

Trustee Knowledge Update

Welcome to the Autumn 2009 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 quarter that trustees may need to be aware of.

STOP PRESS: the Court has just given its judgment in the case of *ITS v Hope* which looked at the extent to which trustees can take into account the existence of the PPF when making decisions about securing benefits prior to entering a PPF assessment period. The court held that there was no hard and fast rule about the extent to which trustees could have regard to the PPF and it depended on all the circumstances of a particular case. However, in this case, where all of the scheme assets would be used to secure only some of the benefits, the availability of PPF compensation was not something the trustees should take into account, as allowing them to do so would be contrary to public policy. The court did however confirm that the trustees did not owe any duties to the PPF as if it were a beneficiary of the scheme.

PPF (<http://www.pensionprotectionfund.org.uk/>)

Levy invoicing for 2009/10: PPF levy invoicing is now underway for 2009/10.

A Guide to the levy will be sent out with all invoices and the invoice should come with “detailed supporting information” setting out how it is calculated.

The Guide explains how the levy has been calculated and the information that the calculation is based on. It also has a section on querying the invoice and what to do if you believe that the information it is based on is incorrect. Queries and appeals must be made within 28 days of the invoice date (the deadline should be set out on the invoice). Therefore, if you have a query about the invoice, you will need to act quickly.

PPF Draft Levy Determination for 2010/11: The PPF has published its draft levy determination and associated documents for the levy year 2010/11. The total levy will be £720m (the existing £700m, indexed to wages). There are no significant changes to the method of calculation, although the cap on the risk based element of the levy has been cut to 0.5% of PPF liabilities.

PPF solution for GMPs approved: The PPF began consultation in April 2008 on how GMPs should be equalised and is now nearing completion of the process. To satisfy its obligations to provide equal benefits for men and women, the PPF must:

- take into account any inequalities in scheme benefits that have arisen as a result of differences in the calculation of GMPs due to gender;
- establish that a “comparator” (a person of the opposite sex doing like work, or work rated as equivalent or of equal value) exists before making any adjustment for equalisation;
- ensure that payments made both before and after the assessment date have been made on an equal basis. (This means that for schemes that enter the PPF, the Board must ensure that all payments made in respect of pensionable service after 17 May 1990 are equal.)

The equalisation method the PPF seems likely to adopt is broadly to make a comparison of the total male and female pension based on rights accrued up to the date of PPF entry and then the pensioner should be paid the higher of the male or female estimate that applies in their particular case.

The Regulator agrees that equalising GMPs using the method that the PPF proposes would be “a pragmatic way of addressing the difficulties of Benefit Equalisation for GMP, for schemes that enter the PPF at the end of the assessment period as well as those that ultimately wind up and buy out benefits outside the PPF”. The PPF has asked the Regulator to consider confirming this view in its own guidance.

The Board is currently considering the mechanics of calculation and issues in relation to comparators after which it will make another statement.

Use of discretionary powers - draft: This is guidance on when the PPF will use its discretionary powers. However, it is only guidance and not legally binding and does not restrict the way in which the PPF can exercise its powers.

It looks at various cases where the information supplied to the PPF may have been incorrect. It says that it will only accept corrections to data in very limited circumstances and gives a number of factors that the PPF will consider when exercising its discretion to use corrected data. A number of examples are given as to when the PPF will and will not exercise its discretion.

The Guidance also looks at how the PPF will react to changes in contingent assets between levies. It says that where there is an “unacceptable change” to a contingent asset: the levy will be recalculated as if that asset had never been in place; *“where an unacceptable change occurs between levy years, no credit at all will be given for any contingent assets in the latter year (even if there remain some contingent assets with value which would otherwise satisfy the recognition requirements)”*; and the scheme may not be given credit for any contingent assets in future years until the position has at least been restored to that which prevailed before the unacceptable change occurred. Unacceptable changes are not likely to be ones permitted by the standard form agreements or outside of the control of the parties. Trustees considering a change to an existing contingent asset should consider this guidance.

