TRAVERS SMITH

What's happening in
Pensions

Issue 1 **April 2008**

Internal dispute resolution procedure changes

The Pensions Act 2004 (Commencement No.11) Order 2008 has confirmed that the new one or two stage IDR procedure regime under Pensions Act 1995, as amended by the Pensions Acts 2004 and 2007, takes effect from 6 April 2008. New regulations have also been finalised and a Code of Practice from the Pensions Regulator on the new "reasonable periods" under the amended legislation has been laid before Parliament.

We have produced a briefing note on this subject. Please contact us if you have not received it.

www.opsi.gov.uk/si/si2008/pdf/uksi_20080627_en.pdf
www.opsi.gov.uk/si/si2008/pdf/uksi_20080649_en.pdf
www.thepensionsregulator.gov.uk/pdf/Cop11DisputeResolution.pdf

New Employer Debt Regulations

The Government has laid regulations amending the 2005 Employer Debt Regulations with effect from 6 April 2008. They affect employers ceasing to employ active members in defined benefit schemes on or after that date.

We have produced a briefing note on this subject. Please contact us if you have not received it.

The Pensions Regulator has subsequently published an update to its guidance on Multi-employer Withdrawal Arrangements, reflecting the new law. The Regulator will be consulting on more detailed replacement guidance in the coming months.

www.dwp.gov.uk/mediacentre/pressreleases/2008/mar/pens060-140308.asp
www.thepensionsregulator.gov.uk/whatsNew/multiEmployer.aspx

New clearance guidance from the Pensions Regulator

Following a consultation exercise launched in September 2007, the Pensions Regulator has finalised and published new guidance on clearance applications. This replaces the April 2005 guidance. Clearance is a protection that parties can apply for, often in connection with a proposed transaction or restructuring, to be sure that the Regulator will not issue a contribution notice or financial support direction against them in connection with that matter.

The new guidance adopts a "principles-based approach". Type A events – which are suitable for clearance applications - are no longer specifically defined (but examples are given), and Types B and C events are no longer referred to. The Regulator expects clearance applications (which will still be voluntary) only in respect of Type A events. Type A events are now all events that are materially detrimental to the ability of the scheme to meet its liabilities.

Events are split into employer-related events (including changes in creditor priority, returns of capital, changes in group structure, sale and leaseback transactions, the granting or repayment of inter-company loans, and asset sales) and scheme-related events (including compromises of section 75 debts, apportionment of deficits and arrangements that prevent section 75 debts from being triggered). Employer-related events are Type A events only if there is a "relevant deficit" in the scheme; scheme-related events are Type A regardless of the scheme's funding position.

Whether or not there is a "relevant deficit" will be measured on the highest of the following bases: FRS17/IAS19, s179 (PPF), the scheme's technical provisions, and the ongoing basis (where no technical provisions yet). However, an unspecified, stricter basis can be used "reflecting the impact of an event identified by trustees and employers where the employer-related event is significantly detrimental to the scheme's ability to meet its liabilities (including where there is a significant weakening of the employer covenant)", and a buyout basis should be used if there are questions about the employer continuing as a going concern, if the scheme is winding-up, or if there is scheme abandonment.

The new clearance guidance covers much larger territory than just applications for clearance statements: it also includes many matters of importance to trustees, notwithstanding the Regulator's stated view that it is not normally appropriate for a trustee to apply for clearance. For those familiar with the old guidance, the following new points will be of interest.

- The Regulator expects trustees to have had the opportunity to consider, take advice and negotiate before a clearance application is made.

- The Regulator expects that responsible employers will wish to pay for trustees to obtain independent financial advice in relation to an upcoming Type A event.
- Trustees are expected to take account of the covenant of the wider employer group, to the extent that the group could be responsible for scheme funding.
- Trustees should negotiate mitigation where they have identified a materially detrimental event.
- Trustees should be cautious about agreeing to fetter their powers or discretions, or agreeing restrictions on their duties.
- The consideration of clearance applications will be delayed if the trustees have not considered (and presumably addressed) conflicts of interests.
- In the Regulator's view, the Scheme Administration Regulations can be used to require the employer, auditor or actuary to provide information about the employer covenant.
- The Regulator expects all applicants for clearance in relation to the same event to use the same form and to be named individually. There is a redesigned clearance application form.
- There is a now a long, specific list of documents that the Regulator expects to be submitted with clearance applications.
- The legislation permits applications for wide clearance statements, stating that in the Regulator's view the applicant would not be a party to a specified act or deliberate failure to act, but the Regulator discourages applications that would require extensive investigation.
- The new guidance reflects the new options for dealing with employer debts, following the amendments to the Employer Debt Regulations (see above): clearance will still be a factor to consider in these situations.

