

Welcome to the April 2012 edition of pensions news for employers. The newsletter covers a number of topical issues which companies should be aware of. For further information, please contact your usual Barnett Waddingham consultant or email corporateconsulting@barnett-waddingham.co.uk.

Budget 2012

The Chancellor of the Exchequer delivered his 2012 Budget speech in the House of Commons on 21 March and said "I don't intend to make any significant changes to pensions relief".

There had been reports in the press that the Government "quad" of David Cameron, George Osborne, Nick Clegg and Danny Alexander were looking at ways of saving more money by restricting (or removing) higher rate tax relief on pension contributions and restricting (or taxing) the currently tax-free lump sums on retirement. However these reports proved to be unfounded.

The Chancellor did, however, confirm that the Government intends to press ahead with combining the State Second Pension and Basic State Pension into a single-tier contributions-related state pension worth around £140 per week.

Full details will be published later in the Spring, but we expect one consequence of the reforms will be to end contracting-out for salary-related schemes. This will lead to a rise in costs for employers and employees who are currently contracted-out (because there will be no further National Insurance rebates), unless pension benefits are correspondingly reduced. We expect that transitional arrangements may be put in place.

Other Aspects

The headline-grabbing news related to the reduction in the top rate of income tax from 50% to 45% from the 2013/14 tax-year. This means that careful tax planning will be required for some individuals, particularly in relation to pension contributions before and after April 2013.

The Chancellor also covered some other pensions-related points in his speech:

- There will be an overall limit on income tax relief of 25% of income for those seeking to claim more than £50,000 of relief. However the Government has confirmed that this will not impact on pensions tax relief arrangements.
- The Government will consult shortly on integrating National Insurance and income tax systems.
- The Government plans to automatically link the State Pension Age to life expectancy in future.
- As previously announced, the Government will create a "Pension Infrastructure Platform" to be owned and operated by pension funds. The platform is intended to help raise capital from pension schemes to invest in UK infrastructure, from 2013.
- The Government will simplify income tax allowances to aim for a single personal allowance for taxpayers regardless of age, and to spread the tax relief fairly across working age people and pensioners. The personal allowance will rise from £8,105 to £9,205 for 2012/13 and to £10,000 for 2013/14. From April 2013, existing age-related allowances will be frozen at 2012/13 levels (i.e. £10,500 for those born between 6 April 1938 and 5 April 1948, and £10,660 for those born before 6 April 1938) until they are aligned with the personal allowance.
- The maximum term of UK Government bonds ("Gilts") is currently 50 years. The Government will consult on whether to issue even longer dated Gilts or even issue them in perpetuity. There was, however, no mention of issuing Gilts with coupons linked to Consumer Prices Index (CPI) inflation which would provide a better match for many pension scheme liabilities.



Asset-Backed Funding - Changes to the tax rules

In our January newsletter we reported that draft legislation for the Finance Bill 2012 was published on 29 November 2011 and this included a provision to change the tax relief granted to employers in respect of asset-backed pension funding arrangements.

On 22 February 2012, HMRC issued an announcement and published further legislation to take effect from the same date to "remove any unintended and excessive tax relief being given to an employer in respect of any asset-backed contributions (ABCs) made to their pension schemes."

The legislation will apply as follows:

1. New arrangements - where the contribution is paid on or after 22 February 2012, then the February legislation will apply.
2. November-February arrangements - where an ABC arrangement had been set up with the employer contribution paid on or after 29 November 2011 but before 22 February 2012, the November legislation applies to determine whether upfront relief is available.
3. Pre-November 2011 arrangements - where an ABC arrangement had been set up with the employer contribution paid before 29 November 2011, the November legislation applies if the arrangement continues at 29 November 2011. Where the November transitional rules do not apply, the transitional provisions in the February legislation will apply to payments that arise on or after 22 February 2012.

The main difference between the two sets of provisions is that the February legislation introduces new qualifying conditions that must be met in order to qualify for upfront relief as well as meeting the tax rules for structured finance arrangements (like ABCs).

The conditions are:

- The pension contribution promised upfront under the arrangement must be due to be paid to the pension scheme and not intended to be held in a subsidiary structure.