Regulator (<http://www.pensionsregulator.gov.uk>)

Pensions Regulator investigation into money purchase pre-retirement literature: The Regulator has looked at literature from a number of money purchase schemes. Of the 97 schemes who submitted literature:

- 98% offered the open market option, although take up of the open market option was viewed as remaining low, at 23% of DC members retiring
- 57% of schemes had some scope for improvement in the standards of the retirement information sent to members
- 30% had alleged legislative breaches of retirement disclosure regulations
- 6% were referred to regulator casework teams to follow up the substantial changes required to their retirement literature or processes

As a result of this review, a letter will be sent to 4,500 schemes, highlighting the findings of the investigation and encouraging trustees to review the pre-retirement literature sent out to their members.

Guide for employers talking to employees about pensions: sets out questions that employers may be asked by their employees about pensions and suggests possible answers and other sources of information that employees can be referred to.

The Guide is published jointly with the FSA and looks at the information that employers can give employees without falling foul of financial services legislation. It includes things such as whether it is a good idea to join the scheme, what the employer can say in general about pensions, what advice they can give when employees are approaching retirement

and in relation to investment options and how far they can go in promoting their scheme.

Whilst the Guide is aimed at employers, it contains useful information for any trustees dealing with member queries.

Government

(<http://www.dwp.gov.uk/consultations/>)

Draft amendments to Employer debt regulations: provide two new circumstances when a section 75 debt will not arise when an employer ceases to participate in a scheme. The new provisions are intended to help in corporate restructurings where another employer takes over responsibility for the employees of the exiting employer and the exiting employer's liabilities in relation to the scheme. If this happens, a section 75 debt will not be payable if the trustees are satisfied that:

- the new employer is “at least as likely” to meet the exiting employer's liabilities and its own continuing liabilities; or
- scheme assets are at least equal to the value of the PPF liabilities; less than 2% of final salary members are involved; the value of the scheme's PPF liabilities relating to the exiting employer is not more than £100,000; and in a rolling period of three years, no more than 5% of final salary members are subject to transactions falling within this provision.

In both cases no insolvency event must be likely in relation to either employer within the next 12 months and certain formal steps must be complied with.

A similar outcome can be achieved using the existing provisions on scheme apportionment arrangements, but those arrangements require trustee consent whereas these new exceptions will apply automatically if the relevant conditions are satisfied.

These Regulations are due to come into force in April 2010 but we understand that the Government is considering making further changes

Tax

(<http://www.hmrc.gov.uk/pensionschemes/index.htm>)

Update to Manual re Anti-forestalling: this is guidance on the special annual allowance charge which we described in previous editions. It contains some useful examples on how the charge will work in particular circumstances and help with determining when it applies.

Guide to using online services for Scheme Administrators and Practitioners: provides information about the role of the Scheme Administrator (which is

usually the trustee), how to access and use the Online Service, and what reports and returns need to be filed online. Includes information on how to file an Event Report and a Scheme Return and how to add or remove someone as a scheme administrator.

Personal Accounts <http://www.dwp.gov.uk>

Consultation on auto-enrolment: From 2012, employees will either need to be automatically enrolled into a pension arrangement provided by their employer or into the new personal accounts arrangement. This consultation looks at the mechanics of how auto-enrolment will work. It is proposed that implementation will be phased in over a three year period depending on the size of the employer. Generally, large employers will be required to start automatic enrolment before smaller employers.

The consultation paper also proposes that minimum employer contributions will be phased-in in defined contribution schemes over 3 years: 1% of qualifying earnings from October 2012; 2% the following year and then 3% after that.

In defined benefit and hybrid schemes it is proposed that employers will be able to defer automatic enrolment for up to 3 years (where the employee is entitled to join the scheme). There are special provisions which will apply where the scheme is closed within the 3 year deferral period.

Cases

Heyday (age discrimination)

This case concerned whether the permitted default retirement age of 65 in the UK age discrimination legislation was lawful. The court held that it was. There was a legitimate policy objective - to maintain confidence in the labour market and facilitate workforce planning.

