

### State Pension Reform: Flat-rate State Pension and the end of Contracting-out

The Department for Work and Pensions (DWP) has published a **White Paper** setting out details of its plans for reform of the State Pension system. In particular, from April 2017 "at the earliest", the current system (Basic State Pension plus State Second Pension (S2P)) will be replaced with a single flat-rate pension of around £144 per week (in today's prices) for everyone with a 35-year National Insurance Contributions (NICs) record.

The Government expects to reduce the number of people reliant on means-tested benefits by around 80% as a result.

From 2017, the ability to contract-out of S2P via a salary related scheme will cease. Rebates of NICs enjoyed by employers and employees by virtue of being contracted-out will be abolished with employees paying an additional 1.4% of relevant earnings in NICs after the change.

Employers will pay an additional 3.4% of relevant earnings in NICs when contracting-out ends. The Government expects that many employers will consider amending benefits to mitigate this rise in costs. The Government will legislate to make it easier for employers in this situation to amend scheme benefits without requiring trustee approval, although the legal requirement to consult members on changes will remain. The Government expects that the majority of affected members will receive more in State Pension than they will pay in additional NICs.

The DWP and Her Majesty's Revenue and Customs (HMRC) are expected to produce a series of factsheets for employers to use when communicating contracting-out changes to their employees. The Government has also outlined plans for a 5-yearly review of State Pension Age (SPA).

### Quick Facts – The Single-tier Pension

- From 2017 "at the earliest".
- Single flat-rate pension of up to £144 per week (in today's prices).
- Minimum NIC record to qualify (expected to be 10 years).
- 35-year NIC record to qualify for full pension.
- Transitional arrangements to ensure past State Pension rights not worsened.
- Individuals reaching SPA before 2017 not affected.
- Late retirement ("deferral") still possible, though not in exchange for lump sum.
- Contracting-out will end. NIC rebates will cease.
- SPA reviewed every 5 years by independent body.

### Chancellor's Autumn Statement

The Chancellor of the Exchequer delivered his Autumn Statement in December against a backdrop of low economic growth and worsening forecasts. It was no surprise therefore that the "age of austerity" is expected to continue for several years.

#### Smoothing in Scheme Funding

The DWP has now launched a "**call for evidence**" on allowing smoothing of assets and liabilities in scheme funding valuations.

The DWP is seeking views on how and whether this could be incorporated into scheme funding legislation. The Government intends to set out detailed proposals of changes to legislation "as soon as practical in 2013". In the meantime, The Pensions Regulator (TPR) has **said** that "until it is clear as to whether the regime will be altered in any way, there is no change in the responsibilities of trustees and sponsors".

Following a spate of Quantitative Easing (QE), recent low gilt yields have driven up estimated liabilities for many schemes. TPR had previously rejected calls to allow trustees to adjust discount rates to mitigate the impact of QE.

The DWP is also considering whether TPR should have a new statutory objective to consider the long-term affordability of deficit recovery plans. The Government is particularly determined to ensure that pensions legislation "does not act as a brake on investment and growth". TPR chairman Michael O'Higgins, speaking at the Professional Pensions Show in 2012, has previously warned trustees not to be "recklessly prudent" in the valuation assumptions they make and in the investment strategy they use.

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# Our Services

Barnett Waddingham provides professional services spanning pensions, life and general insurance.

Our services include:

- Scheme actuary and associated services to the trustees and employers associated with defined benefit pension schemes.
- Advice in relation to defined contribution schemes.
- Pension accounting for UK and international companies.
- Administration and management services including pensioner payroll, preparation of annual accounts and secretarial services.
- Investment strategy reviews and advice on scheme evolution strategy.
- Management of closed schemes, wind-ups and reconstructions and schemes in PPF assessment.
- Employer risk management through buy out options, transfer exercises and PPF levy management.
- Advice on group personal pensions, stakeholder schemes and personal accounts.
- Group risk advice covering group life assurance, private medical benefits and income protection benefits.
- Analysis and modelling of mortality and longevity risk for insurance companies, reinsurance companies, investment banks and pension schemes.

