department, and the Financial Services Authority in relation to their regulation of Equitable Life, and upheld the general complaint that there was regulatory failure for more than a decade in the period before Equitable Life closed to new business in 2000.

The Government has accepted some (but not all) of the Ombudsman’s findings. However, it intends to set up a scheme to provide ex-gratia payments for those who have been most disproportionately affected. The Rt Hon Sir John Chadwick (former Lord Justice of the Court of Appeal) has been asked to advise the Government.

*Compensation for Equitable Life policyholders?*

The Government has apologised to policyholders “on behalf of public bodies and successive governments responsible for the regulation of Equitable Life between 1990 and 2001, for the maladministration we believe has taken place.”

## National Association of Pension Funds (NAPF)

### ***Pension Provision and the Economic Crisis: New survey from the NAPF***

The NAPF’s latest survey on “Pension Provision and the Economic Crisis” hit the headlines after it was published in late January 2009.

The survey looks at the economic crisis from the perspective of both employers and employees and includes an action plan for the Government, regulators and the industry.

*Survey reveals possible changes on the horizon for some*

Among other things, the report notes that:

- half as many employers as in July 2008 predict “no changes” for existing members of open private sector defined benefit schemes; and

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- only 33% of respondents with defined benefit schemes which are currently open to future accrual for existing members, but closed to new members, considered there would be no further changes to their scheme – this compares with 50% of respondents to the July 2008 survey.

## **Pension Protection Fund (PPF)**

### ***PPF confirms levy estimate for 2009/10***

The PPF has confirmed that it has set a pension protection levy estimate of £700 million for 2009/10. This is in line with its August 2007 announcement that it would set a levy estimate of £675 million for the next three years, indexed to wages, so long as there was no significant change in risk. The PPF has also confirmed a final levy scaling factor (which schemes can use to calculate their individual levy bills) of 2.22.

*Levy scaling factor set at 2.22*

The publication of the final levy scaling factor in advance of the 2009/10 levy year is intended to help levy payers with their financial planning and provide further certainty. The PPF has responded to industry feedback during the consultation on the 2009/10 levy by making minor changes to its other 2009/10 proposals, which are set out in its policy statement.

### ***Consultation on including longer-term risk***

In November 2008, the PPF unveiled proposals to “make the pension protection levy paid by eligible pension schemes more tailored than ever before to the individual risk those schemes pose to the PPF.”

*Consultation on the future of the PPF levy*

Two key features of the proposals are to:

- assess the probability of a scheme’s sponsoring employer going bust during a five year period, as well as separately assessing the probability of it becoming insolvent during a one year period (as now);
- take account of the risk that a scheme’s investment strategy poses to the PPF when calculating its individual levy.

The PPF anticipates that the inclusion of longer-term risk when calculating individual levies will be fairer for levy payers. The PPF has also said that it expects these proposals to reduce the volatility seen in the current formula, which will help make individual levies more predictable.

### ***Deadlines for contingent assets and guidance on “Exchange”<sup>8</sup>***

For the 2009/10 levy year, the deadlines for submitting certificates are:

- contingent assets – 5pm on 31 March 2009;
- deficit reduction contributions (special contributions paid into a scheme since the last actuarial valuation to reduce any deficit) – 5pm on 7 April 2009; and
- notification of full (100% of assets and liabilities) or partial block transfers – 5pm on 7 April 2009.

For the first time, schemes will be able to use “Exchange” (TPR’s on-line service) to submit all voluntary certificates for contingent assets, deficit reduction contributions and block transfers (however, supporting documentation will still need to be submitted in hard copy to the PPF). The PPF has issued guidance about the information which eligible pension schemes

*Voluntary certificates to be submitted via “Exchange”*

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<sup>8</sup> For more details, please see our Alert: “Contingent Assets - Hurry while stocks last!” dated 23 January 2009

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need to provide so that their pension protection levies can be calculated correctly.

### **Revised Commutation Factors, Compensation Cap Factors and Early Retirement Factors**

The PPF has revised commutation, compensation cap and early retirement factors. These factors have been revised to reflect changes in market yields and, following a consultation with the actuarial profession, the changes in the methodology used to set the valuation assumptions.

The new factors should be used for all determinations for PPF compensation, and section 143 and section 179 valuations with an effective date on or after 1 January 2009.

