

Trustee Knowledge Update

CMS Cameron McKenna

Welcome to the May 2013 edition of our Trustee Knowledge Update. It aims 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 edition focuses on the key legal developments over the last three months that trustees may need to be aware of.

Government

GMP Equalisation

The Government has published an interim response to last year's consultation on potential sex discrimination issues in relation to GMPs. Among other things, it had consulted on a possible methodology for equalising the effect of GMPs. This was the subject of widespread criticism as it would have required constant monitoring of benefits and provided both men and women with the higher level of benefits at all times. Although the Government remains clear that overall benefits for male and female members must be equal, a final version of this proposed methodology will not now be published. The Government is still considering whether further advice is required for schemes to deal with potential equalisation issues. It is looking at whether the GMP conversion process could be used to equalise scheme benefits and whether statutory guidance is required to help schemes using this process. There is no timescale for any further action.

Transfers and small-pots update

The Government has issued further details of its proposals to deal with small dormant pots of pension. They are much as expected and confirm that:

- automatic transfers will initially be only of "pure" money purchase pots
- a pot is eligible for automatic transfer (a) once all contributions have ceased and either the individual has left employment or a fixed period has elapsed; and (b) if was created after a specified date (so not all historic pots)
- the pot size limit will initially be £10,000
- there will be an option for members to leave pots in a previous employer's scheme, but they retain a right to request a transfer to another arrangement
- the Government will be able to specify standards for automatic transfer schemes
- short service refunds will no longer be payable from money purchase schemes from 2014.

The Government is still considering exactly how this will work in practice. There is no specified time frame for these changes but the Pensions Bill 2013 contains relevant legislation and regulation making powers.

Office for National Statistics - Consumer Price Inflation

Two new measures of inflation have been launched: CPIH (which includes owner-occupiers' housing costs) and RPIJ (an improved version of RPI, calculated using formulae that meet international standards). At the same time, the status of RPI as a National Statistic has been cancelled. However, the ONS will continue to publish it every month.

The question of which index trustees should use for pensions up-rating will depend on the wording of scheme rules, and schemes are not required to change their approach. However, trustees should ensure that they remain aware of ongoing developments.

Update on defined ambition schemes

More detail has emerged at an NAPF conference about the Government's ideas on defined ambition schemes. There are currently three proposed models:

- giving the sponsoring employer the option to adjust normal pension age to take into account revised longevity assumptions
- allowing employers to provide a pension with only discretionary indexation for future accrual and no spouse's benefits. Additional benefits could be provided depending on the health of the scheme at any time
- allowing benefits to start as DB but convert to DC when the member leaves employment. When an employee leaves, retires or dies the pension amount would be crystallised into an equivalent DC fund.

More details should be published in the summer.

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

The Occupational and Stakeholder Pension Schemes (Miscellaneous Amendments) Regulations

These Regulations make various changes to existing legislation. In particular, several changes are aimed at facilitating transfers to schemes which are closed to future accrual: connected-employer bulk transfers will be possible where the transferring and receiving scheme relate to members who are, or *have been*, in employment with the same employer and contracted-out benefits can be transferred to a scheme which was formerly contracted-out.

Changes to thresholds for 2012/13

April 6th brought with it changes to a number of figures that schemes use to calculate benefits. The key ones are:

- lower earnings limit - £109 per week
- upper earnings limit - £797 per week (a reduction from the previous year)
- primary threshold - £149 per week
- secondary threshold - £148 per week
- GMP increase rate - 2.2%
- GMP revaluation rate using s148 orders - 1.8%
- earnings trigger for auto-enrolment - £9,440 and qualifying earnings band for auto-enrolment - from £5,668 to £41,450.

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

Finance (No.2) Bill 2013

This will enact various tax measures announced since the March 2012 Budget, including:

- reducing the annual allowance to £40,000 in respect of the 2014/15 tax year;
- reducing the lifetime allowance to £1.25million from 6 April 2014 and providing for a new "fixed protection 2014" to protect members who have built up large pension pots within current limits (further details of which are in the Finance Bill 2013/14);
- giving power to modify the fixed protection provisions "to help ensure that individuals do not lose fixed protection in circumstances outside their control" (which could help with individuals who would otherwise be auto-enrolled);
- allowing drawdown pensioners to choose to receive an authorised pension from their scheme of up to 120% of the amount of an equivalent annuity (increased from 100%); and
- allowing schemes to continue to pay a bridging pension up to state pension age without incurring unauthorised payment charges.

Recent RPSM updates – April 2013

There are a number of updates to the Registered Pension Schemes Manual to reflect recent changes to pensions legislation and some clarifications. The main changes:

Test-Achats – reflect regulations which adjust the calculation of drawdown pensions so that a female member who has elected to have a drawdown pension will be able to have her maximum income calculated on the basis of male GAD tables.