We also have a dedicated team that provides a wide range of services to the life assurance and general insurance industries in the UK and overseas including statutory actuarial roles.

Through our associated company, Barnett Waddingham Investments LLP, we provide assistance to individuals in respect of all aspects of their financial wealth management. These services include investment advice together with executive pension counselling, and retirement option advice including an annuity bureau.

Barnett Waddingham is also a leader in the provision of self invested personal pensions (SIPPs), small self administered pension schemes (SSASs), specialist executive pension plans (EPPs) and other retirement arrangements.

*Chancellor's Autumn Statement continued...*

## Taxation: Annual and Lifetime Allowances

The Annual Allowance (AA) applies a limit to tax efficient pension contributions to a defined contribution (DC) arrangement and increases in the value of benefits built up in a defined benefit (DB) scheme each year (calculated using a factor of 16:1). When it was first introduced the AA was £255,000 but it was reduced to £50,000 from 6 April 2011. From April 2014, the AA will reduce further to £40,000.

Contributions or benefit accrual above the AA results in a tax charge. In the main the reduction to the AA is likely to affect higher earners, who should seek retirement planning advice on how to deal with this. However, longer-serving members of DB schemes and those awarded large pay increases may also be affected. HMRC has confirmed that there will be no changes to previous "carry forward" allowances. This means that any unused allowances available for carry forward from the tax years 2011/12 to 2013/14 and will still be based on the £50,000 limit.

The Lifetime Allowance (LTA) applies to the value of benefits built up over an individual's working life. In a DC scheme the LTA is compared with the accumulated pension fund value on retirement. In a DB scheme, pension benefits are valued for this purpose using a factor of 20:1. The LTA was reduced from £1.8 million to £1.5 million with effect from 6 April 2012. The Chancellor has decided to make a further cut to £1.25 million with effect from the 2014/15 tax year.

A fixed protection regime to help with the transition will be available to those who have already accrued benefits above the revised LTA. This will work in a similar way to the existing fixed protection regime, allowing members to retain an LTA of £1.5 million if they stop all further pension saving.

The Government has also, subject to consultation with interested parties, proposed an additional 'personalised' protection regime. This would allow individuals with pension rights in excess of £1.25 million at 5 April 2014 to protect the pension benefits they have already earned when the LTA is reduced and, unlike fixed protection, they will be able to carry on saving. However, further pension saving will be subject to a tax charge when benefits are taken.

Further details on the Autumn Statement can be found in our [information sheet](#).

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## DWP: Reinvigorating Workplace Pensions

The DWP has published *Reinvigorating Workplace Pensions*, a strategy document intended to generate discussion about increasing and improving pensions saving and restoring confidence in the UK's pension system.

One of the main focuses of the paper is the establishment of a framework for so-called Defined Ambition (DA) pension arrangements. Although not a formal consultation, the DWP intends to meet with industry and consumer bodies to explore ways forward. The paper also notes that the DWP is monitoring DC scheme changes closely and that a review of disclosure regulations will begin later in 2013.

### Defined Ambition

Under DA, risks do not fall solely on the employer or the member as is the case with DB and DC schemes. The DWP notes that the current legislative framework already allows for risk-sharing, for example in the form of Career Average Revalued Earnings (CARE) schemes, cash balance schemes and schemes that adjust retirement ages to reflect improving life expectancies.

The document briefly explores new DA models which might be facilitated in future, starting from a DB standpoint ("DB-lite" schemes) or a DC standpoint ("DC-plus" schemes).

Possible DB-lite approaches include:

- Schemes that offer a core level of provision with discretionary extras such as optional indexation or spouse's benefits.
- Schemes providing a DB pension but, on leaving, retirement or death, the benefits are converted to a DC fund of equivalent value.
- Schemes that pay a core pension plus a discretionary amount that fluctuates according to the funding position of the scheme.

The DWP also explores DC-plus options such as:

- A “money back” guarantee where the individual will get back at least the contributions they have paid in
- A guarantee to cover retirement income in later years (so the scheme would pay the pension up to a set age with later instalments paid from an industry-wide fund).
- Guaranteed investment returns or a guarantee of a minimum income in retirement.

