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sackers extra

THE QUARTERLY

SEPTEMBER 2008

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.

In this issue

PENSIONS REFORM

Finance Act 2008

Royal Assent

Royal Assent

The Finance Act 2008 received Royal Assent on 21 July 2008. The Act implements the measures announced in the 2008 Budget (and pre-Budget report)[1] and paves the way for Regulations to be made under it.

The Registered Pension Schemes (Authorised Payments) Regulations 2008

Additional flexibility for schemes

These draft Regulations provide for a number of payments made by registered pension schemes to be authorised and to be taxed as such. The new authorised payments include:

- payments of pension paid in error;
- payments of arrears of pension (or commencement lump sums) after death;
- payments which continue for a short time after a member's death; and
- payments to or in respect of members who were previously untraceable.

The draft Regulations also relax the rules on trivial commutation, allowing certain "stranded pots" and benefits under £2,000 in a scheme to be commuted.

The Regulations are expected to be finalised and become law in the Autumn.

Companies Act 2006

Conflicts of Interest

Directors' conflicts

– authorisation required

From 1 October 2008, company directors will have a new statutory duty to avoid situations of conflict. (A classic situation in which this might arise is where a trustee director is also a director of the principal employer.)

Where a potential conflict exists, this may be authorised – either under the company's articles of association or by the board of directors. Any authorisation should ideally be given as soon as the potential for conflict arises, i.e. before or on appointment to the board. The parameters in which directors may continue to act should be clearly set out, rather than simply imposing a blanket authorisation. Directors will also be required to declare the nature and extent of any interest in an existing or proposed transaction or arrangement to the rest of the trustee board. A register of interests may be useful here, provided this is regularly brought to the board's attention.

A duty not to accept benefits from third parties will also mean that employers and trustee companies need to take care to ensure that any arrangements for remunerating trustee directors are appropriately structured.

These changes are in addition to the Pensions Regulator's draft Guidance on Conflicts for trustees, published for consultation in February 2008.[2]

[1] For more information, please see our Alert "Budget 2008 – What's in it for pensions?" dated 14 March 2008
[2] For more information, please see our Alert "Conflicts guidance – a high five from the Regulator" dated 29 February 2008

Pensions Bill 2008

Update

The Pensions Bill is still going through Parliament, a new version having been published on 18 July 2008. Key amendments proposed in this latest version include:

Anti-avoidance changes

- an amendment to the Pensions Act 2004 designed to bring into force the changes proposed by the recent consultation on the extension of the Pension Regulator's anti-avoidance powers[3];
- recognition that insurance-based workplace pensions can qualify as automatic enrolment schemes as an alternative to Personal Accounts from 2012, following confirmation from the European Commission that this is consistent with European law; and

Extension of automatic enrolment

- come 2012, a ban on "encouraging or forcing workers to opt-out of pension saving" by, for example, offering higher salaries or one-off bonuses. The Pensions Regulator will be responsible for enforcing this prohibition.

Protected Rights

SIPPs can hold protected rights

SIPPs and protected rights

Regulations will come into force on 1 October 2008 which will permit self invested personal pensions (SIPPs) to hold protected rights (rights referable to contracting-out on a money purchase basis). SIPPs wishing to hold protected rights will need to have a valid contracting-out certificate and applications can be submitted to HMRC prior to the legislation coming into force.

Maternity and Adoption Rights

No change

Pensions during maternity leave

Pension rights during maternity and adoption leave have not been straightforward for many years, as they are governed by several inter-linking pieces of legislation. Changes made to the Sex Discrimination Act 1975 (SDA) in April 2008 have added a further layer of complexity, posing the question whether for women expected to give birth on or after 5 October 2008, pension benefits need to be continued throughout the leave period.

Although the SDA has changed, the policy intention from the Government (expressed by BERR (the Department for Business, Enterprise and Regulatory Reform) and HMRC) appears to be that pension rights have not. Indeed, the Government has responded to concerns about this by providing additional amending legislation aimed at clarifying the issue (although this in itself is far from clear).