Some connected matters that were covered by the consultation draft, such as conflicts of interests and the trustees' role in protecting members' interests, are to be dealt with in separate guidance.

www.thepensionsregulator.gov.uk/whatsNew/PN08-06.aspx
www.thepensionsregulator.gov.uk/guidance/clearance/index.aspx

Pensions Regulator consultation on draft conflicts of interest guidance

The Pensions Regulator has published draft guidance on trustees' and advisers' conflicts of interest. Consultation on the draft guidance closes on 30 May 2008. The draft guidance covers such matters as:

- documenting a policy for monitoring and addressing conflicts of interest;
- conflicts authorised by the trust deed;
- foreseeing potential conflicts before they arise;
- having trustee appointment procedures that require the disclosure of conflicts;
- keeping an up to date register of interests;
- recording conflicts issues in trustee minutes;
- options for managing and avoiding conflicts;
- confidentiality agreements;
- discussions about remunerating trustees;
- requiring advisers to declare conflicts; and
- sharing advisers with the employer.

Appendices include suggested forms for a register of conflicts, declarations of interests, and a conflicts policy and procedure document. There are numerous references to the need to take legal advice in various circumstances.

There is only a passing reference to the requirements of company law regarding directors' interests, noting (rather unhelpfully, given that they are directly relevant to trustee company boards) that this is outside the scope of the guidance.

www.thepensionsregulator.gov.uk/whatsNew/pn08-04.aspx

Pensions Regulator consultation on mortality assumptions as a new trigger

The Pensions Regulator has published draft guidance on "Good practice when choosing assumptions for defined benefit pension schemes with a special focus on mortality". Consultation on the draft guidance closes on 12 May 2008.

The Regulator is of the view that very many schemes are using inappropriate mortality assumptions when valuing scheme liabilities. It takes the view that mortality assumptions that appear to be weaker than the "long cohort" assumption or that assume that the rate of improvement in longevity will tend towards zero, and have no underpin, are very often inappropriate. They will therefore attract the Regulator’s scrutiny, as regards scheme valuations with effective dates "from March 2007". (This could affect schemes whose trustees have already chosen their assumptions.) Also, mortality assumptions should be evidence-based and clearly and transparently described.

www.thepensionsregulator.gov.uk/whatsNew/PN08-03.aspx

IASB discussion paper on IAS19

On 27 March 2008, the International Accounting Standards Board (IASB) published a discussion paper on reforms to accounting standard IAS19. The deadline for responses is 26 September 2008. The IASB hopes to issue a revised standard by 2011, with the publication of an exposure draft before that.

The IASB proposes to remove the options for deferred recognition of gains and losses in defined benefit schemes, so as to avoid misleading financial reporting and to allow better comparability across companies.

www.iasb.org/News

Money laundering regulations – registration for "trust or company service providers"

"Trust or company service providers" are required to be registered with HM Revenue & Customs (HMRC) from 1 April 2008 (but see below) under anti-money laundering legislation. This clearly includes professional trustees but there has been confusion, partly due to the regulations and partly due to unhelpful HMRC guidance, as to whether other individuals who are paid for acting as trustees (or as directors of a trustee company) need to register and, if so, in what circumstances. The test under the regulations is whether they are acting "by way of business" but so far HMRC has not been clear as to how they interpret this in the context of a pension scheme trustee board. Trustee boards can, for example, include pensioners or deferred members who are offered payment for their time commitment, or an independent person who may not be in business as a professional trustee but who is remunerated on a more professional basis because of his or her skills and/or experience.

The registration deadline is 1 April 2008 but HMRC has announced that, pending updated online guidance (which had not yet been published at the time of writing), trust or company service providers will be allowed to register without penalty until 31 May 2008.

www.hmrc.gov.uk/mlr/

Finance Bill 2008

The Budget was delivered on 12 March 2008. There were a few pensions-related points to note. The 2008 Finance Bill, published on 27 March 2008, will amend primary legislation to make some of these changes. The first five items below are new; the rest were in last October's Pre-Budget Report:

Trivial commutation: The Government will be announcing "changes to ease the administration of making certain trivial commutation payments and to help tackle the issue of small stranded pension pots". "Some small 'stranded pots' as well as pension savings below £2,000 in occupational pension schemes" will be capable of commutation, without looking at benefits in other schemes but only up to a maximum in total of £16,000 (this probably refers to 1% of the lifetime allowance, ie, in fact now £16,500). In other words, an individual's small occupational scheme pension can be commuted for triviality regardless of what benefits he or she may have under other pension arrangements, up to a maximum of £16,000 (or probably 1% of the lifetime allowance).