We would be interested to hear your ideas for implementing Defined Ambition schemes. We are running a £15,000 prize competition in conjunction with Professional Pensions, – see [our website](#) for further details.

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## Auto-Enrolment Update

Auto-enrolment began on 1 October 2012 with the largest employers now required to enrol staff into a workplace pension. Steve Webb, Minister for Pensions, is “proud to be introducing this truly historic change, which will radically alter the way we save for our old age, and see millions more people putting something aside for the future”.

### The Pensions Regulator’s Approach

TPR has updated its five step action **checklist** designed to help trustees prepare for auto-enrolment if applicable. Trustees of DC schemes are encouraged to use **TPR’s tool** for assessing whether their scheme is suitable for auto-enrolment. **Guidance** on whether a DB scheme qualifies is also available on TPR’s website.

TPR has also outlined the ways in which it will encourage auto-enrolment into high-quality pension schemes. TPR has **invited views** on a voluntary “comply or explain” procedure, under which DC schemes would be required to disclose to employers, retirement savers or the Regulator how they incorporate TPR’s principles and features for well-governed DC schemes, or explain why they do not.

### Loophole closed

The DWP has **announced** that it will retrospectively amend legislation to ensure that only employers offering DB pensions to all employees will be able to take advantage of transitional arrangements allowing them to defer automatic enrolment for all eligible jobholders until 2017.

Current rules allow companies with DB or hybrid schemes to defer automatically enrolling existing staff. The Government wishes to make clear its intention that people with access solely to a DC pension scheme (even if part of a hybrid arrangement) will not have their auto-enrolment deferred.

### Enhanced/Fixed Protection

HMRC has warned that valuable Fixed or Enhanced protections from LTA charges could be lost if protected individuals are auto-enrolled into a company pension scheme and do not opt-out within 30 days. To retain Enhanced Protection or Fixed Protection, individuals should make sure that they opt out of auto-enrolment as soon as possible after their employer starts the auto-enrolment process.

As employers must automatically re-enrol opted out employees every three years, it will be necessary for individuals who wish to retain protection to opt out within 30 days every three years.

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## Latest News from TPR and the PPF

### Winding-up – GMP Data

TPR has updated its **winding-up guidance** in which it encourages trustees to adopt a £2 per week tolerance when reconciling Guaranteed Minimum Pension (GMP) data with HMRC, rather than matching “to the penny”. It is hoped that this will not only speed up the process of winding-up but also boost members’ benefits by avoiding costly reconciliation exercises.

### 2013/14 PPF Levy

The PPF has published the **2013/14 Levy Determination** and confirmed that the total levy estimate is £630 million as originally proposed. To raise this amount the PPF confirmed that it will reduce the levy scaling factor from 0.89 to 0.73.

In addition, there will be a relaxation in the requirements for a guarantee from a bank or a custodian, so that in future a credit rating of A- or above will be sufficient. The PPF has also updated its guidance for putting in place contingent assets.

### DC Schemes: Reporting Late Contributions

TPR has published a **consultation** on new codes of practice and accompanying guidance on reporting late payments of contributions to occupational DC and personal pension schemes.

## 2013 Investment Conference

**Our annual Investment Outlook 2013 Conferences took place on Wednesday 16 January in Birmingham and on Wednesday 23 January in London. Slides from the conferences can be viewed on [our website](#).**

Marcus Whitehead chaired the conferences on the theme of “It’s the ~~economy~~ politics stupid”. Over 230 trustees, finance directors and pensions professionals heard presentations from John Redwood MP, Joanne Segars of the NAPF and Alan Rubenstein from the PPF. The conferences also included an equity outlook from F&C, an overview of secured debt and high yield bonds from Babson Capital and a bond outlook from BlueBay. Matt Tickle rounded up the day considering whether financial repression will continue into 2013.

