

Trustee Knowledge Update

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Welcome to the March 2011 edition of our Trustee Knowledge Update. The purpose behind this Update is to inform trustees about changes in the law to help them to comply with the legal requirement for each trustee (or trustee director) to have knowledge and understanding of the law relating to pensions and trusts. This Update focuses on the key legal developments over the last three months that trustees may need to be aware of.

Legislation (<http://www.legislation.gov.uk>)

Pensions Bill 2011

This Bill will make a number of changes to legislation. It:

Surplus: extends the period for trustees to pass a resolution to retain powers to distribute surplus from April 2011 to April 2016 and clarifies when a resolution will be required.

Auto enrolment: legislates for the changes to auto-enrolment as a result of the Government's review (which were set out in TKU Issue 14).

State pension age: amends the timetable for increasing state pension age to 66. It will begin rising from 65 in December 2018 and reach 66 in 2020. The equalisation of state pension ages at 65 will be accelerated so that female state pension age reaches 65 in November 2018.

Increases: The basis for calculating statutory increases to pensions in payment has changed from RPI to CPI. Provisions in the Bill will ensure that where rules currently require pensions to be increased by RPI there will generally be no need to do an annual comparison of RPI and CPI and pay the higher of the two. The Bill also removes the requirement for cash balance benefits to be indexed.

Cases

Association Belge des Consommateurs Test-Achats ASBL (European Court of Justice)

The European Court of Justice decided that the provision in the Goods and Services Directive allowing gender based insurance premiums is contrary to the general principle of equal treatment for men and women and will be invalid from 21 December 2012.

This case did not deal with occupational pension schemes, although it is expected to have a direct impact on the cost of annuities offered by insurance companies in the future. However, schemes will need to consider its implications.

Pensions are dealt with in the Equal Treatment Directive which like the Directive in the case, permits the use of sex based actuarial factors in certain circumstances. In addition, the ECJ has held in cases concerning UK pension schemes that the use of sex-based actuarial factors did "not fall within the scope of [the equal pay provisions] of the EEC Treaty."

European law has developed considerably since these cases were decided and it seems likely that the law in relation to the use of sex-based factors in pension schemes

will move in the same direction as *Test-Achats* (or indeed may have already done so if the case is treated as establishing a general principle). Schemes therefore need to discuss the position with their advisers and determine whether they should change the factors that they use.

Cubic v Weale (High Court)

A Member was allowed to retire at age 60 with an actuarial reduction in accordance with the Scheme rules. He had transferred benefits into the Scheme earlier and claimed that under his previous scheme, he had an absolute right to take a pension unreduced at 60 and he had transferred his benefits on the basis he would have the same rights under the Scheme. The Ombudsman upheld his complaint.

The High Court reversed this decision. The Ombudsman was wrong in law to look at a letter from his employer saying that the transfer "should provide... benefits... equivalent overall to those you would have received" in isolation, particularly when the benefit summary for the new scheme expressly said that taking early pension was subject to trustee and employer consent, and the member signed a form on the transfer which said that he understood that the benefit summary set out the rights to which he would become entitled. Reading the documents together, there was no clear representation that the member would be entitled to unreduced benefits at 60. Nor had the member relied on any representation to his detriment.

Tax (www.hmrc.gov.uk/pensionschemes/index.htm)

Guidance on pension input periods and carry forward

Pension input periods ("PIPs") are used to determine how much of their annual allowance a member has used in each year. Members of defined benefit schemes at A Day that have taken no action in relation to their PIP will have one which ends on 6 April. This is significant as the changes being made to the annual allowance apply to PIPs ending in 2011/12 tax year.

This guidance confirms that it is permissible to retrospectively nominate the first PIP to end on 5 April 2007 (so long as members are told of the nomination). This would mean that the current PIP would end on 5 April 2011 (in the 2010/11 tax year). HMRC has also confirmed in correspondence that the window to retrospectively nominate a PIP will end on Royal Assent to the Finance Bill, rather than on 6 April 2011 (the date from which the provisions of the Bill are planned to be effective). This is expected to be 1 July 2011.

The guidance also confirms that an individual can carry forward relief from a year in which they made no pensions savings and looks in more detail at what carry forward will

be available for the 3 years preceding the changes being brought into force.