The upshot of this is that the position remains as currently, with pension benefits continuing during ordinary maternity leave, whether or not this is paid, but only continuing during any further period of leave (additional maternity leave) to the extent it is paid.

[3] For more information, see our Alert "Proposed Extension of Anti-Avoidance Powers" dated 16 April 2008 (to which Sackers submitted a response)

HMRC Guidance on Salary Sacrifice and Maternity Leave

Salary sacrifice and maternity pay

HMRC has published new guidance which looks at the impact which salary sacrifice arrangements have on Statutory Maternity Pay and what non-cash benefits employers should provide to their employees during statutory maternity leave following changes in the law from 2008.

Risk sharing

Consultation launched

DWP proposes new models of shared risk schemes

In July 2007, the Deregulatory Review of Private Pensions[4] identified that there could be advantages for employers and employees in sharing the risk in defined benefit (DB) schemes more evenly. Following a highly publicised campaign by the Association of Consulting Actuaries (ACA) (amongst others) in support of shared risk schemes, the Government has launched a consultation seeking views on their viability.

The consultation describes three main models of shared risk schemes: conditionally indexed career average schemes; conditional indexation for all DB schemes; and collective defined contribution (DC) schemes. Sackers will be responding to the consultation which closes on 28 August 2008.[5]

REGULATORY

HM Revenue & Customs (HMRC)

HMRC u-turn on anti-money laundering

HMRC u-turn

Since 15 December 2007, "trust or company service providers" (TCSPs) who are providing their services "by way of business" have been required to comply with certain anti-money laundering requirements, including registration with HMRC. As we reported back in February,[6] this definition may have included paid trustees.

On 31 July 2008, HMRC published revised guidance on who needs to register as a TCSP. Whilst the guidance could be clearer, the upshot is that occupational pension scheme trustees (both individual trustees and directors and secretaries of trustee companies) are generally excluded from the need to register. This is because one of the exclusions from registration specifically recognises that occupational pension schemes are a low risk area.[7]

Pensions for Adult Dependant Children

More transitional protection

HMRC has published a draft Order which will amend the Taxation of Pension Schemes (Transitional Provisions) Order 2006 to introduce further transitional provisions in relation to adult children who are dependants.

If adopted, this amendment will permit pensions to be paid on the death of a member to financially dependent children who are over age 23, or who have ceased full-time education or vocational training (where permitted by scheme rules on 6 April 2006, and those rules have not changed substantially).

[4] Lewin, C and Sweeney, Ed; July 2007 – Deregulatory Review of Private Pensions: An independent report to the Department for Work and Pensions
[5] For further information, please see our Alert: "Risk Sharing – the Government consults" dated 11 June 2008
[6] For more information, please see our Alert: "Trustees and the New Anti-Money Laundering Regime" dated 7 February 2008
[7] For more information, please see our Alert "Anti-Money Laundering – HMRC U-Turn" dated 31 July 2008

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The Pensions Regulator (TPR)

Draft guidance for trustees on the new transfer value requirements

New CETV rules come into force on 1 October 2008

With less than two months to go to the introduction on 1 October 2008 of the new requirements for calculating and verifying transfer values for members, TPR has published draft guidance designed to help DB scheme trustees understand and fulfil their new responsibilities.

The draft guidance covers:

- the calculation of a cash equivalent transfer value (CETV);
- disclosure requirements;
- the calculation of non-statutory transfer values; and
- DB transfers-in.[8]

Delayed introduction of longevity changes

In February, TPR issued a consultation on the regulation of DB schemes which set out a new approach to mortality assumptions. TPR suggested that these assumptions be used as a "trigger" for funding plans.

Longevity changes to apply from September 2008

Changes will not now apply until the beginning of the next DB scheme valuation cycle, starting in September 2008. This will impact on valuations and follow-up recovery plans that must be submitted to TPR by December 2009.

