

Pensions - June 2012

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LATEST NEWS FROM THE COURTS

The Queen's Speech

In a *speech* at the State Opening of Parliament the Queen has set out the Government's *legislative plans* for the next 12 months, which include a Pensions Bill and a Public Service Pensions Bill.

Reform of the State pension system will be set out in a Pensions Bill, which will:

- increase State Pension Age (SPA) from 66 to 67 between 2026 and 2028 (see *Pensions News – July 2011*). The Government will also legislate for future changes to SPA to be linked with increases in life expectancy in the UK.
- replace the current state pension system with a flat-rate state pension of around £140 a week. It is expected that the new structure will only be applied to those not already in receipt of their state pension.

Barnett Waddingham's Malcolm McLean *welcomed the concept* of a new flat-rate pension but warned: "There are also a number of points of detail which will bear further scrutiny when they emerge, including how accrued rights to the state second pension above the baseline of £140 will be treated, and what impact the ending of contracting out rebates from defined benefit schemes will have on national insurance contribution payments for employees and employers".

A Public Service Pensions Bill will implement the changes to public sector pensions in line with agreements reached with trade unions for the three largest public sector schemes. The changes include amending benefits to be based on career average salary, rather than final salary, and aligning normal retirement ages to SPA. The Bill will also introduce cost controls so that "future unforeseen changes in the cost of pensions are shared by members and employers".

ECJ: Withholding Tax

The European Court of Justice (ECJ) has ruled that French tax laws which apply a 15%-25% withholding tax on dividend payments to investment funds not resident in France were in breach of European Union law.

The decision means that UK pension funds could reportedly reclaim around half a billion pounds from French tax authorities on claims made between 2004 and 2009, if further legal action in France is successful.

RPI/CPI: QinetiQ

The High Court has ruled that where trustees have discretion in their scheme's rules to select the index used to increase pension benefits, a switch from using the Retail Prices Index (RPI) to the Consumer Prices Index (CPI) would not breach section 67 of the Pensions Act 1995 which protects members' accrued rights.

In the case of *Danks and others v QinetiQ Holdings Limited and another*, the High Court ruled that the trustees of the QinetiQ Pension Scheme could switch to CPI for increasing all preserved and pension benefits in future.

TPR: Governance Survey

The Pensions Regulator (TPR) has published a report on its sixth occupational pension scheme **governance survey**. Some of the key findings were:

- Trustees of larger schemes are more likely to meet regularly, provide training support and be aware of TPR's guidance.
- Overall, 96% of schemes assess their governance as very or fairly effective.
- 72% of trustee boards meet at least every six months. However, 22% of trustee boards for small defined contribution (DC) schemes meet only once a year, or less.
- Of the 76% of schemes who have used TPR's Trustee Toolkit, 91% viewed it positively.
- Only 54% of schemes sent new trustees on **introductory training courses** in 2012.
- 7% of trustees of large defined benefit (DB) schemes and 74% of trustees of small DC schemes had not undertaken formal training in the last 12 months.
- 65% of trustee boards had not taken particular steps to improve communication with members.
- Some trustees of DC schemes rate their understanding of scheme charges as "poor" – in particular 9% did not understand total charges deducted from member funds.

PPF: Strategic Plan 2012

The Pension Protection Fund (PPF) has published its **2012 strategic plan**.

The plan describes how the PPF will operate over the next three years, by which time it expects to have almost 500,000 PPF and Financial Assistance Scheme (FAS) members and an investment portfolio of £17 billion.

The PPF intends to concentrate on customer service (including members and levy payers). It plans to make sure that its systems can be scaled, and review its hedging process and manager monitoring systems with a view to remaining on track to achieve its target of self-sufficiency by 2030.

PPF: 7800 Index

The **latest update** of the Pension Protection Fund's (PPF) 7800 Index of schemes' funding on a s179 basis has been published.

The aggregate funding position of the 6,432 schemes in the index is estimated to have worsened over the month to a deficit of £216.8 billion at the end of April 2012 (there was an aggregate deficit of £206.2 billion at the end of March 2012). Funding has worsened over the year (there was an aggregate deficit of £8.2 billion at the end of April 2011).

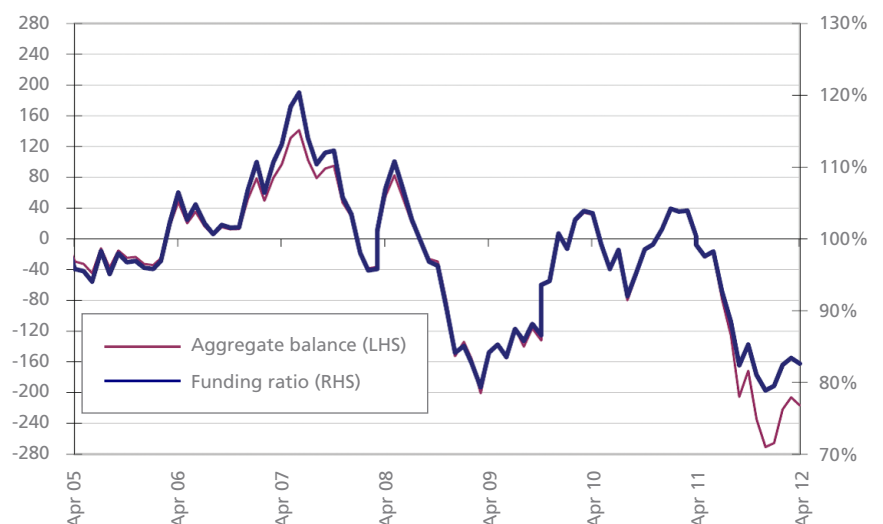
TPR: Record-keeping Survey

TPR has published a report on its third **survey of scheme record keeping**.

