Sackers

The Quarterly

March 2013

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

The Quarterly March 2013

In this issue

Abbreviations commonly used in the Quarterly:

Alert/News: Sackers Extra publications (available from the Sackers Extra area of our website or your usual contact)

AA: Annual Allowance

DB: Defined Benefit

DC: Defined Contribution

DWP: Department for Work & Pensions

GAD: Government Actuary's Department

GMP: Guaranteed Minimum Pension

LEL: National Insurance Lower Earnings Limit

LGPS: Local Government Pension Scheme

LTA: Lifetime Allowance

NEST: National Employment Savings Trust

NICs: National Insurance Contributions

PAYE: Pay as you Earn

PPF: Pension Protection Fund

RPI: Retail Prices Index

SPA: State Pension Age

TPR: The Pensions Regulator

UEL: National Insurance Upper Earnings Limit

On the cover: Fuat Sami (Partner) and Michaela Berry (Partner)

Current Legal Agenda

There is more information on the latest developments on page 2

Automatic enrolment

Since its introduction in October 2012, auto-enrolment has been continuing to keep employers and schemes busy. 2013 will be a big year for many, as employers with 500 or more people in their PAYE scheme will come within scope by the end of the year.

DC schemes

For more on TPR's DC approach, see page 6

With DC a popular choice for auto-enrolment, TPR continues its drive to set the standard for DC schemes. As part of this process, TPR is consulting on a new code of practice and regulatory guidance, as well as its proposed regulatory approach for the administration and governance of work based DC pension schemes.

The new DC regulatory framework will be based on delivering good member outcomes and built around DC quality features that represent the standards and behaviours that TPR expects trustees to attain.

PPF contingent assets

Deadlines for 2013 are set out on page 7

Ahead of this year's PPF levy deadline, the PPF has revised its contingent assets guidance. The guidance now contains useful detail which will help with certification and may change the approach taken. Employers and trustees who have or who are intending to use guarantees (or other forms of contingent asset) for PPF purposes should get in touch with their usual Sackers' contact.

DB scheme funding

For details of the Government's call for evidence, see page 6

In April 2013, TPR is due to publish its second annual statement on scheme funding, with the aim of helping schemes with valuations falling in the year from September 2012.

The Chancellor's Autumn Statement announced a consultation on a possible new statutory objective for TPR and the potential smoothing of discount rates in actuarial valuations. Both of these are now the focus of a call for evidence by the DWP.

The new statutory objective would require TPR to consider the long-term affordability of deficit recovery plans for sponsoring employers, with a view to ensuring that DB regulation does not inhibit investment and growth. TPR has confirmed that, for now, it remains "business as usual" until such time as a new objective is in place (which, if introduced, is unlikely to be before 2014).

As regards discount rates, the DWP is looking at whether to allow companies undergoing valuations this year to use smoothed discount rates, recognising that "volatility in measures of pension schemes deficits can make it hard for companies to manage their investment plans and attract external funding."

Investment matters

A key area of focus for pension schemes as investors includes the NAPF's new Stewardship Policy which is designed to give pension funds a "clear roadmap" to address their responsibilities as investors.

For more details of this and other issues affecting pension scheme investors, please see the latest edition of our **Investment Briefing**, which will be available from the end of February 2013.

Automatic Enrolment

Auto-enrolment Underway

Thresholds for 2013/14

Auto-enrolment thresholds revised

Revised auto-enrolment thresholds for 2013/14 will be introduced from 6 April 2013:

- the earnings trigger has been set at £9,440, to tie in with the PAYE personal allowance. This is the minimum level of earnings payable for an individual to qualify as an "eligible jobholder"; and
- the qualifying earnings band (on which contributions are payable to eligible jobholders) will be £5,668 - £41,450 (the LEL and UEL respectively).

While the auto-enrolment trigger and the lower limit of the qualifying earnings band have both been increased, the upper limit of the qualifying earnings band has been reduced, in line with the reduction in the UEL.