- The pension scheme must be the lender giving an 'advance' (the pension scheme investment) to the employer directly or indirectly through a Special Purpose Vehicle (SPV). For example, the pension scheme would use the contribution to purchase a stake in the SPV.
- The advance must be wholly paid out of the promised contribution.
- The contribution must equal both the advance and the financial liability recorded in respect of the advance.
- From the outset, regular payments due to the pension scheme under the arrangement must reduce the financial liability to nil by the earlier of the completion day or 25 years.
- The payments must be of equal amounts due at intervals of no more than one year and must be received by the pension scheme to form part of the scheme's regular assets.
- The total amount of the payments due to the pension scheme must not be less than the contribution.

If the conditions are not met, tax relief will only be granted to any payments actually made to the pension scheme under the arrangement.

Employers and schemes that have these arrangements in place will need to consider which tax rules will apply to them. However we still believe that these arrangements are, and will remain, an important option for companies in funding their pension schemes, particularly if they have suitable assets available.



Significant deals completed

Communications firm Communis has set up an asset-backed contribution arrangement with its pension scheme, whereby the pension scheme will have rights to an annual income stream from one of its properties for the next 15 years.

The FTSE listed firm Pendragon has also used an asset-backed deal whereby a number of the Company's properties have been transferred to a central asset reserve with their pension schemes then being given an interest in this asset reserve. This has resulted in its accounting deficit of £69.7m at the start of last year being reduced to £8m as at 31 December 2011.

Engineering firm Costain has agreed the transfer of £20m worth of Private Finance Initiative (PFI) holdings (used for funding public infrastructure projects with private capital) to its pension fund as well as carrying out enhanced transfer value and pension increase exchange exercises in a bid to reduce their liabilities and overall risk associated with the pension fund.

The high-tech manufacturer Denso has entered into a buy-out with Pension Insurance Corporation for two of its pension schemes (£200m liabilities) that are open to future benefit accrual. This is the first significant deal where a scheme remains open to future benefit accrual.

Enhanced Transfer Value Exercises - FSA proposals to change transfer value analysis

The FSA published a consultation paper at the end of February, outlining proposals to change the way IFAs carry out pension transfer value analysis.

A transfer value analysis is the advisory process of comparing the benefits being transferred out of a defined benefit scheme with those that could be offered by a personal pension or defined contribution scheme.

The FSA is proposing changes to the assumptions which advisers are required to use when comparing benefits under the different arrangements to ensure that individuals considering a transfer are given a fair assessment of what they might receive in retirement under each arrangement.

As part of a risk and liability management exercise employers may offer some incentive to members who transfer from a pension scheme, for example an enhanced transfer value or a cash payment. The proposed changes are likely to be costly for employers as transfer values will need to increase before a transfer is recommended by a financial adviser. The FSA has estimated that the proposed changes will prevent an undervaluation of benefits of up to £20 billion.

Stronger Funding Targets? - Solvency II and UK pension schemes

As reported in our January newsletter, there has been much speculation on whether the European Solvency II regime will ultimately be applied to UK occupational pension schemes.

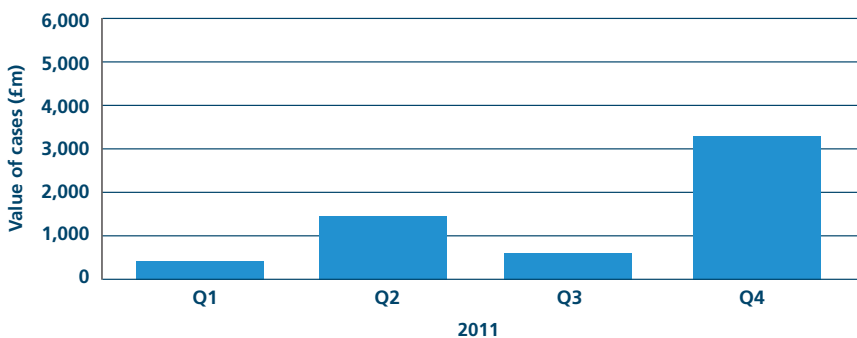
Commissioner Michel Barnier has moved to calm fears that UK pension funds will be subject to the same rules as insurance companies when changes are made to the Institutions for Occupational Retirement Provision directive.