### **New Chief Executive**

With effect from 1 April 2009, Alan Rubenstein will become the new chief executive of the PPF, taking over the role from Partha Dasgupta.

A former managing director of Lehman Brothers, Mr Rubenstein is a qualified actuary, former Vice-Chairman of the NAPF and chairman of its Investment Council. He is also on the Management Board of the UK Actuarial Profession and a Council Member of the Faculty of Actuaries.

### **Trustee Good Practice Guide**

The PPF has published new guidelines for trustees who are managing pension schemes through a PPF assessment period.

The guide is designed to help affected trustees take their scheme through the assessment period effectively and efficiently. In particular, it aims to help trustees understand more about the assessment period itself, as well as the PPF's expectations of trustees during an assessment period.

## **The Pensions Regulator (TPR)**

### **Scheme Funding: Analysis of recovery plans and clearance applications**

TPR has published a report outlining its findings in the context of scheme funding (where recovery plans have been put in place) and clearance applications.

TPR notes that recovery plan data shows that positive steps are being made to address deficits, but that recovery plans were, for the most part, set in "economically benign circumstances". Highlights from the report include:

- an increase of technical provisions from 107% to 119% of s.179 (PPF) liabilities. The average technical provisions funding level also increased from 86% to 90%;
- the strengthening of longevity assumptions. The average assumed expected age at death for a 65 year old man increased from 85.3 to 86.0 for current pensioners and from 86.5 to 87.6 years for future pensioners who are currently aged 45;
- the reduction of the average recovery plan period from 9 to 6 years (weighted by scheme size); and
- a downward trend in clearance applications, which TPR puts down to increasing industry understanding of TPR's requirements and a decline in merger and acquisition activity.

The report also notes that the economic factors affecting recovery plans over

*New factors for PPF  
compensation on or after  
1 January 2009*

*Guidance for trustees of  
schemes in a  
PPF assessment period*

*Downward trend in  
clearance applications*

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the next year are expected to be very different and that reactions to economic circumstances in preparing a recovery plan are likely to be complex. Given that companies might suffer short-term stresses in the near-term but recover soon after, TPR suggests that “the appropriate solution to an increase in the deficit in such a situation may be the introduction of a back-loaded recovery plan and other safeguards for members’ security, rather than simply increasing the recovery plan length”. In any event, TPR expects to see trustees keeping existing recovery plans and the employer covenant under review.

### *Fresh approach to recovery plans during recession*

#### ***Clearance and abandonment guidance updated***

TPR has made minor amendments to its guidance on clearance and on the abandonment of defined benefit pension schemes, to ensure that they reflect changes made by the Pensions Act 2008.

While there have been no changes to the clearance process, changes have been made to the guidance “for accuracy”, which are intended to reflect, among other things:

- the factors for TPR to consider where relevant when deciding whether a contribution notice would be reasonable;
- the additional mandatory requirement for TPR to consider the reasonableness of a party’s actions in the circumstances when deciding whether a contribution notice would be reasonable;
- and the removal of the good faith escape clause applicable to contribution notices.

### *Minor amendments made*

The guidance does not yet address the new material detriment test for imposing contribution notices (or the associated statutory defence), but TPR is expected to produce additional guidance materials to cover these issues in due course.

#### ***Record Keeping – response to consultation***

TPR has published a report on the responses received to its July 2008 consultation on the importance of good record keeping.

Aimed primarily at scheme administrators, the consultation explained why good record keeping is an essential component of pension scheme administration and identified some of the problems encountered as a result of poor record keeping practices.

The final guidance has moved away from TPR’s original proposal that measurement of data should be based on a series of simple tests on member data (based on “core”, “additional” and “numerical” data) to give an indication of the completeness of that data. Instead, tests of “common” and “conditional” data have been proposed. Common data applies to every member of any type of scheme, whereas conditional data is dependent on the type of scheme, scheme design and system design. It will be up to trustees, providers and administrators to determine which conditional data items are relevant to their scheme.

## **Personal Accounts Delivery Authority (PADA)**

#### ***Decumulation Consultation***

PADA (the organisation tasked with designing and implementing the new personal accounts scheme) has launched a consultation on “Securing a retirement income” which considers the options for helping members to get a good deal when they retire.



