TRAVERS SMITH

What's happening in Pensions

Issue 21 *September 2010*

Indirect employer-related investments

From 23 September 2010, a pension scheme's *pro rata* share of employer-related investments held by collective investment schemes in which they invest will count towards the 5% statutory limit. This includes collective investments structured as unit trusts, investment trusts or insurance policies.

23 September is the deadline for the UK to align its employer-related investment legislation fully with the requirements of the EU's "IORP" directive. That directive requires EU member states to introduce legislation requiring that:

> "*… investment in the sponsoring undertaking shall be no more than 5% of the portfolio as a whole and, when the sponsoring undertaking belongs to a group, investment in the undertakings belonging to the same group as the sponsoring undertaking shall not be more than 10% of the portfolio*".

At present, the UK law has exemptions for employer-related investments held indirectly through pooled fund vehicles. Regulations already made in 2009 (see **WHiP Issue 9**) remove the exemption for investments held via "qualifying insurance policies" from 23 September 2010. (These are insurance policies issued by insurers authorised by the FSA or the equivalent body in another EEA country). When those regulations were made, the Government said that it was still thinking about whether the exemption for widely-held collective investment schemes would be compatible with EU law after 23 September 2010. We and other parties made submissions to the Government pointing out the difficulties for trustees in monitoring underlying investments.

The Government has now laid amending regulations that will withdraw the exemption for collective investment schemes. The Government's position is that must do this in order to comply with EU law.

There is nothing in the new amending regulations to address other problems with the legislation that arise when trustees wish to invest in the products of scheme employers who are insurers or investment managers.

It is disappointing that the Government has not taken a pragmatic view and that, having had a long time to consider the matter, it has announced the change only 21 days before implementation. Trustees will need to consider whether the new "look-through" requirements might cause them to exceed the 5% limit on employer-related investments now or in the future. Obtaining the necessary information or reassurances from fund managers will not always be easy.

Press release:
http://www.dwp.gov.uk/newsroom/press-releases/2010/sep-2010/dwp115-10-020910.shtml

Amending regulations:
http://www.legislation.gov.uk/uksi/2010/2161/contents/made

Equality Act 2010

The Government has announced that the bulk of the Equality Act 2010 (see **WHiP Issue 18**) will be brought into force on 1 October 2010. The Act is intended to consolidate existing anti-discrimination legislation, bringing sex, age, race, disability, sexual orientation, etc discrimination legislation together under one Act. In doing so, there is no intention to make any changes to the law.

New regulations providing exemptions in the fields of age and sex discrimination, which replace regulations issued under legislation that is about to be repealed, match those available under the current legislation almost word for word.

Regulations:
http://www.legislation.gov.uk/uksi/2010/2132/made

http://www.legislation.gov.uk/uksi/2010/2133/made

CPI in place of RPI

Most of the Government's stated objectives for using CPI instead of RPI can be achieved without having to change the law (see **WHiP Issue 20**). But some changes

Consultation:
http://www.dwp.gov.uk/consultations/2010/fas-ppf-regs-2011.shtml

are required, notably for the Pension Protection Fund and the Financial Assistance Scheme.

The DWP has now published draft regulations concerning the use of CPI instead of RPI in relation to compensation payments made by the PPF and FAS. The regulations will make the following changes to PPF compensation from 31 March 2011:

- Revaluation of compensation will be by reference to CPI for periods from 1 April 2011.
- The section 143 funding test for schemes that have entered a PPF assessment period before the CPI change is in force may be applied using CPI if the actuary believes that the scheme may be able to buy out benefits on that basis.

There are further changes, for example, as to the increase of PPF compensation in payment, which cannot be made by regulations because they require an Act of Parliament. The Pensions and Savings Bill is going to be used for this purpose. It is intended that the Bill will receive Royal Assent by the end of 2011 so that 2012 indexation payments can be calculated using CPI.

It remains to be seen whether the Bill will include provisions to help private sector schemes move from RPI to CPI.

