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News on Pensions

MAY 2014

From the courts

IBM loses 'good faith' case

The High Court has ruled that IBM breached its duty to members of its two UK pension schemes when it amended pension scheme benefits (known as 'Project Waltz') in 2009. The judgement in *IBM v Dalgleish* serves as a warning to companies to tread carefully when amending defined benefit (DB) pension schemes.

In 2006, IBM made a number of changes to members' benefits that included giving members the choice between continued DB accrual (but with part of their pay becoming non-pensionable) or moving to a defined contribution (DC) arrangement for future benefits.

Then, in 2009, IBM made further changes to the schemes through Project Waltz. In particular, the DB sections were closed to future accrual and the link to active members' pensionable salaries broken. At the same time, a new, less generous, early retirement policy was implemented.

The schemes' members argued that, following the 2006 changes, they had expected the schemes to remain open to future accrual for the foreseeable future. Project Waltz therefore breached the duties owed by IBM to the scheme beneficiaries.

The case considered IBM's contractual duty and their 'Imperial' duty* of good faith to employees. The judge found that Project Waltz was in breach of both duties. He also ruled that IBM had breached contractual duty when it consulted with members in a manner which was 'neither open nor transparent'.

The judge also noted that, during the earlier exercises, members had been given the expectation that DB accrual would continue, at least in the short term. In particular it was found that member communications as part of the previous scheme changes 'were not simply statements and communications; they were intended to be, and were, acted upon by the members when they decided whether or not to give up DB accrual.

Whilst the judgement deals with the breach of duties, the practical implications remain unclear until a further hearing is held. In the meantime, employers who are considering changing benefits should do so carefully and in particular should carefully consider any communications with members.

Court of Appeal: Honda

The Court of Appeal has upheld a decision of the High Court that Honda employees should receive a *higher scale of pension benefits* than previously thought, placing additional liabilities of £47m to £70m on the Scheme Funding basis on the Honda UK Pension Scheme. The error stems from the wording of a Deed of Adherence.

High Court: Gleeds

The High Court has ruled that changes to the Gleeds Retirement Benefits Scheme, purportedly made by deeds of amendment since 1990, are not valid because the sponsor *signatures were not witnessed* which means the sponsors of the scheme face up to an additional £45m liability. Further, some employees had not become members of the scheme as had been previously believed.

** Imperial Group Pension Trust Ltd vs Imperial Limited (1991), which said that employers should not act to damage the trust between them and their employees, and that this duty should be taken into consideration when exercising discretion under a pension scheme's rules.*

CPS proposes an end to tax relief

The Centre for Policy Studies (CPS), an independent think tank, has published a report on *Retirement saving incentives: the end of tax relief and a new beginning*. The CPS observes that 'the top 1% of earners receive 30% of all tax relief (costing £8.8 billion)'. In the report, the CPS therefore proposes the scrapping of all tax relief on pension contributions, replacing it with a more redistributive 50p Treasury contribution for each £1 saved, irrespective of the saver's taxpaying status. The Treasury contribution would be limited to £4,000 and would be equivalent to a flat rate of tax relief of 33.3%.

The CPS cites evidence from Denmark that up-front tax relief does not significantly incentivise passive savers to increase their savings. It also proposes that:

- Employers' pension contributions should be taxed as if part of employees' gross income.
- ISAs and pensions should share an annual combined contribution limit for individuals of £30,000.
- The 25% tax-free 'pension commencement lump sum' should be scrapped (with protections put in place for accrued rights).
- The lifetime allowance (LTA) should be scrapped.
- The 10p tax rebate for pension schemes on share dividend income should be reinstated.
- Provided they stay inside the pensions system, individuals should be allowed to bequeath unused pension pots to third parties free of Inheritance Tax.
- Carry-forward of unused annual limits should be permitted for a period of up to ten years.

The CPS report comes shortly after Pensions Minister Steve Webb revealed that he believed tax relief on pensions should be a flat rate for all. The Liberal Democrat minister argued that 'people who get it at 40% get shed loads' of tax relief, adding that: 'If you gave everybody 30% then that spreads it much more evenly.'

2014 Budget update

Following the shake-up of DC pensions announced in March's Budget (see *News on… Pensions – April 2014*), the government has *announced* that people who have taken a tax-free lump sum from their DC pensions will now have 18 months to decide what to do with the remainder of their retirement savings.