The reason given by TPR for the change is to ensure that it has sufficient time to fully consider all of the responses it has received to the consultation, and to clarify that the original proposed date of introduction did not mean that schemes needed to restart valuation processes that had already begun.

Consultation on record keeping

TPR has launched a new consultation which is aimed at those who are responsible for pension scheme record-keeping and those who administer schemes. The consultation period will end on 15 October 2008.

Importance of good record keeping

TPR notes that poor record-keeping can lead to significant additional costs in a number of areas (such as during buy-outs or wind-up) more expensive administration, claims from disgruntled members, and inaccurate actuarial valuations. These costs are ultimately borne by members, the employer, or both. TPR's consultation calls for views on some specific steps, to be implemented by providers and trustees, which TPR recommends as good practice.[9]

Guidance: relations with advisers

Best practice guidance

TPR has published guidance on "Relations with Advisers" to help trustees make the best use of the expertise that advisers and service providers can bring to a pension scheme.

The best practice guidance outlines key issues which trustees may wish to take into account when appointing a new adviser or when reviewing the

[8] For more information, please see our Alert: "Countdown to the new transfer value regulations" dated 30 July 2008

[9] The importance of good record-keeping was brought to the fore in the recent determination of the Deputy Pensions Ombudsman in *Tyler v. (1) Robert Fleming Benefit Consultants and (2) Minet Benefit Consultancy* which resulted in Minet having to compensate a member who had 'disappeared' from the scheme's records. For more information on this, please see 7 Days dated 4 August 2008

performance of an existing one, as well as providing tips on getting the best service from current advisers.

Q&A for DC Schemes

Additional DC guidance

The Q&As bring together key issues from TPR's guidance for DC schemes, providing links to other relevant guidance and the trustee toolkit where relevant.

The Q&As cover a number of topics including: regulation; governance; administration; investment; charges; retirement and member understanding. The guidance does not, however, include any new requirements over and above those which already exist.

Personal Accounts Delivery Authority (PADA)

Charging structure for personal accounts

Personal Accounts charging structure under consultation

The Pensions Act 2007 established PADA as a non-departmental public body. Its initial remit is to advise the Government about Personal Accounts so that policy takes full account of operational and commercial considerations. In line with this remit, PADA will make a recommendation on the charging structure for Personal Accounts.

The summary of responses to its January 2008 paper "Building Personal Accounts: choosing a charging structure, a discussion paper to support consultation" (the Discussion Paper) reveals that there is currently no clear consensus on the charging structure. Of the various options proposed in the Discussion Paper, most respondents were broadly split in favour of one of two options:

- an Annual Management Charge (AMC) only structure, favoured for its simplicity and transparency - although it would be slower to build scheme revenues than other options; or
- a contribution charge with an AMC, seen as the most sustainable of the options with flexibility to deal with a range of business risks - but likely to be perceived as complex by members.

PADA is expected to make a recommendation to the Department for Work and Pensions later this year.

Miscellaneous

Financial Reporting Standards – Consultation

Improvements sought for financial reporting

The Accounting Standards Board (ASB) has issued a Financial Reporting Exposure Draft on Improvements to UK Financial Reporting Standards (UK FRS). This seeks to maintain the existing levels of convergence between UK FRS and International Financial Reporting Standards and, where the UK FRS is based on its international equivalent, will incorporate improvements stemming from the international standard.

The ASB has also taken this opportunity to propose other improvements to UK FRS which have been brought to its attention. The deadline for comments is 27 September 2008.

Equitable Life Report: A decade of regulatory failure

The report of the Parliamentary Ombudsman, Ann Abraham, into the collapse of The Equitable Life Assurance Society (Equitable Life) was published on 17 July 2008.

Ten determinations of maladministration were made 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 in the period before 1 December 2001. Ms Abrahams has called upon the Government to apologise to Equitable Life policyholders for what her report describes as "serial regulatory failure", and to establish and fund a compensation scheme for those policyholders.