*“Excellent conference, very informative and useful. Highly recommended.”*

– N. Daud Rusa Consulting Ltd

# News in Brief

## Retail Prices Index

The National Statistician has **announced** that, following consultation, a widely-expected change to the construction of the Retail Prices Index (RPI) will not be implemented. Instead, a new index - RPIJ - will be introduced, which is more closely aligned with the Consumer Prices Index (CPI). RPI will continue to be used as the reference for determining RPI-linked pension increases and returns from index-linked gilts and bonds.

Trustees of schemes that have retained the RPI inflation measure for future pension increases and/or revaluation of deferred pensions will be interested to understand in due course whether they have an option to switch to the RPIJ measure, which is expected to be lower (and therefore cheaper).

The next in our series of free seminars will cover the different measures of inflation and the implications for pension schemes, as well as a round-up of other recent pension issues. This seminar will take place across our offices on the following dates: 26 February - Birmingham, 27 February - Amersham, 28 February - Leeds, 5 March - London, 6 March - Cheltenham, 7 March - Liverpool.

Please email [seminars@barnett-waddingham.co.uk](mailto:seminars@barnett-waddingham.co.uk) if you would like to attend.

## Impact of the "Test-Achats" judgment

European insurance companies have been required, since 21 December 2012, to adopt unisex or gender-neutral terms for all insurance products purchased by consumers.

This has led to improved annuity rates for females, but at the cost of a further blow to annuity costs for men. The legislation only directly impacted policies purchased by individuals, so bulk purchase annuities are unaffected and some insurance companies are continuing to offer gender-specific rates where an annuity is purchased by a scheme for an individual, rather than by the individual themselves.

## 2011 Census: Older Age Mortality

The latest official population estimates for England and Wales for mid-2011, derived from the 2011 Census, differ materially at high ages from previous estimates. These are an important component of our understanding of mortality at older ages, where data from pension schemes and insurance companies are sparse. Analysis by our specialist longevity team has highlighted potential weaknesses in the census-based high-age estimates of mortality rates, which could significantly reduce the estimated value of pension liabilities for a scheme with a particularly high proportion of lives aged over 80.

## Bridging pensions – State Pension Age

Many schemes with normal retirement age (NRA) before State Pension Age (SPA) provide members with a bridging pension between NRA and SPA when the State pension commences. The DWP is consulting on draft regulations that will allow trustees of schemes providing bridging pensions to modify rules via a resolution (with employer consent) to reflect changes to SPA.

## Equality Act – Survivor Benefits

A man has won a legal battle to secure **equal pension benefits for his civil partner** at an employment tribunal on the grounds that such discrimination contravenes both European Union law and the European Convention on Human Rights. We understand the decision has been appealed.

Innospec had used the exemption contained in the Equality Act 2010 that permits employers and pension funds to exclude civil partners from spouses' benefits relating to service prior to 5 December 2005 and offered the member's civil partner £500 a year in the event of his death. The tribunal agreed that he should receive the equivalent of a full spouse's pension, which amounted to £40,000 a year.

Whilst the tribunal decision is not binding on any other schemes (i.e. it relates only to the employer and individuals involved), trustees and companies may wish to consider the issue now, as it may lead to further tribunals, court rulings or a change in the Government's stance.

## Trustee Training

Many clients and contacts have used our one-day Trustee Training course to bring new trustees up to speed or as a refresher course. Details of courses being run in 2013 can be found on our website [here](#).

We have also been considering running a longer two-day course covering the syllabus of the Pensions Management Institute's (PMI) Award in Pension Trusteeship (APT). Award attendees could then choose to sit the PMI's exam at the end of the course.

If you would be interested in a course designed for this purpose, we would like to hear from you. Please email [Trusteeseminars@barnett-waddingham.co.uk](mailto:Trusteeseminars@barnett-waddingham.co.uk) to register your interest.

This bulletin is a summary of some recent developments and not a comprehensive description. Although we try to ensure its accuracy, Barnett Waddingham LLP accepts no liability for any errors or omissions it may contain. Readers should take professional advice in relation to their own circumstances and/or refer to the original source material as appropriate. Barnett Waddingham LLP holds your contact details for its own communication purposes only. We do not disclose these details to third parties. If you no longer wish to receive newsletters from us, please let us know.

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