

Current Pensions Issues - Summer 2013

TPR: Annual Funding Statement 2013

In 2012, The Pensions Regulator (TPR) published its first statement on funding, setting out what it expected of trustees and employers undertaking valuations at the time. TPR has now published its "[Defined Benefit Annual Funding Statement 2013](#)", aimed at trustees and employers undertaking valuations with effective dates between 22 September 2012 and 21 September 2013 (Tranche 8).

TPR's [analysis](#) shows that, on average, Tranche 8 schemes can expect to see an increase in funding deficits since their previous valuation and will need to either request increased contributions or make use of flexibilities under the funding framework:

- As a starting point, TPR expects trustees to consider whether the current level of contributions being paid by the sponsoring employer(s) can be maintained.
- Trustees should consider an integrated approach to assessing employer covenant, investment and funding risks. For example, when setting an investment strategy, trustees should take into account the employer's ability to make up any further shortfalls that might arise.
- Trustees may change their valuation assumptions to reflect changes in market conditions and the outlook for future investment returns, but should carefully document any reasons for changes and consider the risks involved.
- Trustees may use different assumptions for investment returns in the Recovery Plan from those used in the valuation of Technical Provisions. TPR comments that this should, however, be consistent with the scheme's overall risk management approach.

TPR is updating its regulatory approach to move away from mechanical triggers (based on, for example, the level of Technical Provisions or length of Recovery Plans) instead focusing on issues such as deterioration in employer covenant strength, the shape of Recovery Plans and the investment performance assumed in Recovery Plans. TPR will also focus its efforts on the schemes it considers pose the greatest risks and will consult in the autumn on its approach.

Following the 2013 Budget announcement that TPR is to be given a new statutory objective (see Pensions Bill 2013 article below), TPR will update its Code of Practice on Funding Defined Benefits later this year. In the meantime TPR has reiterated that, if investment in the business is being prioritised at the expense of affordable deficit repair contributions, it expects this investment to be used to improve the employer's covenant.

HMRC: Lifetime Allowance Protections

The [Finance Act 2013](#) received Royal Assent on 17 July 2013, including legislation reducing the Lifetime Allowance (LTA) from £1.5m to £1.25m and the Annual Allowance (AA) from £50,000 to £40,000 from 6 April 2014 as well as the introduction of Fixed Protection 2014 (FP14) intended for those who think they may be affected by the reduction in the LTA.

The Government has also announced that Individual Protection 2014 (IP14) will be introduced to give individuals greater flexibility in protecting pension savings from LTA tax. Her Majesty's Revenue and Customs (HMRC) [is consulting](#) on the detail and implementation of IP14.

- FP14: Under FP14, savers will retain an LTA of £1.5m, provided they make no new pension savings after 5 April 2014. The application form for FP14 will be available from Monday, 12 August 2013 (although HMRC will not acknowledge any before 1 November 2013). Applications for FP14 must be received by HMRC on or before 5 April 2014.
- IP14: Under IP14, savers will have a "personalised" LTA based on the value of their savings at 5 April 2014 (minimum of £1.25m and up to a maximum of £1.5m). Individuals could continue to make contributions without paying an LTA charge on their pre-2014 savings, but would pay LTA charges on additional savings. It is proposed that savers will have three years from 6 April 2014 to apply.

It is also proposed that individuals be allowed to hold both IP14 and FP14 (or its predecessor Fixed Protection 2012) subject to meeting eligibility conditions. Fixed Protection will take precedence, with protection reverting back to IP14 if fixed protection is lost. Individuals with "Primary Protection" and "Enhanced Protection" will not be able to apply for IP14.

Trustees may wish to flag the need for action with pension scheme members who could be affected – including any deferred members – by the change to the LTA.

Please contact your usual Barnett Waddingham consultant if you would like to discuss this issue in more detail. Alternatively, please contact [Bhargaw Buddhdev](#).

Trustee Training - New London Date

Due to popular demand we have scheduled a further trustee training day on Thursday 21 November 2013 in our London office. To book a place on this course, or our trustee training days in Leeds (17 September) or Bromsgrove (20 November), please visit [our website](#).

Our Services

Barnett Waddingham provides professional services spanning pensions, and life and general insurance.