The survey of 646 schemes demonstrates that there has been progress in this area, with an increase in the proportion of schemes having processes in place or planned to measure common data (such as names, addresses and dates of birth), and an improvement in the proportion of schemes with a common data score over 90%. More action is being taken by administrators, including attending trustee meetings frequently.

TPR has set a deadline of December 2012 for schemes to **meet its target** of 100% of common data in place for members joining a scheme from June 2010 onwards, and 95% for members joining before then.

47% of schemes have a common data score above 90%, and 33% are above 95%. TPR reminds trustees that they are solely accountable for a scheme's record keeping.



Auto-enrolment: CARE Schemes

The Department for Work and Pensions (DWP) is seeking comments on **draft regulations** intended to permit a wider range of career average revalued earnings (CARE) schemes to qualify for the purposes of automatic enrolment.

CARE schemes can be used as qualifying schemes for auto-enrolment if members' accrued rights are revalued at or above a prescribed minimum rate (the lower of CPI inflation or 2.5 per cent each year) whilst a jobholder is in pensionable service.

The current regulations do not allow a CARE scheme to be a qualifying scheme if it has a mix of guaranteed revaluation below the minimum level and a discretionary power to revalue at a higher rate. The proposed changes will allow a CARE scheme with a mix of guaranteed and discretionary revaluation to be a qualifying scheme as long as the revaluation is funded for and included in the scheme's Statement of Funding Principles.

TPR: BMAL Pension Scheme

TPR has published a report explaining its decision to approve an "extremely uncommon" Regulated Apportionment Arrangement (RAA) in relation to the British Midland Airways Limited Pension and Life Assurance Scheme.

The Scheme had an estimated deficit of around £450 million on a "buy-out" basis. TPR was asked for clearance in relation to a transfer of the Scheme's liabilities to a shell company within the Lufthansa group (the 100% shareholder of the BMI Group) as the sole sponsoring employer. Lufthansa had committed to provide voluntary support to the pension scheme over a 25-year recovery plan, despite having no legal obligation to fund the scheme.

However, this support was not expected to prevent a deterioration in the Scheme's funding position without future investment outperformance. The Regulator's view, therefore, was that the proposal was not in the interests of members or PPF levy payers.

Following further discussions, TPR agreed to a controlled entry to the PPF via a RAA. Under the RAA, the Scheme (and hence the PPF) received £16 million – much more than would have been received if the Scheme's existing statutory employer had become insolvent. Lufthansa will also provide a further £84 million on a voluntary basis to top up members' benefits outside the PPF.

TUPE: Pension Benefits

The **High Court has ruled** that when pension scheme members transfer employees under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), the new employer is liable for any pension benefits falling due after early retirement but before normal retirement date.

In the case of *The Proctor & Gamble Company v Svenska Cellulosa Aktiebolaget* and another, the judge ruled that the early retirement portion of the benefit did not fall within the "old age" exemption in the TUPE regulations, and would fall to be met by the purchaser. The previous employer would then retain responsibility for payments after normal retirement age, even where this was as a result of a benefit granted on early retirement.

FRC/FSA: Pension Illustration Assumptions

The Financial Reporting Council (FRC) and the Financial Services Authority (FSA) have published a joint **consultation** on actuarial assumptions used in projections of the returns from financial products.

The consultation aims to bring the assumptions used for personal pension illustrations in line with those used for transfer value analysis and Statutory Money Purchase Illustrations (SMPIs).

Providers of retail financial products are required to illustrate potential future investment returns on three rates of return, currently 5%, 7% and 9% for tax-advantaged products such as personal pensions, and adjust these rates downwards where a product is not likely to be able to achieve such returns. The FSA proposes a reduction in these projection rates to 2%, 5% and 8% respectively.

The use of updated gender-equal mortality rates is also proposed, in line with the guidance for SMPIs. Finally, additional assumptions will be introduced for transfer value analyses where a defined benefit pension is indexed in line with CPI rather than RPI inflation.

CMI: Working Papers 61 & 62

The Continuous Mortality Investigation (CMI) of the Actuarial Profession has published its **Working Paper 61**. The paper presents the results of an investigation into the mortality experience by industry classification of pensioners of self-administered pension schemes.

The results indicate that the financial sector appears to experience lighter mortality (ie individuals live longer on average) than the majority of other industry categories. However, it is possible that the differences can be explained by differences in the average pension amount in each industry (ie that wealth/income is a more reliable indicator of life expectancy).

The CMI has also published its **Working Paper 62**, which analyses mortality experience for self-administered pension schemes over the period 2003-2010 based on data collected up to 30 June 2011. The annual update of experience shows a gradual improvement in mortality rates.

You might also find our recent publications on the following topics useful:

- ***Incentive Exercises – Industry Code of Good Practice***
- ***Buy-outs, Buy-ins and Longevity Swaps***
- ***Key points of Annual Allowance and Lifetime Allowance charges***

For further information on any of the topics in this bulletin, please speak to your usual Barnett Waddingham consultant, or visit our website www.barnett-waddingham.co.uk

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