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The personal accounts scheme will not provide annuities, but PADA intends to ensure that members have clear information about the decisions they need to make, and how they can buy one. As well as informing members about the open market option, it is proposed that personal accounts members will have access to a panel of providers who agree to meet certain conditions set by the scheme. It is hoped that this will help to simplify the buying process for members.

### **Annuity purchase and personal accounts**

The consultation closes on 4 March 2009. PADA intends to publish a summary of responses by 4 June 2009.

#### **Procurement process**

PADA has also launched a procurement process for scheme administration services for personal accounts.

The services to be procured include: employer participation; enrolment; collection and reconciliation; cash management; accessing pension savings; and administration of account (i.e. updating member and employer records; complaint handling; divorce and dissolution of civil partnerships).

### **Administration of personal accounts**

As a public body, PADA is procuring services for the personal accounts scheme via the public sector procurement processes. This means that services are bought through “fair and open competition in accordance with European Union procurement directives.”

PADA is expected to make an announcement on the award in the summer of 2010.

## **CASES**

### **High Court**

#### ***Foster Wheeler Limited v Hanley & Others*<sup>9</sup>**

The High Court has confirmed that there is no “one size fits all” method for equalising benefits for men and women in the light of the *Barber* judgment.<sup>10</sup> Trustees have discretion to choose their method of equalisation.

### **No “one size fits all” method of equalisation**

In the Court’s most recent equalisation foray, the company and trustees had closed the *Barber* window (i.e. the period between 17 May 1990 (the date of the decision) and a valid rule amendment to equalise benefits) by means of implied consent (effectively allowing members to take benefits unreduced between 60-65). Construing the scheme rules, the judge concluded that where members have mixed accrual (with normal retirement ages of 60 and 65 inside and outside respectively of the *Barber* window) they can take *all* of their benefits from age 60.

The requirement for consent was therefore inapplicable.

Leave has been granted for appeal to the Court of Appeal and we therefore await developments in this case.

#### ***Capital Cranfield Trustees Limited v Beck and Tabor***

Closure of the *Barber* window was also the focus of this case which concerned a scheme in an assessment period for PPF purposes. The PPF needed the trustee to obtain confirmation as to whether the *Barber* window had been

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<sup>9</sup> For more details, please see our News: “All things being equal” dated December 2008

<sup>10</sup> *Barber v Guardian Royal Exchange*, European Court of Justice, 17 May 1990

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closed effectively, because the exact extent of the scheme's deficit would depend on this.

An announcement issued in 1994 was not effective to equalise benefits - being unsigned, it did not meet the amendment requirements of the scheme's rules. The judge therefore had to consider whether the definition of normal retirement date (NRD) in the scheme rules was flexible enough to permit the change of NRD which had been envisaged.

NRD was defined as age 60 for female members who joined the scheme before 30 September 1992 and age 65 for "any other member" or "*such day as the Employers shall determine in any particular case and notify in writing to the member concerned.*"

The judge concluded that the flexibility in this definition was confined to a particular case (or particular cases) only. As the 1994 announcement sought to alter the scheme rules in general (rather than in a particular case), it could not be said to alter the rules effectively. In addition, extending the definition of NRD more widely would amount to an attempt to create a new amendment power, which would be without any of the safeguards expressly provided for in the existing amendment power.

As a result, it seems that the *Barber* window under this scheme was never closed. This means that the liabilities are likely to increase (as male members' benefits are brought into line with female members' benefits for service from 17 May 1990).

*Barber window never closed*

## **Pensions Ombudsman (PO)**

### ***Peck v (1) First Group plc (2) The First UK Bus Pension Scheme Trustee Limited***

Employees may be bound by the terms of a collectively bargained pay and benefits agreement, even if their contracts of employment do not expressly permit amendment by such deals.

Peck was a member of the First UK Bus Pension Scheme but not a member of the recognised union. Neither Mr Peck's conditions of service nor his employer's standard terms and conditions of employment referred to collectively bargained agreements.