Our services include:

- Scheme Actuary and associated services to the trustees and employers associated with defined benefit pension schemes.
- Advice in relation to defined contribution schemes.
- Pension accounting for UK and international companies.
- Administration and management services including pensioner payroll, preparation of annual accounts and secretarial services.
- Investment strategy reviews and advice on scheme evolution strategy.
- Management of closed schemes, wind-ups and reconstructions and schemes in PPF assessment.
- Employer risk management through buy-out options, transfer exercises and PPF levy management.
- Advice on group personal pensions, stakeholder schemes and personal accounts.
- Group risk advice including group life assurance, private medical benefits and income protection benefits.
- Advice to individuals and employers on pension provision for executives, including pre-hire, advice upon early termination and tax efficiency in the lead up to retirement.
- Analysis and modelling of mortality and longevity risk for insurance companies, reinsurance companies, investment banks and pension schemes.

We also have a dedicated team that provides a wide range of services to the life assurance and general insurance industries in the UK and overseas including statutory actuarial roles.

Through our associated company, Barnett Waddingham Investments LLP, we provide assistance to individuals in respect of all aspects of their financial wealth management. These services include investment advice together with executive pension counselling and retirement option advice including an annuity bureau.

Barnett Waddingham is also a leader in the provision of self invested personal pensions (SIPPs), small self-administered pension schemes (SSAs), specialist executive pension plans (EPPs) and other retirement arrangements.

Pensions Bill 2013

The [Pensions Bill](#) 2013 primarily focuses on reform of the state pension system and in particular the introduction of the single-tier state pension. There are also a number of important issues relating to private pensions. A summary of the main changes is set out below:

State pension reform

The Basic State Pension and State Second Pension (S2P) will be replaced by a flat-rate state pension, estimated to be worth around £144 a week, from April 2016. Individuals with 35 or more years of National Insurance (NI) contributions will qualify for the full amount. Those with an NI record between 10 and 35 years are expected to receive a proportion of the full amount.

One of the key consequences of the move to a flat-rate pension is that contracting-out of S2P defined benefit (DB) schemes will be abolished from April 2016.

Employers will be given the power to amend their DB schemes' future service pension benefits, without the need for trustee consent, to take into account the loss of contracting-out rebates. An actuary will be required to certify that the proposed amendments meet certain statutory requirements.

The Pensions Bill will also bring forward the increase in State Pension Age (SPA) to 67 by eight years, now taking place between 2026 and 2028, and facilitate future regular reviews of SPA in the light of rising life expectancy.

New Objective for TPR

The Bill introduces a new objective for TPR "to minimise any adverse impact on the sustainable growth of an employer" with a DB scheme. The objective is not intended to apply in any wider context than Scheme Funding, although it remains to be seen how it will work in practice.

TPR does not expect the new objective to change the way employers and trustees approach scheme funding.

Power to ban incentive exercises

The Pensions Bill will give the government the power to ban incentivised transfer exercises at any point within seven years of the legislation coming into force. It is reported that the power is only intended to be used if the industry's voluntary code (see [News On... Current Pensions Issues – Summer 2012](#)) is not followed.

Other changes

- The Department for Work and Pensions (DWP) has confirmed that it will implement a "[pot follows member](#)" system of automatic transfers whereby accrued defined contribution (DC) pension savings of under £10,000 will automatically transfer when an employee changes job. Members will have the right to leave their pension pots in the previous employer's scheme, but the government may in future prescribe standards for automatic transfers.
- Furthermore, schemes will no longer be able to offer refunds of contributions to members who leave DC schemes within two years of joining.
- The Bill also includes power to legislate in relation to administration charges in automatic enrolment schemes.

The Bill is expected to receive Royal Assent in early 2014.

Latest news from The Pensions Regulator and the PPF

Record-keeping

The results of TPR's [latest record-keeping survey](#) have shown that "many schemes are still falling short of the standards The Pensions Regulator has set... despite steady improvements in some areas."

The results also show that the majority of large and medium trust-based schemes are engaged with the measurement of "common data" and over half meet the target for common data overall. However, the survey highlighted that measuring "conditional" data – more detailed data such as contribution history, date of leaving and other items needed to accurately calculate a member's benefit – is less of a priority for schemes.

Scheme Funding

TPR has published an updated [Scheme Funding Analysis](#) for valuations and Recovery Plans of UK DB and hybrid pension schemes. The update is based on “Tranche 6” schemes – those with valuation dates between 22 September 2010 and 21 September 2011.

By 31 March 2013 TPR had received just over 1,500 Recovery Plans in respect of Tranche 6 schemes with around 400 schemes reporting a funding surplus. On average, Tranche 6 schemes held assets covering 95% of their Technical Provisions and Recovery Plans had been extended by around 2 years compared with previous Recovery Plans for these schemes.