Hybrid schemes: Protection for auto-enrolment savers

The Government has announced[1] that it intends to ensure that transitional arrangements that were designed for companies with DB or hybrid pension schemes are only used for workers who have access to defined benefits.

Closure of loophole for hybrid schemes

Current rules allow companies with DB or hybrid schemes to defer auto-enrolment until 2017. An amendment to the Pensions Act 2008 (to be retrospective to 19 December 2012) will tighten the rules to ensure that only employers offering defined benefits to a jobholder (whether in a DB or a hybrid scheme) will be able to defer auto-enrolment until 2017. All eligible jobholders without access to defined benefits will need to be automatically enrolled from their automatic enrolment date (but their employer can take advantage of the phasing-in of DC contributions).

National Employment Savings Trust

NEST restrictions under review

NEST is the Government established, UK wide, trust based occupational pension scheme that is available for any UK employer to use to meet its auto-enrolment duty.

Having reviewed responses to a call for evidence on two of the existing constraints in the NEST scheme – the annual contribution limit of £4,400[2] and the restriction on transfers to and from the scheme – NEST acknowledges[3] that there is a "strong case" for removing these restrictions. To do so would remove complexity and the administrative burdens for employers and allow NEST members to take active decisions about their retirement savings that other pension scheme members currently benefit from. NEST's response suggests that the restrictions should be removed by spring 2014.

Larger DC schemes display more quality features

TPR has published research[4] in connection with auto-enrolment which suggests that larger DC schemes (those with 1,000 or more members) are more likely to display the quality features necessary for good outcomes for retirement savers than small or medium sized schemes.

1 In a written ministerial statement (19 December 2012)

2 In 2012/13 earnings terms

3 NEST Corporation response on Supporting automatic enrolment (1 February 2013)

4 Principles and features of good quality pension schemes: Initial analysis of the presence of the regulator's defined contribution quality features in FSA regulation of work-based personal pension schemes (3 January 2013)

Pensions Reform

State Pensions

Introduction of a single tier flat rate state pension[5]

A DWP Pensions White Paper[6] confirms that a flat rate state pension of £144 per week[7] will be introduced from 2017 (at the earliest). All individuals with a NICs record of 35 years will be eligible for the flat rate pension.

Introduction from 2017?

There will be a period of transition to the flat rate state pension, designed to ensure that individuals who would have been entitled to a higher payment than the new flat rate pension at the date of the change will not lose out. Affected individuals will be entitled to a top-up.

A draft Pensions Bill to implement these measures was published in January 2013.

State pension age

The draft Pensions Bill also sets out a more structured framework within which to consider changes to SPA in future. The new structure provides for:

Framework for future changes to SPA

- a periodic review of SPA, with the first review in the next Parliament;
- the review to be based around the principle that people should expect to spend a certain proportion of their adult life in retirement; and
- the review to be informed by reports from GAD analysing the proportion of adult life people reaching SPA within a specified time period can expect to spend in retirement.

Cessation of DB contracting-out

One consequence of the move to a single tier state pension is that contracting-out for DB schemes will be abolished.

It is intended that past service contracted-out rights will be retained within schemes, meaning that schemes will be required to retain records and continue to apply the restrictions attached to DB contracted-out benefits (unlike the position for most schemes affected by the abolition of DC contracting-out).

End of DB contracting-out on the horizon

In addition, the contracting-out rebate will no longer be available. The rebate is currently paid to schemes that are contracted-out on a DB basis to reflect the fact that they provide benefits in place of the state second pension. The total rebate (for employer and member) is 4.8%, which includes a rebate of 3.4% for sponsoring employers.

The draft Pensions Bill includes a general power to amend schemes to reflect the abolition of DB contracting-out, including a mechanism for employers to amend scheme rules without trustee consent to reflect the loss of this rebate. However, much of the detail will be included in regulations which are due to appear in draft once the Bill has been formally introduced to Parliament.