Anti-avoidance – disguised remuneration

Legislation will be introduced in Finance Bill 2011 to ensure that where trusts and vehicles such as Employer Financed Retirement Benefit Schemes (unregistered pension schemes) are used, there will be a tax charge on sums made available to employees by the trust. The amount will count as employment income and will be subject to PAYE and National insurance. The legislation will apply to rewards from 6 April 2011 but anti-forestalling provisions apply from 9 December 2010. There will be protection for specified types of arrangements including registered pension schemes. The tax treatment of benefits which are genuinely available to substantially all employees not just selected individuals will not be affected.

HMRC has published details on how these provisions are intended to work in a series of FAQs. The FAQs explain in greater detail when the charge will apply and how the exemptions operate.

Pension Scheme Newsletter 44

The Government announced in July 2010 its intention to remove the unauthorised payments charge where an individual aged between 50 and 55 transfers a pension in payment on or after 6 April 2010. The Government has decided that the protection should extend to situations where an individual buys a scheme pension or an annuity using funds from an unsecured pension fund.

The Government also wants to clarify that the date on which the normal minimum pension age test should apply is the date of the first payment of pension. In Newsletter 38, HMRC incorrectly stated that the relevant date was the date on which the member became entitled to draw their pension. Where people have acted in reliance on that Newsletter, HMRC accepts that there should be no unauthorised payments charge in respect of payments of pension made before age 55.

Pensions Newsletter 45

There is a further reminder that the transitional regime under the Finance Act 2004 which allows references in schemes to the previous tax regime to continue to work, will expire on 5 April 2011. Schemes need to consider whether they need to take any action before that date.

HMRC is also considering the impact of the Scotland Bill (which devolves tax setting powers to the Scottish Parliament) on occupational pension schemes.

Draft guidance on reduction of lifetime allowance

From 6 April 2012, the lifetime allowance will be reduced to £1.5 million from £1.8 million. The draft guidance summarises how the lifetime allowance works and when benefits will be tested against it.

There will be a new form of protection called 'fixed protection' which will be available to people who expect the amount of their pension savings to be more than £1.5 million. Individuals will have to apply for fixed protection before 6 April 2012 and it will protect benefits up to £1.8 million where they stop accruing benefits in any registered pension scheme by 5 April 2012. If employees are auto-enrolled into a scheme and do not opt-out within 1 month, they will lose fixed protection. Anyone with existing primary or enhanced protection will continue to be unaffected by the reduction in the lifetime allowance.

The amount of pension savings that can be commuted on grounds of triviality will no longer be linked to the lifetime allowance – it will be fixed at its current level of £18,000.

Summary of discussion document on when annual allowance charge can be paid from scheme

The Treasury has announced more details of its plans to allow annual allowance charges to be met from benefits. If members trigger an annual allowance by reference to benefits in one scheme, and their total annual allowance charge is over £2000, that scheme must meet the charge (in so far as it relates to it) from the member's benefits where the member so requests.

The Government does not intend to prescribe how schemes should adjust benefits, but the method should be "fair and accurate". Schemes will be able to establish their own time limits and processes for doing this (but the election must be made by the 31 July in the year after the tax charge arose - or 31 December 2013 for the first election). If a member is approaching a benefit crystallisation event, they must make the election for the scheme to pay the tax before benefits come into payment and the scheme must adjust the benefits before they come into payment.

Regulations will require trustees to provide active members whose savings exceed the annual allowance with the information they will need to work out the amount of the charge. The information will need to be provided by the 6th October following the end of the tax year (or 6th October 2013 for the 2011/12 tax year). The employer must supply trustees with information to calculate the pension input amount no later than 6th July following the end of that tax year (or 6th July 2013 for the 2011/12 tax year).