Stamp duty: Pension Scheme deeds that previously needed to be submitted to HMRC's Stamp Office to be stamped with £5 fixed duty will no longer need to be. This applies to deeds executed and dated from 13 March 2008 onwards.

Employers' tax relief: There is provision to clarify that before 6 April 2006 (and since 1 April 2004, when legislation was changed) only employer contributions actually paid to exempt approved pension schemes in the relevant accounting year were entitled to tax relief.

Unauthorised payments: There is provision to "allow certain payments from pensions schemes to be taxed in the same way as other authorised payments made by pension schemes instead of as unauthorised payments". This refers to the tax chargeable on such authorised payments. At present, regulations may deem certain previously unauthorised payments to be authorised, but cannot provide for their taxation treatment: this means that some such payments are not subject to tax, including income tax. The primary legislation will therefore be amended to allow regulations to provide for this.

Overseas schemes: UK tax relief and charges for overseas pension schemes will "equate with those for registered pension schemes" from 12 March 2008 for non-UK defined contribution schemes and from 6 April 2008 for non-UK defined benefit schemes.

Pension increases: Changes will be made to how the lifetime allowance operates for pension increases (benefit crystallisation event 3 (BCE3)).

- Pension increases of £250pa or less will be exempt from the BCE3 test.
- Currently there is an exemption from the BCE3 test if all pensioners receive the same increase; now only a class of 20 is needed for the exemption to apply.
- Pension increases will be exempt so long as they do not exceed a "normal" rate of increase in a 12 month period (5% or RPI if higher).
- For this purpose, schemes may use the RPI increase figure for any month within 12 months before the pension increase occurs.

- Rounding up will not require a further BCE3 test.

The changes will be backdated to 6 April 2006 (apart from the change in calculation of RPI which will have effect from 6 April 2008).

Protected lump sums: In order to simplify the administration of protected benefits, where, after 6 April 2006, additional contributions are made or additional benefit accrues in respect of a member with a protected pre-6 April 2006 uncrystallised lump sum of over 25% of the value of the member's benefits, trustees will not have to calculate whether relevant benefit accrual has taken place.

Employer's tax relief: There are provisions designed to avoid the spreading of tax relief on large employer contributions by routing them through a different company. This will apply to payments made on or after 10 October 2007 (when this was first announced) under binding obligations entered into on or after 9 October 2007.

Inheritance tax anti-avoidance: Surrenders of annuity payments from 10 October 2007 and increases in pension rights attributable to the death of a connected member from 6 April 2008 will be chargeable to inheritance tax. This will not apply to schemes with more than 20 members, provided that the same increase provisions apply to all members.

Taxable property: The definition of "investment-regulated pension scheme" (schemes where more than 10% of the members can direct or influence some part of the scheme's investment) is to be amended to ensure that unauthorised payment charge provisions do not unintentionally catch large schemes with defined contribution AVC arrangements or some schemes with a closed defined benefit section and an open defined contribution section. This will be backdated to 6 April 2006.

Overseas schemes:

From 6 April 2006, protection from inheritance tax will be restored for savings in overseas pension schemes that are tax-recognised and regulated in their own country, or that provide a pension income for life.

www.hmrc.gov.uk/budget2008/index.htm
www.hm-treasury.gov.uk/budget/budget_08/bud_bud08_index.cfm
http://services.parliament.uk/bills/2007-08/finance.html

Breakspear and others v. Ackland and another (2008) ALL ER (D) 260 (FEB)

This is a High Court case concerning the disclosure (or otherwise) of an expression of wish letter. The issue arose in the context of a family trust and a wish letter issued to the trustees by the effective settlor at the time the settlement was made. It is for various reasons not directly applicable to pension scheme trusts (and the judge is careful to say this). It does, however, look at precedent case law that is equally relevant to pension schemes, including *Re Londonderry's Settlement* and *Schmidt v Rosewood Trust Ltd*, so it will be of interest when considering whether pension scheme trustees can be required to disclose an expression of wish form in disputed death benefit claims. This is only a High Court decision, interpreting the decisions of higher courts.

The High Court (Briggs J) ruled as follows:

- *Re Londonderry* and *Schmidt* are still good law (and a court of first instance is not entitled to overturn them anyway). The judge interpreted them as meaning that trustees have a discretion whether or not to disclose confidential materials that are relevant to the exercise of their discretion. It will often be in the interests of beneficiaries to keep wish letters confidential:

  "trustees should in general regard a wish letter … as invested with a confidentiality designed to be maintained, relaxed or if necessary abandoned, as they judge best serves the interests of the beneficiaries and the due administration of the trust."