5 Please see our Alert: "Pensions White Paper" (15 January 2012)

6 Single-tier pension: A simple foundation for saving (14 January 2012)

7 Using today's prices

Pensions Tax Issues

Reduction in the Annual and Lifetime Allowances

Further reductions from 2014/15

In his Autumn Statement in December 2012, the Chancellor announced further reductions to the tax relief available to pension savers.[8] For the tax year 2014/15 onwards:

- the AA for tax relief on pension savings will be reduced from £50,000 to £40,000; and
- the standard LTA will be reduced from £1.5 million to £1.25 million.

Transitional protection will be available in the form of "fixed protection 2014", based on the fixed protection regime introduced from April 2012. As with fixed protection, it will be possible to lose the new protection in certain circumstances, for example, where new contributions are paid to a DC arrangement or, in a DB arrangement, the member's pension and lump sum rights increase by more than a specified percentage at any time during the tax year.

The Government is also expected to consider whether to offer a form of personalised protection that 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. However, in contrast to fixed protection, it is envisaged that individuals with personalised protection would not be subject to restrictions on future contributions or accrual.

These changes have been included in the draft Finance Bill 2013,[9] which is due to be introduced formally to Parliament following the 2013 Budget.[10]

Pensions Drawdown

As an alternative to purchasing an annuity at retirement, a member may (if scheme rules allow) draw down cash from their pension pot to provide an income. The amount of drawdown pension that may be taken as income each year is the "annual amount" of a "relevant annuity" that the drawdown pensioner could have purchased.

Gender neutral pricing

Gender neutral annuity rates

Following the December 2012 deadline for implementation of the *Test-Achats*[11] case, regulations[12] have been introduced which provide for male and female drawdown pensioners to be treated the same from 21 December 2012, by providing that the maximum drawdown pension for women is calculated using the existing male rates. As a result, the maximum drawdown rate for female pensioners was increased, with no impact on the maximum drawdown pension that men may take.

Drawdown cap

Capped drawdown rate to increase

Quite separately, George Osborne announced in the Autumn Statement that for capped drawdown arrangements, the annual amount would be increased from 100% of a "relevant annuity" to 120%. This is to allow flexibility as a result of the material drop in annuity rates.

8 Please see our Alert: "Autumn Statement 2012" (6 December 2012)

9 Please see our Alert: "Finance Bill 2013" (13 December 2012)

10 The Budget will be on 20 March 2013

11 *Association belge des Consommatuers Test-Achats ASBL* (Case C-236/09). Please see our Alert: "Is it the end of the road for sex-based actuarial factors?" (2 March 2011)

12 The Registered Pension Schemes (Relevant Annuities) (Amendment) Regulations 2012

Public Sector Pensions[13]

Implementing the changes to public sector pensions

Public Service Pensions Bill

Once in force, this Bill will create a unified legal framework to underpin the new public sector pension arrangements agreed in principle between the Government and the unions. Key changes include:

- a move from DB to career average pension schemes;
- the linking of normal pension age to SPA for most public sector workers; and
- improved governance arrangements, including regulatory oversight by TPR.

Fair Deal

The Fair Deal guidance sets out standards for protecting the occupational pensions of staff who are compulsorily transferred to private sector employers, for example on a public sector outsourcing.

Following consultation, the Government has confirmed that the Fair Deal will be retained but is now consulting[14] on revised guidance which would allow companies admission to the relevant public sector scheme in respect of transferred members (rather than providing their own "broadly comparable" pension arrangements).

Local Government Pension Scheme

Draft regulations[15] for the new LGPS (due to come into force in April 2014) are now available. They cover the core elements of the new scheme, in particular, provisions relating to membership, contributions and benefits.

In addition, GAD has published a statement[16] which sets out the effect of the new regulations on GAD's assessment of the "broad comparability" requirement for LGPS. In brief, no new applications for passport certificates against LGPS will be accepted, except where a short-term need can be justified. Existing certificates of "broad comparability" will not be invalidated as a consequence of the new regulations, but they will become invalid once the new regulations are in force for any transfer of staff which occurs on or after that date. Where applications for GAD certificates are currently in progress, it will be for the applicants to decide whether to continue to proceed – GAD will continue to process applications unless otherwise notified in writing.

