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Pensions law – the week in review

16 November 2009

AT A GLANCE

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1 DEPARTMENT FOR WORK AND PENSIONS (DWP)

1.1 Research report No. 617: Understanding small employers' likely responses to the workplace pension reforms

The DWP has published[1] the findings of research carried out in early 2009 which examined the likely behaviour of small employers in connection with the forthcoming workplace pension reforms which are due to commence in October 2012. The report looks at the effect that these reforms will have on employers' administrative systems and how they will cover the cost of this and the monthly contributions.

Among the main findings, the research indicates that:

- the idea of a 'saving culture', in which people take responsibility for saving for the future and do not rely heavily on credit, is highly regarded by all employers;
- although there was broad support for the general aims of the reforms, because of the economic climate at the time the research was carried out, small employers were concerned about an increase to the cost of their businesses;
- employers found it difficult to estimate the cost of each administrative stage required to implement the reforms. This was partly due to a lack of understanding of the detail of the reforms and partly due to the way in which some small employers outsource their administration; and
- employers did not hold strong views on the phasing-in of employer and employee contributions. Those who were not already contributing to a pension thought it was a good idea which would "soften the blow" of contribution costs. However, those already contributing to pensions felt that a 3% contribution at the outset would be less confusing and reduce administration.

[1] 12 November 2009

The research, which was carried out on behalf of the DWP by BMRB Ltd, was commissioned as part of a programme of research and analysis to inform policy development, implementation and estimation of the likely impacts of the workplace pension reforms.

The DWP's press release and the research report can be accessed by clicking on the links below:

http://www.dwp.gov.uk/newsroom/press-releases/2009/november-2009/dwp065-09-121109.shtml

http://research.dwp.gov.uk/asd/asd5/rports2009-2010/rrep617.pdf

2 HM REVENUE & CUSTOMS (HMRC)

2.1 Pre-Budget Report date announced

The Chancellor has announced that he will deliver his Pre-Budget Report to Parliament on Wednesday 9 December at 12.30pm. HMRC has said that it aims to publish full details of all of the announcements which will affect HMRC customers on its website within 30 minutes of the speech ending.

We will include an update in 7 Days on 14 December 2009.

HMRC's announcement can be accessed by clicking on the link below:

http://www.hmrc.gov.uk/pbr2009/index.htm

2.2 Registered pension scheme forms updated

Following consultation with customers, HMRC has updated forms APSS301 (Amendment to a Registered Pension Scheme Return - occupational pension schemes) and APSS313 (Amendment to a Registered Pension Scheme Return - non-occupational pension schemes) and their accompanying explanatory notes, to include additional guidance to assist customers to complete the forms.

HMRC's forms and notes for registered pension schemes can be accessed by clicking on the link below:

http://www.hmrc.gov.uk/pensionschemes/returns-and-reports.htm

2.3 Improvement of online information

HMRC has announced that it is carrying out a review of the pensions pages of its website. It is aiming to make it easier for customers to find the information they need, as well as to ensure that its information is up-to-date and correct.

HMRC's announcement can be accessed by clicking on the link below:

http://www.hmrc.gov.uk/pensionschemes/pension-improvement.htm

3 THE PENSIONS REGULATOR (TPR)

3.1 2009 Recovery Plan report

On 10 November 2009, TPR published the latest edition of its annual analysis of recovery plans from defined benefit and hybrid pension schemes. The report provides an overview of the first triennial cycle of the new scheme funding regime and covers the valuation effective dates for recovery plans from 22 September 2005 to 21 September 2008. It is based on all recovery plans for underfunded schemes received by TPR as at 31 July 2009.

This year's edition focuses more on trends observed in recovery plans by TPR. Some of the key findings indicate that:

- there has not been a material increase in schemes triggering TPR's scrutiny on technical provisions (funding targets);
- there has been an increase in both recovery plan lengths and back-end loading. TPR notes that this resonates with its statement on the employer covenant in June 2009[2], in which it made reference to the flexibility of the funding framework for employers facing short-term cash constraints;

[2] http://www.thepensionsregulator.gov.uk/pdf/EmployerCovenantStatementJune2009.pdf

- there has been greater prudence in the selection of mortality assumptions, in the light of evidence of increasing longevity and TPR's guidance.[3] Schemes have moved towards the use of baseline mortality assumptions which reflect more up-to-date mortality experience in combination with adjustments which allow for future mortality improvements and an underpin;

- there has been an increase in the mean effective single discount rate adopted, reflecting increasing reliance on future investment returns (it should be noted that the data predates market activity in 2008 and early 2009);

- the weighted average recovery plan length was 8.3 years (up from 6.1 years); and

- there has been an overall reduction in the number of clearance applications in the financial year 2008/09 from the previous year.