Under current rules, retirees have to choose what to do with their remaining pension savings within six months of taking a cash sum, or face a 55% tax charge on the cash sum. However, the government has recognised that this could disadvantage people who wish to wait and access the increased flexibility that should be in place in April 2015.

HM Revenue and Customs (HMRC) has since published *information* for savers who took a lump sum and have not yet decided what to do with the remainder of their pension savings. The HMRC note also explains the options available to retirees who have already arranged an annuity but are able to cancel because they are still within the provider's 'cooling off' period.

HMRC has said it will not introduce rules which would enable savers to cancel an annuity after the provider's cooling off period has elapsed.

The Pension's Regulator (TPR) has published *2014 Budget: update for DC pension schemes*, to help trustees and others understand the impact of the proposals. TPR confirmed it will review its DC code and regulatory guidance in light of the Budget changes.

Finally, the Financial Conduct Authority (FCA) has published new *guidance* for pension providers (for example, insurers, annuity providers and financial advisers) to assist them during the period to April 2015. The FCA is encouraging firms to highlight the budget changes to customers who are making retirement decisions in the coming year to enable them to make informed decisions.

PPF news

PPF Strategic Plan

The Pension Protection Fund (PPF) has published its *plan for the next three years* in which it describes how it will 'continue to develop in size, scale and complexity'.

In its Strategic Plan for 2014 to 2017, the PPF confirms that it remains on course toward its 2030 self-sufficiency funding target. Throughout the coming year the PPF will be reviewing its models for investment, risk and finance operations to 'ensure they remain best in class and appropriate for its growing size and scale'. The PPF will also continue to work towards bringing its member services in-house.

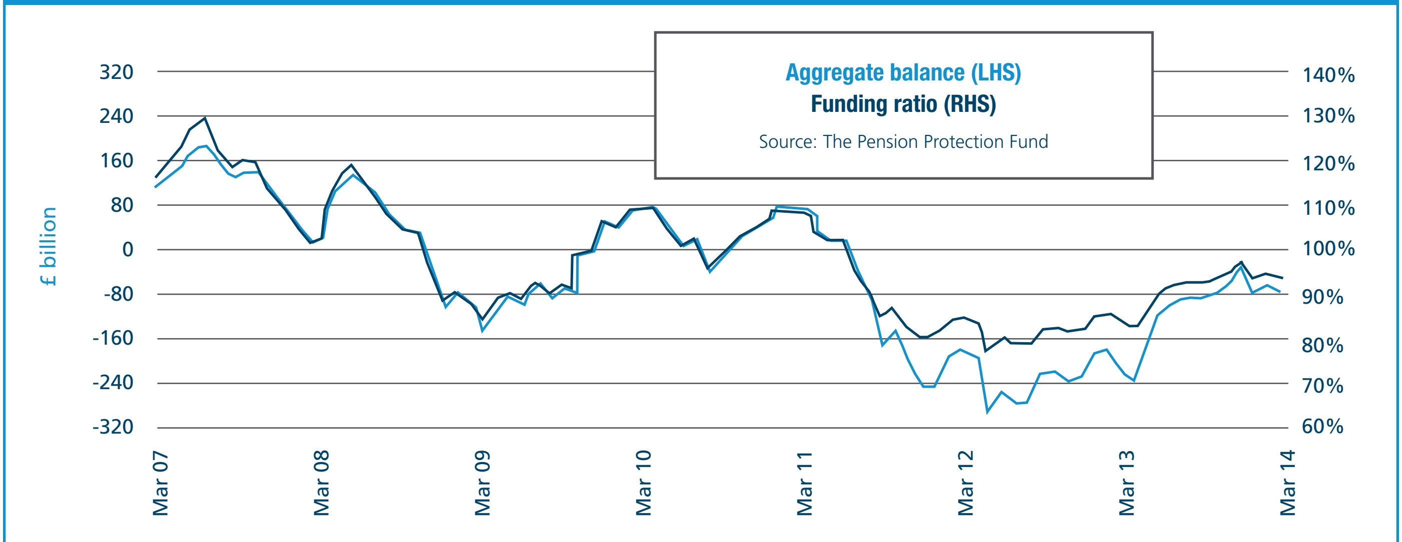
PPF 7800 Index

The *latest update* of the PPF 7800 Index of schemes' funding (on the s179 basis) has been published.