Pension Increases

RPI Review

No change to RPI

Following a consultation in October 2012,[17] the Consumer Prices Advisory Committee has now confirmed[18] that there will be no change to RPI. However, an additional inflation measure – "RPIJ", based on the "Jevons" method which uses a geometric approach to calculating averages – will be adopted from March 2013. It is currently unclear what this additional index is to be used for, although it would be available in future as an alternative to RPI.

13 For more on the latest developments, please see our Public Sector Briefing (December 2012)

14 Consultation on the Fair Deal policy: response to the consultation (19 November 2012)

15 Local Government Pension Scheme 2014: Draft regulations on membership, contributions and benefits (December 2012)

16 Broad comparability work against the LGPS in England & Wales (29 January 2013)

17 Please see our Alert: RPI 2.0 – ONS consultation on changing the index (10 October 2012)

18 Please see our Alert: "RPI – No change" (10 January 2013)

Regulatory

Department for Work & Pensions

DB scheme funding[19]

Call for evidence

The DWP has issued a call for evidence[20] on whether there is a need for:

- legislation that would explicitly allow the "smoothing" of asset values and liabilities in funding valuations (i.e. averaging asset prices and discount rates over a longer period of time, instead of using current market spot rates), to counter the effects of the current economic situation; and
- a new objective for TPR to consider the long-term affordability of deficit recovery plans for sponsoring employers.

The Government plans to weigh up a number of factors, among them the interests of pension scheme members and the need to maintain the solvency and profitability of sponsoring employers, as well as the potential impact on the PPF levy and the wider economy. If the call for evidence ultimately prompts legislative change, the Government intends to bring forward more detailed proposals and implement changes "as soon as practicable in 2013".

The Pensions Regulator

Response to scheme funding announcements

Business as usual on scheme funding

Responding to the Government's proposals on scheme funding (first announced in the 2012 Autumn Statement[21] and outlined above), TPR has said[22] that it will continue to regulate in accordance with the existing regulatory framework, until such time as any changes are introduced. In the meantime, TPR has advised that trustees and sponsors should continue to develop their funding arrangements in accordance with TPR's April 2012 funding statement[23] and other related guidance, and in line with the statutory timetable.

Setting the standard for DC schemes

DC scheme standards

TPR is consulting on a package[24] of new measures for DC schemes, including a new code of practice and regulatory guidance, with the aim of boosting member outcomes for retirement saving.

The new framework will be built around quality DC features that represent the standards and behaviours that TPR expects to trustees to attain and is underpinned by TPR's six DC principles.[25] Occupational DC trust based schemes (excluding "micro schemes"[26]) will be expected to demonstrate how they comply with quality DC features or explain any inconsistency with them. Work based personal pensions (namely, contract based schemes) are to be considered separately, but TPR intends to apply similar principles in due course.

19 Please see our Alert: Pensions and Growth - A call for evidence (29 January 2013)

20 "Pensions and Growth": Whether to smooth assets and liabilities in scheme funding valuations / Whether to introduce a new statutory objective for the Pensions Regulator (25 January 2013)

21 Please see our Alert: Autumn Statement 2012 (6 December 2012)

22 In a statement on 5 December 2012

23 "Pension scheme funding in the current environment" (April 2012)

24 Please see our Alert: TPR sets the standard for DC schemes (15 January 2013)

25 Please see our News: "TPR's recipe for good DC provision" (October 2012)

26 Schemes with between 2-12 members, as TPR does not expect such schemes to be used for auto-enrolment

Report on UK Coal

TPR has published a report[27] explaining the actions that enabled the restructuring of the UK Coal group.

Following extensive discussions, a plan was agreed which has resulted in substantially all of the economic interest in the group transferring from shareholders to the trustees of the UK Coal Sections. TPR worked closely with the trustees and the group during negotiations and provided clearance for the restructuring.

Pension Protection Fund

PPF levy

The PPF has confirmed in its latest Levy Determination that the pension protection levy estimate will be £630 million.

