Hogan Lovells

Pensions monthly update - keeping you on track

September 2012

Pension briefing

HIGHLIGHTS

Hogan Lovells pension group is delighted to send you our news Alerter for September, setting out developments over the last two months.

Our Pension Planner gives a comprehensive overview of legal developments in the previous 12 months and expected future changes.

Record-keeping - upcoming deadline

The Pensions Regulator's deadline of 31 December 2012 for trustees and administrators to meet its record-keeping targets is fast approaching. It expects all schemes to have 100% of new common data (created from June 2010) and 95% of legacy common data (created prior to June 2010) in place by the end of this year. (Common data is information such as National Insurance number, date of birth and address which all schemes are expected to have in place in respect of all members.) The Regulator has issued a reminder, making clear that schemes which anticipate significant difficulties in meeting the targets are expected to approach the Regulator.

Dates for your diary

23 January 2013 – Recent developments in pensions

Our regular informal breakfast seminar aimed at trustees and sponsors of occupational pension schemes and their advisers. Speakers from the Hogan Lovells pension team will review legal developments over the past six months and will explain the practical implications for pension schemes. To pre-book a place please click on the link in the email Alerter.

Please note that this seminar was originally planned for 9 November 2012 and has been postponed.

20 March 2013 - Trustee training

A half-day seminar aimed at trustees with some experience or who have attended our one day introductory course (or similar training). Focusing on the trustee's perspective, we will consider developments in the past six months and will look ahead at what we can expect in the coming year. To pre-book a place please click on the link in the email Alerter.

Recent publications

We are delighted to attach our updated briefing note "Insolvency and restructuring of employers – issues for trustees of defined benefit pension schemes" and a note on basic pension legislation for trustees.

AUTO-ENROLMENT

Earnings thresholds 2013/14

The DWP has issued consultation on proposed auto-enrolment thresholds for 2013/14 as follows:

- £9,205 for the earnings trigger (to align with the PAYE threshold);
- Around £5,720 (projected value) for the lower limit of the qualifying earnings band (to align with the National Insurance Contributions (NICs) lower earnings limit);
- £41,450 for the upper limit of the qualifying earnings band (to align with the NICS upper earnings limit. (Maintaining the current limit of £42,475, or uprating this amount in line with earnings to £42,971, are also being considered).

Pensions Regulator guidance

The Pensions Regulator has issued updated guidance, following the amendment of staging dates and the publication by the DWP of guidance on certifying defined benefit and hybrid schemes. Areas covered by the guidance include: assessing the workforce; applying postponement; processing pension scheme membership outside the auto-enrolment process; processing opt-outs; safeguards for workers; and record-keeping.

FROM THE DWP

Contracting-out: bulk transfers and amending scheme rules

The DWP has issued draft regulations for consultation, intended to:

- clarify the current restrictions on amending contracted-out (and former contracted-out schemes) in response to concerns that the current requirements do not work for former contracted-out schemes;
- allow bulk transfers without consent to be made between schemes with the same sponsoring employer even where one scheme no longer has any active members;
- allow bulk transfers without consent from a contracted-out scheme to former contracted-out schemes;
- allow bulk transfers without consent to schemes established outside the UK but within the European Economic Area. (An unintended consequence of the implementation of the IORP directive was to allow bulk transfers without consent to UK or non-EEA schemes only).

FROM THE TAXMAN

Overseas schemes – age 75 relaxations

Regulations have been finalised which extend the relaxations on payment of benefits after age 75 applicable to registered pension schemes to relevant non-UK schemes. The amendments include allowing: a "drawdown pension" to continue after age 75, flexible drawdown where a minimum income requirement of £20,000pa is met, and payment of the same amount of lump sum after age 75 as would have been permissible before the member reached that age.