TPR notes that the recovery plans covered by the report were agreed "in more turbulent economic times" than earlier plans, but that the full impact of the recession will only become clear next year.

http://www.thepensionsregulator.gov.uk/whatsNew/pn09-16.aspx

http://www.thepensionsregulator.gov.uk/pdf/scheme-funding-analysis-2009.pdf

4 CASES

4.1 Independent Trustee Services Limited v Hope (HC, 10 November 2009)

The High Court concluded that trustee of a scheme eligible for the Pension Protection Fund (PPF) was not permitted to "select against" the PPF by buying annuities only for certain members - relying on the PPF to pick up the cost of providing a larger proportion of benefits for the rest of the members.

[3] http://www.thepensionsregulator.gov.uk/pdf/MortalityAssumptions.pdf

Background

The Trustee of the Ilford Pension Scheme (the Scheme) applied to the High Court for directions. The Trustee asked whether it was permissible to buy out annuities for certain members of the scheme before the scheme entered the PPF.

The origins of this case lie in the position of a small group of former senior managers who took early retirement from the Scheme before their employer (the Ilford group of companies) went into administrative receivership. Given a substantial deficit in the Scheme, it is inevitable that the Scheme will be wound up in the near future, with the result that it will enter the PPF. The senior managers will have their pensions cut when the Scheme enters the PPF. This is because PPF compensation is only 90% of a capped amount[4], not the full value of any pension (excluding future increases) unless the member has reached the pension scheme's normal retirement age. Apart from the group of senior managers, it is clear that the other members will be better off if when the Scheme enters the PPF.

The Proposal

The Trustees were asked to consider purchasing annuities outside the Scheme for the group of senior managers (and top-ups for other members affected by the compensation cap), using the bulk of the Scheme's assets. Combined with the compensation that the PPF would pay if it assumed responsibility for the scheme, the proposal was that members would receive benefits equal to those that they would receive under the scheme if it were fully funded. The senior managers obtained advice that this was a proposal that the Trustees could properly implement. But as Mr Justice Henderson said in summing up, "the vice of the present proposal …is that the bulk of the Scheme's assets will be spent in the purchase of annuities, but there will not be a corresponding reduction in the Scheme's liabilities", meaning the PPF would end up footing a much larger bill for compensation.

Therefore, the question for the court was essentially whether the Trustees were permitted to take into account the existence of the PPF when making the decision to purchase annuities.

[4] For 2009/10 the cap is £31,936.32

Decision

Although the questions for the court were complex, the judge concluded that the Trustee should not be allowed to purchase the annuities for two main reasons.

- *Improper purpose*: the proposed purchase of the annuities would be an "improper use" of the power contained in the Scheme's Trust Deed and Rules to buy-out benefits, because it ignored the limitation implicit within the power that the benefits purchased would be a fair share of the assets of the Scheme.

- *Public policy*: the floodgates argument put forward by the PPF and the Pensions Regulator, that approval of the present proposal would in all probability soon lead to a proliferation of schemes designed to take advantage of or "game" the PPF. The judge concluded: "I have little doubt that, if the present proposal were approved, numerous and ever more ingenious attempts to take advantage of the PPF would soon follow, and unless amending legislation were passed to counter the threat, the PPF would find itself under increasing, and possibly fatal, pressure".

The judge also concluded that the reduction in benefits for the senior managers was not large enough to fall foul of the EC Insolvency Directive.[5]

Comment

The Trustee's application to allow the proposal to purchase benefits for certain members before the Scheme enters the PPF was rejected. This means that the members who retired early with significant pensions in payment will have their payments reduced when the Scheme enters the PPF.

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[5] Directive 80/987/EEC

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