Abolition of protected rights - reflect regulations which permit the payment of partial short-service refunds by schemes that were contracted-out on a defined contribution basis before 6 April 2012 and have not amended their rules to remove protected rights restrictions (as rules may not permit the refund of the former protected rights element).

Finance Act 2011 - add to guidance on the various changes following the Finance Act 2011 that removed requirements for members of take their benefits by age 75. Schemes should however be aware that there are still ways in which members over age 75 are treated differently and some changes to tax treatment after age 75.

Regulator (www.pensionsregulator.gov.uk)

Pensions Liberation

The Regulator, HMRC and Action Fraud have published several leaflets on pensions liberation aimed at both members and pensions professionals.

The leaflets give a number of examples of members who have transferred pensions to pension liberation schemes in return for promises of cash incentives and tax free cash. They highlight warning signs trustees should be aware of:

- receiving scheme is newly registered and transferring trustees have never previously come across it but are now being requested for transfers by several members
- unsolicited offers from the scheme to member
- transfers overseas
- offering benefits before age 55 and/or loans to members
- no documentation available
- members encouraged to speed up transfer and pressuring trustees
- talk about exploiting a legal loophole.

The Regulator will take concerns over liberation into account when looking at late payment of transfer payments but will expect to see evidence that the trustees have tried to establish the legitimacy of the receiving scheme.

Where trustees are concerned about a proposed transfer, there is suggested wording explaining the potential problem to send to members. There are also leaflets aimed at members that highlight the potential downside for them of pensions liberation and the tax charges.

New objective for the Pensions Regulator

The Chancellor announced in the Budget that the Regulator will be given a new objective "to support scheme funding arrangements that are compatible with sustainable growth for the sponsoring employer and fully consistent with the... funding legislation". The draft wording of this objective appears in the Pensions Bill 2013 and provides that the Regulator should exercise its powers in relation to scheme funding "to minimise any adverse impact on the sustainable growth of an employer".

Annual funding statement

The Regulator has published its second annual funding statement, aimed at schemes undertaking valuations with effective dates between 22 September 2012 and 21 September 2013. The Regulator acknowledges that trustees may need to make greater use of the flexibilities available within the funding regime but says that where trustees weaken assumptions or reduce employer contributions, they should document the reasons for doing so.

It encourages trustees to produce plans that take an integrated approach to managing the risks to their scheme, including funding levels, investment performance and the employer covenant. The statement also confirms that the Regulator is moving away from triggers focused on individual items (e.g. recovery plans more than 10 years long) and will now consider a range of different factors.

PPF (www.ppf.gov.uk)

GMP Reconciliation Guidance for PPF Schemes

Where mismatches occur between a scheme's records and NISPI's records, the scheme should undertake "one pass" to reconcile the two. "One pass" is *"a reasonable attempt in each case to resolve the issue and, where appropriate, agree any changes with NISPI"*. Trustees can agree with their administrators what constitutes a reasonable attempt. If they can resolve the query by "one pass", trustees should take appropriate action and either accept GMP liability for the member or give the evidence to NISPI so they can correct their records. Where queries cannot be resolved with "one pass", there are tables with a more detailed approach to be taken for fixing records.

The PPF says that whenever a scheme has an address for the member and is otherwise unable to resolve the query, they should write to the member to ask for information to assist, although any cases where a response is not received should not hold up the scheme transferring to the PPF, as unresolved issues will be taken up by the PPF post-scheme transfer.

Observations on the PPF's assessment of guarantor strength for selected Type A contingent assets

This reflects the PPF's position on last man standing schemes where the guarantor is also an employer. It confirms that the PPF will *"recognise contingent assets where we consider it is likely the guarantor could meet the deficit of the other employers (which are assumed insolvent) whilst still continuing to trade so that it can meet its own obligations over time..."*

Cases

Wheels Common Investment Fund Trustees Ltd v Commissioners for HMRC (ECJ, First Chamber)

This is the test case established by NAPF and the Wheels Common Investment Fund to challenge HMRC in relation to the payment of VAT on investment management services supplied to occupational pension schemes.

In this application for a preliminary ruling, the parties sought to establish whether the funds held by the Wheels CIF trustees and the underlying Ford trust funds were "special investment funds". The Court held that an investment fund which pooled the assets of a retirement pension scheme was not a 'special investment fund' within the meaning of the relevant provisions, management of which might be exempted from VAT. An investment fund in which the assets of a retirement pension scheme were pooled was not sufficiently comparable with collective investment undertakings to be in competition with them, and they could not be regarded as meeting the same needs. In particular, under a pension scheme members did not bear the risk arising from the management of the fund, and contributions paid by the employer were a means by which he complied with his legal obligations to his employees.