FROM THE PENSIONS REGULATOR

Financial support directions and insolvency

The Pensions Regulator has issued a statement on its approach to financial support directions (FSDs) in insolvency situations, following the Court of Appeal decision in 2011 which confirmed that liabilities under an FSD ranked as an expense of an administration. Points to note include:

- The Regulator does not intend deliberately to delay issuing an FSD until after an insolvency event to take advantage of the post-insolvency priority order.
- When assessing what financial support is reasonable, a key consideration will be the amount the scheme would receive under an FSD if the pension trustees ranked as an unsecured creditor (which would be the case if the FSD were issued prior to the recipient's insolvency).
- The Regulator will also consider the return that unsecured creditors would receive had the FSD been issued prior to the insolvency event. The Regulator expects that this will result in a level of support that achieves broad equity between the pension scheme trustees and the recipient's unsecured creditors.

FROM THE OMBUDSMAN

Pension sharing: member should have been aware of his unusual situation

The Deputy Pensions Ombudsman has held that, although providing several estimates of a member's pension entitlement which dealt with his pension sharing order inconsistently (or not at all) was maladministration, the member had not suffered financial loss. In addition, he should have been aware of his particular circumstances in relation to his divorce and pension sharing order and, knowing that at least one of the statements was wrong, should have done more to check the information he was receiving. (*Bore*)

Reference to RPI increases and revaluation was not maladministration

The Deputy Pensions Ombudsman has dismissed a complaint that references in LGPS scheme literature to revaluation in deferment and increases to pensions in payment being by reference to RPI constituted maladministration resulting in financial loss. The DPO noted the following.

- Once the Secretary of State had decided to use CPI for uprating pensions, the Local Government scheme was obliged to use this index and doing so did not constitute maladministration.
- In the LGPS leaflets, it was reasonable to state the practice for uprating pensions at the time and they did not make a promise beyond what the LGPS regulations provided.

The DPO was not convinced that Mr Frost would have acted any differently in his decisions to join the LGPS and to transfer in previous benefits, had he been aware that the index used for uprating pensions might change. The LGPS was a good quality pension scheme and it would be strange for an employee to decline to join it on grounds of uncertainty about the method of uprating. (*Frost*)

Death in service benefits should have been arranged following TUPE transfer

Following a TUPE transfer, the transferee employer failed to make arrangements for death in service benefits before the member's death shortly after the transfer. The Ombudsman held that appropriate death in service benefit arrangements should have been put in place before the member's death. Although the lump sum benefit would presumably have been paid under a discretionary trust, there was no doubt that it would have been paid to his widow. The transferee employer was directed to pay the widow a sum of four times the member's final pensionable salary with simple interest, uplifted to compensate for any tax which might be payable. (*McCurdy*)

Redundancy: no contractual right to enhanced reduction factor

The member was made redundant and entered into a compromise agreement with the employer, accompanied by a letter stating that, if he subsequently sought early retirement, a reduction factor of 3% would apply rather than the cost neutral factor normally applied to deferred members. The principal employer later refused consent on the basis of the 3% reduction factor requested, and agreed to early retirement only on the standard cost neutral basis.

The Deputy Pensions Ombudsman held that the letter regarding the reduction factor did not amount to a contractual

promise as the member had given no consideration. There had been no alternative to redundancy and, had the member not accepted the compromise agreement, he would have received a much lower statutory payment. He had therefore not relied to his detriment on the statement and the principal employer could not be estopped from going back on its word. (*Wallace*)

Misstatement: reasonable reliance on incorrect benefit statement

The Pensions Ombudsman has held that a 9% discrepancy between the member's correct retirement benefits and the incorrect overstatement of his benefits had been critical to his desired standard of living at age 65. Had the benefit statement he relied on been correct, the member would not have left his job when he did. The scheme administrator was directed to pay compensation of £22,430 in respect of the member's loss of earnings in the period in which he would otherwise have continued working plus £1,110 for lost interest on savings that he had used to replace his net earnings. (*Hallard*)

Misstatement: detrimental reliance

In relation to a claim for an ill health pension, the Pensions Ombudsman has held that the member had relied on incorrect information in the scheme booklet to his detriment. Had the member known that the minimum service requirement for receiving a pension from the Civil Service scheme would be met if he transferred in an occupational (but not a personal) pension, he would have transferred in one of his occupational pensions instead of his personal pensions. (*Paffey*)

FROM THE PENSION PROTECTION FUND (PPF)

Entry to the PPF

Regulations came into force in July 2012 to allow the assessment process for entry to the PPF to be simplified, in particular by allowing the PPF to assess a scheme's ability to pay its PPF liabilities by making a funding determination instead of obtaining a section 143 valuation. This power will be used where a scheme is considered significantly overfunded or underfunded. The PPF consulted on altering its entry processes and has issued a consultation response.