Regulator (www.pensionsregulator.gov.uk)

Recovery plans – assumptions and triggers

Looks at valuations with an as at date of between 21 September 2008 and 2009 and compares them with previous years. Overall, there was an aggregate deficit of £192bn (on the s179 basis) at the end of March 2009, compared with an aggregate surplus of £20bn one year earlier and 84% of PPF-eligible schemes were in deficit. The key trends noted were as follows:

- Average recovery plans increased by one year to 9.4 years.
- The proportion of schemes triggering further Regulator involvement in relation to recovery plans rose to 81%.
- UK gilt yields reached the lowest levels since the start of the scheme funding regime.
- There was a decrease in the number of clearances approved in 2009-2010 reflecting a decrease in applications but an increase in the number and complexity of open cases.

Guidance on transfer incentive exercises

Trustees should start from the presumption that such exercises are not in members' interests, but there is an acknowledgement that in limited circumstances this may not be the case. There are five general principles:

- members should be provided with clear information that is not misleading;
- impartial and independent advice should be accessible to all members and they should generally be required to take it;
- trustees should be consulted and engaged from the start of the process;
- the offer should be open and transparent so that all parties involved in the process are made aware of the reasons for the exercise and the interests of the other parties; and
- conflicts of interest should be identified and appropriately managed in a transparent manner, and where necessary removed.

Government

Independent Commission on Equitable Life

The Treasury has accepted the recommendations of the independent commission to allocate £775 million which equates to 22.4% of non-with profit annuity policyholders' relative losses. Relative gains will be set against relative losses for those with more than one policy and there will be a minimum amount (in the region of £10) below which payments are not made. Priority will be given to the oldest policyholders and the estates of deceased policyholders.

Government response on phasing out default retirement ages

Dismissing someone on grounds of age once they have reached age 65 will no longer be an automatically fair dismissal where the dismissal is on or after 1 October 2011. To avoid claims of age discrimination, an employer will need to objectively justify such dismissals.

In relation to the provision of risk benefits and concerns over the potential cost, the Government said that it "recognises that there is a risk that employers may cease to offer insured benefits as a consequence of the removal of the [default retirement age], and will therefore introduce an exception to the principle of equal treatment on the grounds of age for group risk insured benefits provided by

employers." Unfortunately, it is not clear that the exemption in draft regulations extends to life cover provided in occupational pension schemes. The Government also says "The absence of a [default retirement age], does not affect the setting of a 'normal retirement age'...for the purposes of occupational pension schemes."

PPF (www.pensionprotectionfund.gov.uk)

Guidance for overfunded schemes

This applies to schemes that are "overfunded" in the sense of being in PPF assessment, but with sufficient assets to cover PPF liabilities. Unless there is a scheme rescue, these schemes may be ordered to wind up. The guidance outlines the trustees' power to ask the PPF to reconsider its refusal to admit the scheme (eg. where they are unable to secure the benefits that would have been available from the PPF). It also covers how to obtain "closed scheme" authorisation where trustees, despite having taken all reasonable steps, are unable to get a full buy-out quotation.

Consultation on GMP Equalisation

The PPF is consulting on its approach to calculating compensation in relation to potentially unequal GMPs. Consultation ends on 21 March 2011.

Confirmation of 2012/13 levy deadlines

The PPF is going ahead with the proposed changes to the levy framework from 2012/13. The new formal deadline for submitting scheme information for the 2012/13 levy will be 31 March 2012. It is still important that schemes provide up-to-date information by 31 March 2011 as the PPF will use that to set the levy scaling factor for the first three years of the new framework. If the PPF implements transitional relief to cushion employers falling between the new, wider insolvency bands from 2012/13, this protection will be based on employer insolvency scores as at 31 March 2011.

PPF valuation assumptions changes

The PPF must keep the assumptions used for PPF-related valuations in line with estimated pricing in the bulk annuity market. In the light of the government's proposed change to index PPF compensation by CPI and recent developments in the buy-out market, the PPF is considering amending its existing assumptions.

Ombudsman (www.pensions-ombudsman.org.uk)

Lambden (74315/3) – exceptional circumstances justified awarding £5,000 for distress and inconvenience

Since 2000, the complainant police officer's pensionable service had been overstated by four years giving him 25 years' pensionable service. Had the 25 year figure been correct, it would have allowed him to take unreduced pension from age 50. In 2007, the member resigned and emigrated to New Zealand. He claimed that he would never have done so had he known he could not draw his pension.