However, the judge went on to say that the choice of a default retirement age of 65 had to be considered in the context in which it was adopted in 2006 but *“in the light of changed economic circumstances and the generally recognised problems that a longer living population creates for the social security system the case for advancing the default retirement age beyond 65 at least would seem to be compelling... If [the age 65 restriction] had been adopted for the first time in 2009, or there had been no indication of an imminent view, I would have concluded for all the above reasons that the selection of age 65 would not have been proportionate. It creates greater discriminatory effect than is necessary on a class of people who are both able to and want to continue in their employment. A higher age would not have any general detrimental labour market consequences or block access to higher level jobs by future generations.”*

A Government review of retirement ages is planned for next year.

Ombudsman (<http://www.pensions-ombudsman.org.uk>)

Edwards (75402/1): Definition of dependant

The scheme rules allowed the member to select a Nominated Dependant who could (at the discretion of the trustees) receive a pension on the member's death. A Nominated Dependant had to be:

“an adult person nominated by a Member...[where] at the time of the Member's death the Member was unmarried and both at the date of nomination by the Member and the date of the Member's death the Trustees are satisfied the Nominated Dependant was wholly or partly financially dependent on the Member.”

The trustees' internal guidelines on payment of nominated dependants' pensions stated:

“The Rule is regarded as primarily intended to cover established marriage type relationships and is applicable to opposite or same sex partners... Other long-standing relationships involving material financial dependence or inter-dependence may also be considered... A clear distinction needs to be drawn, however, between those who are financially dependent and those who are merely “helped”, or derive a benefit. The Rule was not intended to cover the latter.”

In this case the trustees decided not to pay any pension to the applicant, who was the member's carer, saying that a child looking after an aged parent was “a fairly normal family situation” and that the applicant had derived a benefit from it (i.e. the close relationship with her father).

The Ombudsman said that the trustees had complete discretion as to whether to pay the pension, if two criteria were established: that the applicant had been nominated by the member (as was the case here), and that she fell within the test of dependence. However: *“As the internal guidelines indicate, the Trustee applies different standards of dependency to those who are not in “marriage type” relationships to those that are. I do not think that is right. Either there is dependency at the time of nomination and death or there is not. The dependency definition is the same for all.”*

It was only once the two criteria had been satisfied that the trustee could look at the wider range of factors such as the nature of the relationship, the extent of dependence, the possibility of change of circumstance. The trustees' finding was therefore maladministration.

James (74792/1): ill health benefits – policy for review

The Teachers' Pensions Regulations provided that a person was incapacitated if “*unfit by reason of illness or injury and despite appropriate medical treatment to serve as [a teacher]*”. When that person ceased to be so incapacitated, the pension ceased to be payable. In practice, Teachers' Pensions applied a test that if a member had returned to full-time teaching work, the pension would cease.

The Ombudsman held that they should not apply this shorthand test without consideration: “*applying a hard and fast rule that any person doing full time teaching, whatever its duration and whatever the work, must automatically at that time be fit to serve as a teacher is not consistent with the regulations...I have no criticism of TP for using the full time test and for presenting it as being determinative. In almost all cases it would be and it may be a practical approach to present it as such. But TP must at least pause to consider the particular case, and particularly so when the decision may result in a substantial overpayment and possible hardship.*”

The Ombudsman said the decision should be reconsidered, starting with whether the member had in fact been fit to serve

as a teacher when working full-time. The case illustrates the importance of trustees being able to tick a box showing that precisely the right test was applied in relation to ill health benefits.

Things to look out for

Minimum pension ages: trustees need to be aware that paying benefits (other than ill-health benefits) before age 55 will become unauthorised for tax purposes from April 2010 unless the member had a right to retire at an earlier date in December 2003 (such rights will need to satisfy certain conditions).

Further changes to anti-forestalling: It is still intended that there will be amending Regulations this year on anti-forestalling, but it is not known what they will say. However, the Government had indicated that it was considering representations on “flexibility for those who change provider” and “less stringent” rules for those who set up new pension arrangements just before Budget Day.

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 **20 January 2010**. If you have any enquiries about any of these courses or would like to reserve a place, please contact Karen Mumgaard at 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 Pensions Act 2004 and all related regulatory publications by viewing our online **Plain English guide to the Pensions Act**. 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/law-now/zones/LN_Pensions.htm. 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.

This Update is intended for clients and professional contacts of CMS Cameron McKenna LLP. 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.