Barnier said: "To be clear: I have never said or suggested that pension funds should be subject to exactly the same rules as Solvency II. If that had been the Commission's intention, we would have proposed this back in 2007 when we presented the Solvency II directive," he said.

He continued: "I have seen various estimates of the impact of Solvency II on pension funds. These make no sense at all because we won't copy and paste Solvency II into pension funds."

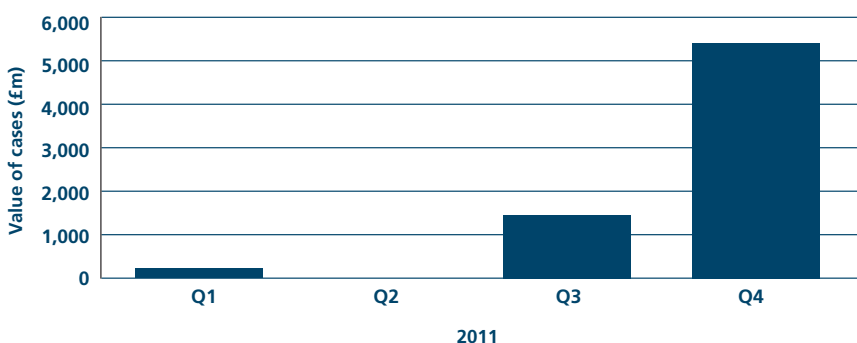
We are running a series of free seminars across Barnett Waddingham's offices during April and May which will consider the potential impact of Solvency II in more detail. See the forthcoming events section of this newsletter.

Buy-outs, buy-ins and longevity swaps



Bulk annuity market business

60% of the value of buy-ins and buy-outs completed during 2011 occurred during Quarter 4. This was helped by large transactions by Legal & General and Rothesay Life plus a strong quarter from Aviva.



Longevity swaps market business

Quarter 4 2011 saw three longevity swap deals completed with pension schemes providing longevity protection for £5.3bn worth of liabilities. In Quarter 1 2012, Deutsche Bank announced a longevity swap with the insurer Aegon in the Netherlands to protect policyholder liabilities worth €12 billion.

Source: Barnett Waddingham LLP

Barnett Waddingham helps client complete buy-in

MetLife®

The Barnett Waddingham insured solutions team has recently helped complete a buy-in for the pensioner members of a £35m liability scheme.

This was completed in an unprecedented two weeks from obtaining the agreement to proceed from the client using our streamlined arrangement with MetLife Assurance. The arrangement with MetLife allows us to produce very accurate indicative buy-in and buy-out quotations based on pricing information provided by MetLife. This allows us to prepare a quick feasibility assessment of whether a transaction is likely to be affordable and then move to complete the transaction within very short timescales. The speed with which the transaction was completed using this process meant that it was possible to take advantage of favourable financial conditions. The buy-in has helped in resolving funding issues as well as increasing security of benefits for members while taking some of the strain off the scheme's sponsor.



Barnett Waddingham launches 'Finance Directors Guide to Pensions'

We have launched an 'online guide to pensions' which aims to keep Finance Directors well informed on a range of pension issues that may affect their business.

The guide will act as a useful general reference point on pensions issues but will also allow Finance Directors to stay up-to-date with the latest industry news with specific sections covering hot topics and a blog.

To view the guide visit the following link:
www.fdpensions.co.uk

Forthcoming Barnett Waddingham Events

April/May 2012 Solvency II Seminar

This seminar will examine the likelihood and timescales of Solvency II applying to pension schemes, and the likely impact for schemes in the UK. The seminars will take place in various locations around the country and are free to attend.

31 May 2012 2012 – the continuing DB challenges from a corporate perspective

This seminar will explore the funding, investment and covenant issues that employers need to consider in 2012 and how can they be tackled from the corporate perspective.

This half-day seminar with lunch, will take place at the One Great George Street in London and you will hear from our in-house as well as external experts on various topics.

For more information on our forthcoming events, please visit the events page on our website www.bwllp.co.uk/C or email seminars@barnett-waddingham.co.uk

For further information on any of the news raised here or for any other corporate matter please contact corporateconsulting@barnett-waddingham.co.uk

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