The Ombudsman held that the member had not reasonably relied on the incorrect information. A letter sent and “probably received” by the member emphatically asked him to check the information recorded (which had the wrong information in relation to pensionable service). Whether or not he ever read the letter, “*having been asked to check wrong information, and not having done so, he cannot successfully argue that he relied on it.*”

The only remedy available to the member was payment for distress and inconvenience caused by the maladministration. The Ombudsman noted that authority suggested that he should not, other than in exceptional circumstances, award compensation for distress of over £1,000. He said: “*I consider these circumstances are highly exceptional. I do not doubt that Mr Lambden has suffered considerable distress. There is medical evidence of it. In part the effect on his health relates to the reliance that I have found was not reasonable, but the distress would still have been significant if he had identified the problem before resigning, as he should have. ... I have also taken into account that the error was discovered but not presented as such, nor softened by apology or explanation. I therefore set the compensation at £5,000.*”

Sheppard (76726/2) - backdated rule could override member booklet

The booklet mentioned an unreduced early retirement payable on redundancy but did not mention that employer consent was required. When the booklet was issued, the scheme only had an interim deed. When the detailed scheme rules were finalised, they included the reference to consent, backdating it to the outset of the scheme.

The Deputy Ombudsman held that case law established that rules generally prevailed over announcements, particularly where announcements specifically referred to

Dates for diaries: Trustee training remains one of the most important ways of ensuring that trustees have the knowledge and understanding required to perform their duties. We have a trustee training course taking place on **18 May 2011**. If you have any enquiries about any of these courses or would like to reserve a place, please contact **Karen Mumgaard – E:** karen.mumgaard@cms-cmck.com.

General: For further information on our pension services, please contact **Mark Grant – E:** mark.grant@cms-cmck.com, **T:** +44 (0)20 7367 2325 or your usual pension partner. Please also visit our new website at www.cms-cmck.com.

Get to grips with the requirements of the Pensions Regulator with our **Field Guide for trustees**. You will need to be a subscriber to our Law-Now website (which is free) to access this guide. Register at <http://www.law-now.com/register>. You can also get help here with understanding the Pensions Act 2004 and all related regulatory publications by viewing our online **Plain English guide to the Pensions Act**. If you are interested in the Pensions Ombudsman’s activities, visit our website www.law-now.com/po-info. This site also has links to around 70 useful pensions websites.

The Pensions team is part of the CMS Cameron McKenna HR group and advises employers and trustees of schemes varying in size, from a few million pounds to several billion pounds. Additionally, we act for some of the largest firms of administrators, actuaries, consultants, brokers and professional trustees. We provide a full range of services in connection with occupational pension schemes, including all aspects of employment law and EU law. The team also works closely with our corporate lawyers, providing support on mergers and acquisitions, insolvency lawyers supporting us on employer covenant issues, and the financial services team which specialises in regulatory and fund management matters.

The information in this publication is for general purposes and guidance only and does not purport to constitute legal or professional advice. It is not an exhaustive review of recent developments and must not be relied upon as giving definitive advice. The Update is intended to simplify and summarise the issues which it covers. It represents the law as at 4 March 2011.

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overriding rules. The fact that the deed was not available at the time the booklet was produced was insufficient to distinguish this case from that general legal principle. There could be no contractual right based on the booklet, because there was no certainty of terms: all relevant documents were expressed as summaries, rather than complete statements of benefits. Moreover, the employer and trustees were not “estopped” from relying on the change made by the later retrospective deed as the member had not relied on any representation to his detriment. However, they were criticised for allowing the booklet to go unamended on this point for some six years after the deed had been executed, and an award was made of £250 for the distress and inconvenience caused.

Things to look out for

GMP Equalisation: The Government has indicated that it intends to publish draft legislation later this year requiring schemes to equalise GMPs.

Finance Bill 2011: Schemes should be considering how they intend to deal with the changes to the annual allowance and the consequential information requirements which will be introduced with effect from April 2011. They should also be considering whether they need to change their pension input periods before the Bill receives Royal Assent (expected to be 1 July 2011).

Auto-enrolment: Employers and trustees should be starting to consider what impact auto-enrolment will have on them and their schemes. The first auto-enrolment requirements will apply from 2012.