Meanwhile, TPR has also [announced changes](#) to their valuation submission acknowledgement letters from June 2013. The letters will now be a simple acknowledgement where TPR has no further queries in respect of the submission, whereas previously they may have included generic comments on aspects such as the assumptions used or employer affordability.

TPR will now only provide feedback following further investigation by a case team. This feedback is intended to be more focused on the scheme's specific issues, reflecting TPR's move away from mechanical triggers. TPR aims to contact schemes within 3 months of a valuation being submitted via its online system (Exchange).

Governance Survey

TPR has published its seventh annual [scheme governance survey](#) regarding standards of governance, administration and trustee knowledge and understanding in occupational pension schemes in the year to March 2013. Key findings include:

- Large schemes and DB schemes are more likely to demonstrate good governance standards than smaller and DC schemes.
- Three in four schemes (75%) have documented their internal controls (up from 68% in 2012).
- 79% of schemes have documented service standards in place and, of these, 82% receive formal reports on the standard of administration at least annually.
- 12% of DC schemes say they have never reviewed their Statement of Investment Principles.

Maintaining contributions - new Codes of Practice

TPR has published a [response](#) to its earlier consultation on two updated Codes of Practice, together with supporting guidance, on reporting late payment of contributions to DC occupational and personal pension schemes

TPR had originally proposed that payment failures should be reported when contributions remain outstanding after 120 days (rather than 90 days) and that members should be notified simultaneously when reporting to TPR (rather than within 30 days as at present). The changes were, however, met with significant opposition during the consultation and so TPR has not incorporated them into the updated versions.

The new codes are expected to come into force in autumn 2013 and a new online system for standardised reporting will be introduced in 2014.

TPR has also published a new [quick guide](#) to paying contributions which sets out information for employers about paying the correct level of contributions to a pension scheme on time. This includes information on how to calculate, deduct and pay contributions.

PPF Strategic Plan 2013/16

The Pension Protection Fund (PPF) has published its [strategic plan](#) for the next three years. The plan outlines the PPF's vision for 2016 as well as setting out updated objectives (which include meeting the funding target of being self-sufficient by 2030, delivering excellent customer service and working within a high calibre framework of risk management).

PPF: Compensation Cap increase

The DWP has revealed that it intends to increase the PPF [Compensation Cap](#) for long-serving members of schemes whose employers enter insolvency. The cap will increase by 3% for each year of service over 20 years, up to a maximum of twice the standard cap.

People who are already in receipt of capped compensation may receive an increase when the relevant legislation is in place, but the increase will not be backdated.

The cost of increasing the Compensation Cap will be met by existing levy payers – the PPF estimates that the change is expected to increase levies by around 4% over the period to 2030.

Trust-based DC: Code of Practice

A [revised version](#) of draft Code of Practice 13 has been released by TPR. The code sets out practical guidance to help trustees to meet the legislative requirements for running occupational trust-based defined contribution (DC) schemes, and is expected to come into force in November 2013. The Regulator will publish associated guidance at the same time.

TPR Corporate Plan 2013/16

TPR has published its latest [corporate plan](#), which sets out its key priorities relating to regulating DB and DC schemes and automatic enrolment.

TPR re-emphasised its focus on internal controls and good administration. TPR will support DB schemes in maintaining or improving funding and will encourage trustees to take an “integrated view” to risk management by considering funding, employer covenant and investment risks together. TPR also intends to develop a compliance and enforcement strategy for DC schemes this year.

News in Brief

EC funding plans dropped

The European Commission (EC) announced that it will proceed with plans for a revised IORP Directive (see [News On... Current Pensions Issues – Spring 2012](#)) without the proposed changes to funding requirements.

The EC will proceed with the other aspects of the review of the Directive in respect of governance and reporting requirements. These requirements are likely to result in a much increased focus on risk management and changes in the way trustee boards work.

Dairy Crest's cheesy funding approach

Dairy Crest has granted a “floating charge” over the sale proceeds of 20 million kilograms of maturing cheese to its pension scheme trustees, to help cover the funding shortfall in the scheme. The scheme had a deficit of around £84m at the end of September 2012. It is estimated that the income from the sale of the cheese could be worth up to £60 million.