- The Court will not normally interfere with a trustee decision not to disclose such documents. (The judge disagrees with trust law text books indicating that the Courts' tendency these days is towards requiring disclosure.)

- In the present case, however, the trustees had indicated that they would in due course ask the Court to approve a proposed method of distribution of trust assets. The wish letter would become directly relevant in those proceedings and the rights of the potential beneficiaries to argue their positions would override the risk of family division. The wish letter should therefore be disclosed but the trustees could avoid this if they decided not to persist with the proposed application to the Court. The application to Court would effectively be a waiving of confidentiality and the *Re Londonderry* principles would be displaced.

www.bailii.org/ew/cases/EWHC/Ch/2008/220.html

"Myners" principles – joint consultation

HM Treasury, the Department for Work and Pensions and the Pensions Regulator launched a consultation on 31 March 2008 on updating the Myners principles – "a voluntary set of 'comply or explain' principles designed to improve trustee investment decision-making and governance of pension funds". The consultation proposes simplified, higher level principles and "a comprehensive suite of authoritative best practice guidance and tools". Responses are requested by 23 June 2008.

www.hm-treasury.gov.uk/newsroom_and_speeches/press/2008/press_32_08.cfm
www.hm-treasury.gov.uk/consultations_and_legislation/myners/consult_myners_index.cfm

Pension protection levy and investment risk

The Pension Protection Fund's chief executive has announced that a consultation on the future of the pension protection levy, to be published later this year, will consider once again whether the levy should take account of investment risk. The PPF had confirmed on 24 May 2007 that investment strategy will not be included as a separate risk factor in the risk based levy for 2008/9 but that key trends that affect the impact of investment risk would continue to be monitored.

www.pensionprotectionfund.org.uk/news-details.htm?id=6449

The PPF has also published a KPMG survey of 95 mainly large pension schemes which considers the impact of investment strategies on the PPF levies they pay.

www.pensionprotectionfund.org.uk/ppf_investment_strategy_and_ldi_survey.pdf

Pension Protection Fund Ombudsman decisions

The Deputy Pension Protection Fund Ombudsman has rejected three appeals against pension protection levy determinations for 2006/7. All three failed, as indeed did the only previous appeal.

- In *GC Bateman Group*, it was argued that the PPF had not considered the merits of exercising its (then) discretion to review levies after the submission deadline had passed. The Deputy Ombudsman was satisfied that this had ultimately been done.
- In *Middlesex Group Limited*, the trustees' argument that levy amounts would be better used to fund the scheme fell, as one would expect, on deaf ears. Complaints that Dun & Bradstreet would not show their workings were dismissed because the Ombudsman had no jurisdiction over Dun & Bradstreet.
- In *Scottish and Grampian*, the trustees had missed the 31 March 2006 deadline for submitting their s179 PPF valuation by three days. The PPF had therefore rolled forward the last MFR valuation, resulting in the risk-based element of the levy being £130,541 rather than £2,624. The Deputy Ombudsman determined that he could not uphold the trustees' appeal because the PPF Board had not used "incorrect" information and could only take into account information provided late if it had requested it itself.

www.ppfo.org.uk/determinations.asp

Salary sacrifice – new HMRC guidance

HM Revenue & Customs has published new salary sacrifice guidance. There are no changes in policy but the new document outlines, in greater detail than previously, the potential downsides for employees of salary sacrifice arrangements, for example, as regards entitlement to state and statutory benefits.

www.hmrc.gov.uk/specialist/salary_sacrifice.htm

Notional earnings cap 2008/9

HMRC has confirmed that the notional earnings cap for the 2008/9 tax year is £117,600.

www.hmrc.gov.uk/pensionschemes/earns-cap-0809.htm

Cohabitation – pension sharing and earmarking

The Government has announced that it is putting on hold any action in response to the Law Commission's report of 31 July 2007 on cohabitation and relationship breakdown, pending a research project by the Scottish Executive. The Law Commission had recommended that pension sharing and earmarking (attachment) orders should be available where cohabiting partners' relationships break down.

www.justice.gov.uk/news/announcement060308a.htm

DWP will not appeal Court of Appeal judicial review rulings

The Government will reportedly not appeal the Court of Appeal's recent decision in the judicial review proceedings brought by the Pensions Action Group. This does not mean extra compensation for affected individuals: the Government had already agreed to increase Financial Assistance Scheme compensation levels to (broadly) PPF compensation levels. Individuals will be potentially entitled to more only if they can convince a court that they saw, read and relied upon the Government literature that the Court of Appeal found to be misleading.

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If you wish to discuss any points arising from this note, please speak to your usual contact in the Travers Smith Pensions team or to one of the Pensions partners: Paul Stannard, Peter Esam and Philip Stear.

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