Key points are:

- The PPF does not intend to set a rigid policy for deciding which significantly over- or underfunded schemes in an assessment period may use the new funding determination route.
- When updating a valuation (instead of carrying out a s 143 valuation), actuaries will be expected to understate the funding level for an overfunded scheme and overstate the funding level for a scheme which is clearly underfunded.
- The PPF will expect actuaries to certify that the funding level is unlikely to exceed 100% of PPF liabilities for an underfunded scheme and vice versa for an overfunded scheme.

The PPF has also updated its guidance on applying for reconsideration of an application for PPF entry or for closed scheme status.

FROM THE PENSION PROTECTION FUND OMBUDSMAN

PPF levy – guidance on valuation of contingent assets was insufficiently clear

In relation to the risk-based levy for 2009/10, the PPF Board rejected a Type B(ii) (real estate) contingent asset, on the basis that the valuation of the property and the legal opinion provided did not meet the requirements of the PPF Levy Determination relevant for that year. The Deputy PPF Ombudsman held that if the valuation was required to be carried out in a particular manner, it should have been made clear by the guidance or the relevant annex to the Determination. She also expressed concern that the PPF had raised new arguments during the course of her investigations, indicating that not all relevant matters had been considered by the PPF at the appropriate stages.

The Ombudsman directed the PPF board to revoke the earlier decision and replace it with a new decision, taking all relevant matters into account. (*NASUWT Managed Pension Plan*)

FROM THE EU

Tax treatment of dividends infringed EU law

The Advocate General has given her opinion in relation to proceedings against Finland concerning its tax treatment of dividends paid to non-resident pension plans. Under Finnish tax provisions, dividends paid to Finnish and non-resident pension plans are subject to a withholding tax of 19.5% but Finnish pension plans may treat such dividends as a deductible expense, where the dividend income is transferred to reserves.

The Advocate General has held that the differential treatment constituted a restriction on the free movement of capital that was prohibited under Article 63 of the Treaty on the Functioning of the European Union. (*European Commission v Republic of Finland*)

OTHER DEVELOPMENTS

Investment: Kay Review

The final report of the Kay Review of UK Equity Markets and Long-Term Decision Making has been issued. It concludes that short-termism is a problem in UK equity markets and that the principal causes are the decline of trust and the misalignment of incentives throughout the equity investment chain.

Pensions Ombudsman and PPF Ombudsman: corporate and business plan and annual report

The Pensions Ombudsman and the Pension Protection Fund Ombudsman have issued their joint annual report and accounts for 2011/12 plus their corporate and business plan for April 2012 – March 2015. Points to note include:

- The number of long-standing cases has reduced: at 31 March 2012 there were only 5 open cases more than two years old (five years previously there were more than 500 open cases of this age).
- Increases in cases are anticipated in relation to defined contribution arrangements (contribution payments, delayed investment or disinvestment); changes to public sector pensions; automatic enrolment; and incentivised transfers.
- During 2012/13, the jurisdiction of the PPF Ombudsman will extend to complaints about maladministration by the PPF in its capacity as manager of the Financial Assistance Scheme.

This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

KEY HOGAN LOVELLS CONTACTS			
Jane Samsworth	**(Partner)**	**+44 20 7296 2974**	**jane.samsworth@hoganlovells.com**
Katie Banks	**(Partner)**	**+44 20 7296 2545**	**katie.banks@hoganlovells.com**
Duncan Buchanan	**(Partner)**	**+44 20 7296 2323**	**duncan.buchanan@hoganlovells.com**
Claire Southern	**(Partner)**	**+44 20 7296 5316**	**claire.southern@hoganlovells.com**

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