Pitt v Holt and Futter v Futter (Supreme Court)

These cases concerned the application of the so called rule in *Re Hastings-Bass* which was broadly understood as saying that the court could set aside a decision by a trustee where *"it is clear that he would not have acted as he did (a) had he not taken into account considerations which he should not have taken into account, or (b) had he not failed to take into account considerations which he ought to have taken into account"*. The Supreme Court followed the judgment of the Court of Appeal and held that a trustee's decision could only be set aside where it could be shown that they had acted in breach of duty and failed to consider something that they were under a duty to consider. *"It is not enough to show that the trustees' deliberations have fallen short of the highest possible standards, or that the court would, on a surrender of discretion by the trustees, have acted in a different way. Apart from exceptional circumstances (such as an impasse reached by honest and reasonable trustees) only breach of fiduciary duty justifies judicial intervention"*. It is however still possible to set aside a particular action because of a mistake as to fact or law where it would be "unconscionable" not to do so.

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

The Trustees of the West of England Ship Owners Insurance Services Limited Retirement Benefits Scheme (PPF should ensure trustees are aware of procedures in other jurisdictions)

The scheme had a type A PPF guarantee from a Luxembourg parent company. The policy of D&B Luxembourg, unlike D&B in the UK, was not to automatically access publicly filed company accounts when calculating failure scores but to use financial statements sent to it by companies. As the parent had never sent such statements to D&B Luxembourg, its failure score was much worse than it would have otherwise been. D&B accepted that the trustees could not reasonably have been expected to know what the practice was in Luxembourg. However, the PPF said that as the levy determination provided that it would *"use the scores set by D&B..."* it had no flexibility to do anything else.

The PPF argued that the Deputy PPF Ombudsman would go beyond her jurisdiction if she made any directions for the use of a failure score other than the normal failure score assigned by D&B. The Ombudsman responded that D&B Luxembourg was instructed by the PPF and the question of what actions it took or did not take was within her remit. She went on to say that it would have been helpful for the PPF to publicise what D&B did in other countries and the trustees could not reasonably be penalised for having failed to guess that it operated differently in different countries. *"Trustees are entitled to assume that D&B is doing its job properly, and should not have to bear the consequences of D&B's shortcomings, or the limitations placed on D&B by the PPF's instructions to it... I cannot see how a public body, properly directing itself, can decide that a statutory levy can be imposed based partly on a procedure that the*

levy payer was unaware of.” The Determination allowed recalculation of the levy.

In relation to professional advice, it was observed that there was no free service available to assist trustees pursuing redress against the PPF, and that *“depending on the circumstances of the case it may be appropriate... to make directions in respect of the cost of [professional advice]”*. In this case, the use of lawyers was justified, and the PPF should contribute £10,000 towards the trustees’ legal costs.

Brand (member could rely on estoppel to defeat trustees’ attempt to reduce “overpaid” pension)

The member retired in 2004, aged 62, and her pension was put into payment. At the time, the parties believed 62 to be normal retirement age (NRA) under the scheme rules. However in 2011 the trustees wrote to the member, saying that they had received legal advice that under the scheme rules her NRA had in fact been 65 since 1993.

The member complained, saying that had she known her NRA was 65 she would have carried on working until then to receive an unreduced pension. All benefit statements issued to her, as well as two early retirement quotes had reflected an NRA of 62. The trustees accepted that the scheme had, until 2011, been administered on the basis that NRA for women was 60 until 1996 and 62 thereafter.

The Deputy Pensions Ombudsman said that she did not need to decide what the correct NRA was because *“representations were made to Mrs Brand by the Trustee over a considerable period which she had no reason to doubt and on which it was reasonably foreseeable that she would rely.”* The scheme booklet and benefit statements amounted to *“clear unequivocal representations”* of the NRA of 60/62.

To succeed in an estoppel claim the member did not need to show what she would have done but merely that the representation was a significant factor which she took into account. It was more likely that not that the representations made as to NRA were a significant factor that the member took into account in making her retirement plans. It would be unconscionable to allow the trustees to go back on those representations. The trustees were directed to provide a pension based on NRA of age 60 until 1996 and 62 thereafter.

Miscellaneous

Changes to the Takeover Code for trustees

From 20 May 2013, trustees of schemes with defined benefit members have new information and disclosure rights about a bidder’s plans for the scheme. The rights will apply to all takeover bids governed by the UK Takeover Code and regardless of scheme size or where the scheme is based.

The bidder will have to include a statement in the offer document of its intentions with regard to employer contributions to the target’s scheme (including the funding of any scheme deficit), the accrual of benefits for existing members, and the admission of new members. The bidder will be held to any statement for 12 months, unless there is a material change of circumstances. Trustees can also require the target to publicise their opinion on how the offer will affect the scheme to its shareholders.

The changes bring the treatment of trustees under the Code broadly into line with employee representatives. They need to be borne in mind by both employers and trustees in listed takeover scenarios.

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 trustee training courses taking place on **11 June 2013 and 15 October 2013** and there will be others at regular intervals after that. 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 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.

The Pensions team is part of the CMS Cameron McKenna Human Capital 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 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 10 May 2013.

CMS Cameron McKenna LLP is a limited liability partnership registered in England and Wales with registration number OC310335.