Serial regulatory failure

CASES

Age Discrimination Round-up

More age discrimination cases are beginning to come through the courts, both at national and European level.

Birgit Bartsch v Bosh und Siemens Hausgerate (BSH) Altersfursorge GmbH

"Age Gap" clauses

"Age gap" clauses were the theme of *Birgit Bartsch*. The Advocate General (A-G) of the European Court of Justice (ECJ) considered whether a rule in an occupational pension scheme which excluded entitlement to a survivor's pension if the survivor was more than 15 years younger than the deceased member was discriminatory.

Mrs B's claim failed because the time limit for transposing the framework directive on equal treatment (the Directive)[10] into national law had not passed when her claim to entitlement to a widow's pension arose. However, the A-G was of the view that there was no reason to exclude discrimination based on relative ages from the scope of the general principal of equality, as age was still the basis for a decision which had an adverse effect. The A-G's view was that the employer would not have been able to objectively justify this direct discrimination.

In contrast with the BSH scheme (which did not provide any benefit to a person caught by the age gap clause), age gap clauses commonly used in the UK tend to provide for the actuarial reduction of a widow or widower's pension where a person is, for example, more than 10 years younger than their spouse. It is arguable that age gap clauses which apply a reduction are more easily objectively justified than those which apply a suspension. Indeed, the Age Regulations[11] contain an exception covering this type of provision.

The A-G's opinion is not binding on the ECJ, and we await the final decision in this case which should appear towards the end of 2008.

MacCulloch v ICI plc

Objective justification

- legitimate aims

The Employment Appeal Tribunal (EAT) considered whether aims identified by an employer for using age and length of service criteria for paying benefits under a redundancy scheme were legitimate and could be used to justify differential treatment on grounds of age and length of service.

Mrs M received a lower payout under her employer's redundancy scheme than an older employee would have received. Both direct and indirect discrimination were alleged because the amount payable under the scheme related directly to age, and also to the number of years of service. The identified aims of the scheme were to: encourage and reward loyalty; provide higher payments to

[10] Council Directive of 27 November 2000 (2000/78/EC) establishing a general framework for equal treatment in employment and occupation

[11] The Employment Equality (Age) Regulations 2006

older workers who were more vulnerable in the job market; and provide a popular, generous scheme to encourage older workers to leave earlier, making way for younger workers and avoiding compulsory redundancies.

Although these aims were considered to be legitimate, the claim did not succeed for technical reasons.

Swann v GHL Insurance Services UK Ltd

Objective justification was also the subject of this recent Employment Tribunal case.

Employees were given a "flex fund" which they could use to acquire additional benefits from a range which included private medical insurance (PMI), additional pension contributions, additional life insurance, childcare vouchers, and gym membership.

Mrs S selected PMI cover, the cost of which increased with age. This led her to complain that this amounted to age discrimination.

Flex fund discrimination was objectively justified

The Tribunal held that because the basic flex fund was overall age neutral (and employees had freedom to decide how they used their fund from a range of options), the employer was able to pass on the enhanced premiums of the insurer (which were based on both age and gender) to its employees, without this amounting to age discrimination. The Tribunal also considered the main aim of the scheme – which was to enhance the recruitment and retention of staff – and found this to be legitimate. Consequently, introducing the scheme was a proportionate means of achieving that aim.

High Court

Hearn v Dobson[12]

This very technical case concerned the application of the Scheme Funding Regulations[13] to a multi-employer scheme and, in particular, whether the creation of a separate fund under the scheme rules should be treated as a separate fund for the purposes of the scheme funding provisions of the Pensions Act 2004.

Background

Partial closure rule operated

Construction Confederation (CC) was the principal employer of the Construction Confederation Staff Pension Scheme (the Scheme). Three other employers participated in the Scheme: the Home Builders Federation Limited (HBF), Housebuilder Media Limited (HBM) and Civil Engineering Contractors Association (CECA).