Pensions Regulator: struggling employers

Statement:
http://www.thepensionsregulator.gov.uk/docs/regulated-apportionment-arrangements-statement-august-2010.pdf

The Pensions Regulator has issued a statement on "Regulated apportionment arrangements (RAAs) and employer insolvency". RAAs are a facility open to employers who wish to reallocate a section 75 debt due from an employer leaving the scheme to one or more other scheme employers. They are used when the employer is insolvent (or is likely to become insolvent) and they require the Regulator's approval.

The Regulator's statement outlines the process for RAA applications, which the Regulator says should also be followed when a scheme is to be transferred to the PPF in order to keep a business afloat.

PPF long-term funding strategy

Press release:
http://www.pensionprotectionfund.org.uk/news/pages/details.aspx?itemID=181

Strategy document:
http://www.pensionprotectionfund.org.uk/DocumentLibrary/Documents/PPF_Funding_Strategy_Document.pdf

The Pension Protection Fund has published its long-term funding strategy for the first time. Its aim is financial "self-sufficiency" by 2030.

The strategy is designed to achieve a "fully funded" position by 2030 in which the PPF has virtually no investment risk and has reserves to cover longevity risks. The PPF will then no longer be reliant on future levy income to pay compensation in respect of schemes that have then already been taken over by the PPF. The strategy also anticipates that the underfunding risks of eligible schemes will reduce as they become better funded and as they de-risk as well.

The PPF hopes that this strategy will reassure employers who plan to continue operating DB schemes that the PPF levy will not ratchet up over the long term as other employers wind up their schemes or become insolvent.

Public sector pension reform

Report:
http://www.public-sector-pensions-commission.org.uk/wp-content/themes/pspc/images/Public-Sector-Pensions-Commission-Report.pdf

The Public Sector Pensions Commission was set up by the Institute of Economic Affairs, Institute of Directors and other groups and is chaired by Peter Tomkins. It has published a report "Reforming Public Sector Pensions: Solutions to a growing challenge". It says that reform of public sector pension arrangements is necessary for various reasons and it sets out a number of options.

Pensions Ombudsman: ill health pension rule

Determination:
http://www.pensions-ombudsman.org.uk/determinations/docs/2010/jul/76135.doc

Mr Atkinson, a pilot for First Choice, began long term sick leave in 2003 and received benefit from his employer's PHI scheme. In October 2007, he requested an incapacity pension from the employer's pension scheme but this was declined on the ground that he was well enough to carry out "ground-based duties related to the occupation of a pilot". In November 2007, his employment was terminated by compromise agreement and he received an unspecified but substantial lump sum. In January 2008 and March 2008 he asked the company to review and review again its incapacity pension decision. Again the application was declined, with the doctor commenting that "*I do not think that* the current medical evidence supports a view that he is permanently unfit to undertake any work, including work appropriate for his qualifications and experience".

Unfortunately, this bore little relation to the definition of "Incapacity" in the pension scheme rules: "*in the opinion of the Principal Employer, the Member is (and will continue to be) incapable of carrying on his occupation because of physical or mental impairment …*".

The Pensions Ombudsman determined that Mr Atkinson's occupation was being a pilot, which meant being actively engaged in flying: a person who could never fly again was not capable of being a pilot. He therefore satisfied the scheme's definition of "Incapacity".

The Ombudsman therefore determined that Mr Atkinson should be awarded a backdated incapacity pension. However, the sum received by Mr Atkinson as compensation for loss of employment should be taken into account. Therefore:

- he would not be awarded interest on the late payment of pension and lump sum because he had had the enjoyment of the compensation payment in the mean time; and
- the payment of the incapacity pension was declared by the Ombudsman contingent on Mr Atkinson repaying the sum he received under the compromise agreement. (It is not clear on what basis, other than on nebulous grounds of overall fairness, the Ombudsman thought he could impose this condition. The rules seem clear that the trustees must pay Mr Atkinson an incapacity pension whether or not he pays back money to his former employer. The employer had made its own mistakes in getting the pension decision wrong and in failing to ensure that the compensation payment was conditional on no claim for an incapacity pension.)

Accounting for pensions: APB practice note

The Auditing Practices Board has issued an exposure draft update of its Practice Note 15 on "The audit of occupational pension schemes in the United Kingdom". It is intended to apply in respect of accounting periods ending on or after 15 December 2010.

Press release:
http://www.frc.org.uk/apb/press/pub2333.html

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