Pension Schemes in Takeovers and Mergers

The Code Committee of the Panel on Takeovers & Mergers has published [new rules](#), which came into effect on 20 May 2013, in relation to the DB pension arrangements of publicly listed target companies subject to takeover bids. Under the new rules, the trustees of such schemes will be considered significant stakeholders (in a similar way to existing employees) and will therefore have to be provided with additional information and be able to feed back their opinion on the impact of a takeover on the scheme.

In addition, offer announcements and documentation for bidders will have to contain much more information regarding the likely effects of the offer on the target company's pension schemes.

Supreme Court ruling: Nortel / Lehman

A previous ruling in the Court of Appeal and High Court that a financial support direction (FSD) issued after a company has gone into administration has "super priority" over other creditors, has been overturned. The previous decision had effectively classed FSDs as expenses of the administration which would have to be met before trade creditors claims were considered.

The Supreme Court [has now ruled](#) in relation to the Lehman and Nortel schemes that FSDs should have the same low ranking as the claims of other unsecured creditors.

VAT on investment costs

The Court of Justice of the European Union (CJEU) [has ruled](#) that investment management fees paid by an employer in respect of its pension scheme are business costs, and so the employer may reclaim any VAT it has paid on these costs (provided the costs are not then passed on to the pension fund). It had been argued that an employer should be entitled to recover VAT on investment management costs because there was a "direct and immediate link" between those costs and an employer's general business.

Historically, HMRC policy has been to allow VAT to be recovered on day-to-day management fees but not on investment management fees, which are classed as scheme expenses. The CJEU ruling potentially leaves HMRC open to claims from UK pension scheme sponsors who have paid their schemes' investment management charges. An update on HMRC's approach is expected in the Autumn.

In the meantime, employers may wish to consider lodging a protective claim with HMRC to ensure that VAT paid in the last four years are protected in the case of any future VAT claim.

Trustee Discretion – Hastings Bass

A recent [Supreme Court judgment](#) has clarified the scope of the "Hastings-Bass" principle. This principle relates to circumstances in which the courts can set aside the exercise of a trustee discretion. It had previously been thought that pension scheme trustees could use this rule to unwind the exercise of a discretion where this has had an unintended effect or if the trustees' deliberations were inadequate.

However the judgement ruled that provided that the trustees are acting within their powers, discretions can only be unwound if there has been a breach of fiduciary duty. The judgement also states that it would usually be inappropriate for trustees to seek to set aside their own decisions in this way and the process should instead be initiated by a member or beneficiary.

Save the Date

Pensions Conference 2013

Barnett Waddingham's Annual Pensions Conference will take place on Thursday 7 November 2013 at The Lancaster London Hotel in London. We are delighted that The Rt Hon Lord Lamont of Lerwick, former Chancellor of the Exchequer, will be our keynote speaker.

Further details will be released in due course, if you have any queries or would like to reserve a place, please contact our [Events Team](#). This is a full day conference and is free to attend.

Investment Conferences 2014

Our Annual Investment Outlook Conferences will return again in 2014. Further details will be available soon – in the meantime, you may wish to add either of these dates to your diary:

- 15 January 2014, National Motorcycle Museum, Birmingham
- 22 January 2014, The Lancaster London Hotel, London

Slides from the 2013 event can be found on [our website](#), where you can also find our commentaries on the "[Less-Than-Great Rotation](#)" from bonds to equities and on [property investment in pension schemes](#).

Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail. Alternatively contact us via the following:

@ info@barnett-waddingham.co.uk

+44 (0) 20 7776 2200

Digital version



AUGUST 2013
BW1066

Barnett Waddingham LLP is a body corporate with members to whom we refer as "partners". A list of members can be inspected at the registered office. Barnett Waddingham LLP (OC307678), BW SIPP LLP (OC322417), Barnett Waddingham Investments LLP (OC323081), and Barnett Waddingham Actuaries and Consultants Limited (06498431) are registered in England and Wales with their registered office at Cheapside House, 138 Cheapside, London EC2V 6BW. Barnett Waddingham LLP is authorised and regulated by the Financial Conduct Authority and is licensed by the Institute and Faculty of Actuaries for a range of investment business activities. Barnett Waddingham Investments LLP and BW SIPP LLP are authorised and regulated by the Financial Conduct Authority. Barnett Waddingham Actuaries and Consultants Limited is licensed by the Institute and Faculty of Actuaries in respect of a range of investment business activities.

Amersham | Bromsgrove | Cheltenham | Glasgow | Leeds | Liverpool | London