Deadlines for 2013

Key diary dates[28] for the 2013/14 levy year are:

- 28 March 2013: Deadline for certification of new contingent assets and recertification of existing contingent assets;
- 28 March 2013: Deadline for submission of Scheme Return to TPR. Information from the Scheme Return is used in the calculation of the levies; and
- 30 April 2013: Deadline for submission of deficit reduction contribution certificates for contributions made up to and including 31 March 2012.

Contingent assets

Revised guidance

The PPF has updated its guidance for putting in place contingent assets, with a view to giving schemes greater assistance on the factors to consider when contemplating the use of guarantees as contingent assets.[29]

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

GMP equalisation

The PPF has confirmed that its method for calculating compensation for men and women to ensure that they are treated equally will apply to all pension schemes in a PPF assessment period.[30]

The PPF is writing to trustees of all schemes in assessment to explain how the changes will affect them.

27 Report under s.89 of the Pensions Act 2004 (7 January 2013)

28 The March dates are slightly earlier than usual because of Easter

29 Please see our Alert: “Contingent Assets 2013/14: Revised guidance on certification of guarantor strength” (10 January 2013)

30 PPF guidance: GMP equalisation

Achieving value for members

We have noticed a theme emerging in the last few months on achieving value for pension scheme members. This section provides a round-up of developments with this focus.

Defined Ambition

Government proposals for new style pension arrangements

Shared risk schemes on Government's agenda

In November 2012, the Government unveiled its strategy for "Reinvigorating workplace pensions". The proposals build on the Coalition Agreement commitment to put in place "arrangements that result in the provision of high quality pension schemes people can trust and take confidence in".[31]

A DWP paper outlines a number of so-called "Defined Ambition" arrangements, as a means of ensuring greater sharing of risk between employers and members. The paper also suggests possible improvements to existing arrangements.

Defined Benefit

Pensions incentive exercises

The draft Pensions Bill contains a power to ban the practice of providing incentives to encourage individuals to transfer their pension benefits from a salary related occupational pension scheme to an alternative arrangement.

Defined Contribution

Joint industry code of conduct on charges

A new non-statutory code of conduct on DC pension charges was published in November 2012.[32]

Encouraging clarity on DC charges

The Code aims to provide employers with clarity and transparency on charges, primarily to assist them in choosing an auto-enrolment scheme. It is intended to apply to all parties providing services to employers in setting up and administering pension schemes, including insurance companies, trust based schemes, financial advisers and benefit consultants. It also applies to unbundled trust based schemes and the default fund used for auto-enrolment purposes.

The Code does not replace existing regulatory requirements on disclosure.

Automatic transfer of pension pots

In December 2012, the DWP let it be known that it no longer intends to legislate to allow refunds of "micro pots". In the response[33] to its 2011 consultation[34] the DWP had agreed to explore the possibility of refunding the very smallest pots. However, having done further work to explore this option, it found that the practice of refunding very small contributions would be complex to administer, because of the need to separate the pots into their constituent parts of employer and employee contributions and tax relief, with different treatment of the contributions depending on the type of scheme (i.e. trust or contract based).

The DWP now intends that, following the introduction of the automatic transfer provisions for people moving between jobs, this will be the standard position for pots of any size. In this way, the Government aims to achieve value for members.

31 Please see our Alert: "The Government defines its ambition" (26 November 2012)

32 Please see our News: "New code aims to provide clarity on DC charges" (December 2012)

33 Government response to the consultation on improving transfers and dealing with small pension pots (17 July 2012)

34 Meeting future workplace pension challenges: improving transfers and dealing with small pension pots (15 December 2011)

Cases

High Court

IBM United Kingdom Pensions Trust Limited v IBM United Kingdom Holdings Limited; IBM United Kingdom and Metcalf

In October 2012, Warren J found that the IBM Pension Plan's Trust Deed and Rules should be rectified to provide an entitlement for active members to retire between the ages of 60 and 63 without employer consent. The rectification did not extend to deferred members as the judge concluded that the intention of both the employer and the trustees was to allow for payment of an unreduced deferred pension from age 63, and this was accurately reflected in the deed. This was the case despite the fact that, as rectified, the deed would not have complied with pre-Pensions Act 2004 preservation requirements.