*Collectively bargained pay agreement binds non-union member*

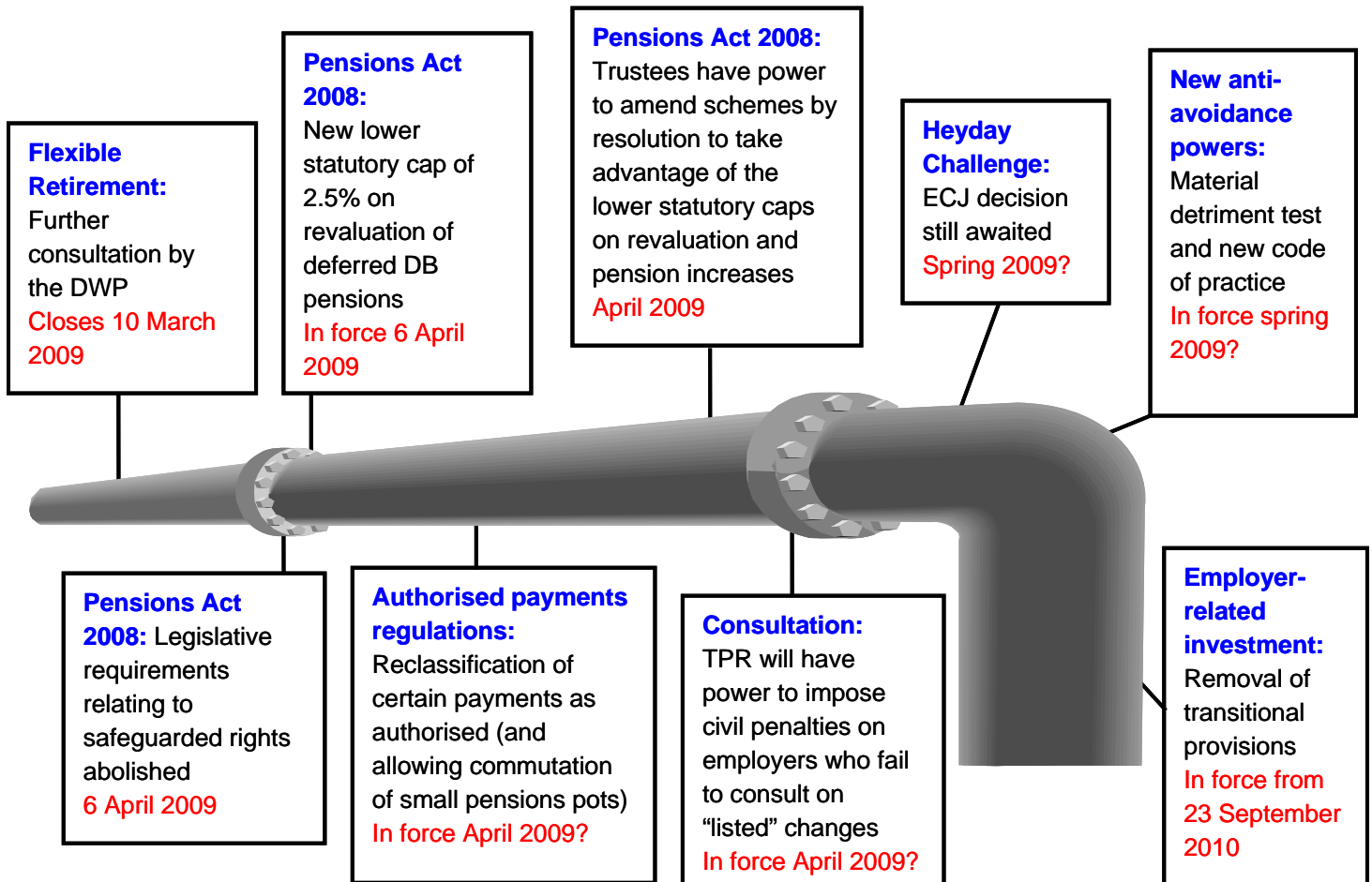
In 2005, employees were offered a "Total Rewards" package, which included a pay rise but rendered any salary increase above the increase in the retail prices index from April 2006 non-pensionable. The rewards package was accepted following a union ballot and the trustee agreed to make the necessary amendments to the scheme. Peck challenged the legality of the amendments.

The Ombudsman determined that union involvement in a pension scheme is not of itself inappropriate. Even though there was no express term in Peck's contract permitting variation by collective bargaining, such a term could be implied on the basis of previous dealings between the parties. (The union had been in operation since Peck's employment commenced and Peck had not previously objected to changes to his contract introduced following collective bargaining).

Because Peck had continued in employment and benefited from the pay rise he had, by his conduct, accepted the Total Rewards package. The trustee had therefore acted correctly in agreeing to the consequential scheme amendments.

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## IN THE PIPELINE



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