The aggregate deficit of the 6,150 schemes in the index is estimated to have increased over the month to £70.0 billion at the end of March 2014 (there was an aggregate deficit of £61.2 billion at the end of February 2014). The funding ratio fell from 94.9% to 94.3%.

There were 4,046 schemes in deficit and 2,104 schemes in surplus.

ESTIMATED AGGREGATED BALANCE (ASSETS LESS S179 LIABILITIES) AND FUNDING RATIO OF SCHEMES IN THE PPF UNIVERSE



Latest from the DWP

DWP: 'Better workplace pensions: further measures for savers'

The Department for Work and Pensions (DWP) has published a Command Paper '*Better workplace pensions: Further measures for savers*', in which it proposes a comprehensive range of measures designed to 'strengthen governance' and 'improve transparency' with a particular focus on protecting members in default funds.

The quality standards set out in the Command Paper are broadly consistent with The Pensions Regulator's (TPR) *31 DC Quality Features*. Earlier this year, TPR had said that it expects trustees to produce Governance Statements from their 2014/2015 scheme year (see *News on…Pensions: March 2014*). Following on from this, the DWP are proposing that:

- trustees must provide a clear, independently audited Annual Statement that they have met the new minimum governance requirements; and
- new duties are imposed on trustees to consider and report on costs and charges.

TPR's Code of Practice and Guidance will be updated to reflect the new governance standards when these are introduced. The DWP is also consulting on whether it should be a requirement for all trust-based schemes to have a named Chair of Trustees who is accountable for demonstrating how the standards have been met.

Auto-enrolment research

The DWP has released some *preliminary findings* from the Employers' pension provision survey 2013 which show that the opt-out rate among big firms stands at around 9-10%. Following these findings, the DWP has reduced its opt out forecast from around 30% to 15% for the lifetime of auto-enrolment.

Scottish independence analysis

The DWP has published an *analysis* of what Scottish independence would mean for social security, pensions and helping people into work. The analysis suggests that while spending on state pension benefits currently costs around £80 more per working-age person per year in Scotland than in the rest of the UK, this gap could increase to £410 over the next 20 years under the Scottish Government's proposed policy changes.

TPR update

Auto-enrolment section 89 report

TPR has published its first *automatic enrolment section 89 report* which sets out the problems experienced by Dunelm Soft Furnishing Ltd in achieving compliance with its auto-enrolment duties. The report explains the steps taken by TPR, which included a statutory inspection and the serving of an Unpaid Contributions Notice.

TPR is encouraging any employer who is experiencing challenges in meeting their automatic enrolment duties to contact them.

DB pension costs research and comparison tool

TPR has published *pension costs research and a comparison tool* for DB schemes. The tool gives a breakdown of costs based on membership size band and shows that costs per member are almost four times higher in small schemes than in large schemes. TPR's research covers investment, administration and actuarial fees as well as other costs such as fees for legal services, independent trustees and covenant services.

Record keeping review

TPR has published the results of its *review of scheme record-keeping* and, as a result, opened seven case investigations. TPR will be monitoring progress, particularly in relation to conditional data, as part of its annual survey of record-keeping and has made it clear that trustees should not view data cleansing as a one-off exercise.

Summer seminar series 2014

Summer 2014 brings two important changes for pension schemes – the PPF-specific insolvency risk model and TPR's new code of practice on funding. Our forthcoming seminar series will look at both these issues and will help keep you ahead of the game and up to speed on the changing pensions landscape. The seminars are free to attend.

For further details, including booking information, please visit our website:

- *The PPF–specific insolvency risk model – how will it affect your levy?* Bristol, Leeds, London, Amersham and Birmingham: 10-18 June 2014.
- *Getting to grips with the new code of practice on funding – are you up to date?* Amersham, London, Leeds and Birmingham: 8-15 July 2014.

To discuss these issues in more detail please contact your usual Barnett Waddingham consultant or use the following:

info@barnett-waddingham.co.uk | +44 (0) 20 7776 2200 | @bw_llp | /barnettwaddingham