In this connected case, the trustees claimed that the employer's failure to consent to an amendment to reflect the preservation requirements as they stood before the Pensions Act 2004, in respect of pre-6 April 2005 service, was a breach of its duty of trust and confidence.

Warren J concluded that IBM was not in breach of its duty of trust and confidence. The amendment for active members reflected the parties' intentions and was in line with what members had been told would be provided. The fact that the amendment failed to take account of more stringent legislative requirements that were no longer in force did not mean that more favourable terms needed to be provided now.

No breach of the duty of trust and confidence

Warren J's summary of the employer's duty of trust and confidence is useful while we wait for a more thorough examination of the issue in the next instalment of the IBM litigation. We understand that this case will reach the courts in February 2013.

Employment Tribunal

Walker v Innospec Limited and others

The Civil Partnership Act 2005 (CPA) came into force on 5 December 2005, enabling same sex couples to enter into a civil partnership. On the same date, an exemption was introduced to allow occupational pension schemes to exclude civil partners from certain benefits accrued prior to the Act coming into force. As a result, pension schemes are required, as a minimum, to provide civil partners with survivors' benefits relating to service on or after 5 December 2005 (and contracted-out benefits for accrual back to 1988). But quite separately, section 61 of the Equality Act 2010 requires every occupational pension scheme to have a non-discrimination rule read into it.

Mr Walker was a member of the Innospec Pension Scheme which provided for a 2/3rds spouse's pension (but for civil partners this benefit is only paid in respect of service on or after 5 December 2005). Mr Walker brought a claim that the Scheme had breached the Equality Act and that benefits should be provided to civil partners in respect of accrual before 5 December 2005 as well as from that date. The Employment Tribunal agreed. It concluded that there had been both direct and indirect discrimination against Mr Walker and that the provision in the scheme rules which restricted civil partners' benefits fell foul of the non-discrimination rule implied into all schemes by the Equality Act.

Tribunal found direct and indirect discrimination

This is a surprising decision. Schemes providing similar benefits to the scheme in this case (in accordance with the CPA exception) should note that Employment Tribunal decisions are only binding on the parties involved. We understand that the decision may be appealed and we will update you further when more information is available.

Sackers Extra Briefing:

Dates for your diary

Sackers Extra Briefing presents seminar and workshop style briefings addressing topical issues of current interest and relevance.

Member statements and overpayments Workshop	28/02/13	**Breakfast seminar (9:00am-10:30am)** A practical approach to dealing with misstatements and overpayments
Member statements and overpayments Workshop	05/03/13	**Lunchtime seminar (12:00pm-2:00pm)** A practical approach to dealing with misstatements and overpayments
Governance Workshop	12/03/13	**Lunchtime seminar (11:45am-1:00pm)** Gaining "trust" through preparation
Pension Managers' Forum	18/04/13	**Lunchtime seminar (11:45am-1:00pm)** Current issues for pensions managers
Quarterly Legal Update	02/05/13	**Breakfast seminar (9:00am-10:30am)** The latest legal and regulatory developments in the pensions world
Pensions for New Trustees - Workshop	14/05/13	**Breakfast seminar (9:00am-10:30am)** Getting up to speed with Trustee Knowledge and Understanding
Quarterly Legal Update	18/07/13	**Breakfast seminar (9:00am-10:30am)** The latest legal and regulatory developments in the pensions world
Employment issues Workshop	25/09/13	**Evening seminar (5:00pm-6:30pm)** The latest legal and regulatory developments in the pensions world
Quarterly Legal Update	14/11/13	**Breakfast seminar (9:00am-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 programme of regular seminars brings together pensions professionals to share and discuss knowledge and best practice. Part of this rolling programme is our "Quarterly" seminar, which focuses on the latest legal and regulatory developments in the pensions world. Our Quarterly video distils content from this seminar into a bite size chunk, highlighting some of the current key issues. You can access the Quarterly video and our "In focus" series of spotlights on specific pensions issues, by scanning the code with your smartphone or tablet.

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