The Scheme was closed to new members with effect from 1 January 2003.[14] Over the course of 2005 and 2006, HBF, HBM and CECA each gave notice that they wished to withdraw from the Scheme and to terminate their liabilities in respect of their employees.

When an employer terminates its liability to the Scheme, under the rules the Trustees had to set up a "Separate Fund". The Trustees were not required to (but could) allocate particular assets to a Separate Fund, they simply needed to record the value of the Separate Fund.

[12] For a more detailed summary of this case, please see 7 Days dated 11 August 2008
[13] The Occupational Pension Schemes (Scheme Funding) Regulations 2005
[14] The Scheme was subsequently closed to future accrual for CC employees after 30 April 2006

The key question identified by the judge was, when the Trustees create a Separate Fund, is that treated as a separate scheme under Paragraph 1 of Schedule 2 to the Scheme Funding Regulations?

Limit on liability?

- If a separate scheme was created, the assets and liabilities attributable to a Separate Fund created in respect of HBF and HBM would be limited to those employers.
- But if a separate scheme was not created, other employers, effectively CC, would be required to take into account the assets and liabilities of the Separate Funds when determining the overall rates of contributions payable by it.

Decision

No separate scheme was found to have been created within the meaning of the Scheme Funding Regulations. This had the effect of increasing the liabilities attributable to CC (and potentially its contributions to the scheme).

For sections of a scheme to be treated as separate schemes for the purpose of the Scheme Funding Requirements, there needs to be more than one employer. In this regard, the judge determined that "a person is only an employer during such time as it employs active members of the Scheme" (such interpretation derived from the express terms of the Scheme Funding Regulations). That being the case, CC was the only remaining employer when the Separate Funds were created.

Scheme was not a segregated scheme

In addition, the judge noted that the formal test under the Scheme Funding Regulations for segregation was not met because although contributions are allocated to a specific employer's section, it was possible for assets held in the Separate Funds to be used to subsidise benefits in other sections.

Comment

Unfortunately this case provides little additional clarity as to who may count as an "employer" for the purposes of the Scheme Funding Regulations. The judge was not conclusively persuaded by the argument that a person could count as an employer if they employed only deferred members. He found CC to be an employer in this case on different grounds, based on the express terms of the Scheme Funding Regulations. His interpretation in this case does not extend to wider pensions legislation (e.g. interpretation of the employer debt or PPF entry legislation).

Pensions Ombudsman

Hedley v Pearl Group Limited

This complaint concerned a refusal by Mr H's employer to grant him an incapacity pension. It is most notable for the Deputy Pensions Ombudsman's (DPO) comments on the way in which decisions should be recorded by employers or trustees.

Background

First complaint

Following a first complaint in 2005, the Pensions Ombudsman (PO) found maladministration in the way in which Mr H's application had been considered. The PO directed the employer to obtain further information from medical experts regarding his conditions at the time he left service and to reconsider whether Mr H met the definition of incapacity under the scheme rules. The information was obtained, but again it was decided that Mr H did not meet the criteria for incapacity under the scheme rules.

In support of his second complaint to the PO's office, Mr H referred to the fact that, following assessment, he met the threshold for state incapacity benefits and that this was a strong indicator of his state of ill-health.

Second complaint

Decision

The DPO found that this time the employer had correctly interpreted the scheme rules. The decision was not perverse as it had been based on the totality of medical evidence available in relation to Mr H's condition at the date of leaving service. While it was reasonable to take into account the fact that Mr H was receiving state incapacity benefits, this was not conclusive evidence in any application for an incapacity pension as the criteria for awarding such benefits were different to those set out in the scheme rules.

DPO says trustees should record reasons for their decisions

Crucially for pension scheme trustees, the DPO also stated that "failure to formally record within the Scheme records the precise reasons why an application has been rejected must surely amount to maladministration". While members are not expressly entitled to see documents which disclose the reasons for trustees' decision-making, the PO has consistently made it clear that trustees and employers should give reasons for their decisions.

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