

## Equalisation Issues

There has recently been a lot of coverage in the press about “equalisation issues” for pension schemes, with the Foster Wheeler case (covered in our Winter 2009/10 Newsletter) and the Government’s announcement on GMP equalisation (covered in our Spring 2010 Newsletter) featuring the most prominently.

### Has your scheme been correctly equalised?

There have been several cases recently which have shown that some pension schemes did not in fact correctly equalise benefits when they thought they had, meaning that the Barber window continued to apply for longer than expected. For example, the announcement issued to members regarding equalisation might not have fully complied with the power of amendment in a scheme’s trust deed and rules, meaning that the amendment only actually came into force at a later date when a subsequent deed was executed.

Trustees may therefore wish to ask their legal advisers to investigate whether their scheme has been equalised correctly to avoid any unexpected equalisation costs arising in the future.

Recent cases have also focused on exactly how members’ benefits are calculated, including (for example) whether members who have the right in principle to take part of their pension at age 60 can actually do so and, if not, whether their benefits are treated fairly.

In other cases, because of the way the scheme rules are worded, members who had the right to take some of

### What is “equalisation”?

On 17 May 1990, the European Court of Justice ruled that men and women had to have the same normal retirement age for pension benefits going forward. The case which raised this issue was Barber vs Guardian Royal Exchange. Before this date it had been permissible, and indeed normal practice, for schemes to have retirement ages of 65 for men and 60 for women in line with the state pension.

It took several more years, and subsequent court cases, until the effect of the Barber judgment on the requirements for equal treatment of men and women were clarified (and there is still no established practice for equalising Guaranteed Minimum Pensions (GMPs) – see below). There was therefore a delay in most pension schemes until the benefits were amended to be equal for men and women (although some schemes changed the position for new joiners at an earlier point).

For service between 17 May 1990 and the date of amendment, men and women are entitled to be treated as if their normal retirement age was the same as that of the advantaged sex. This period is often called the “Barber window”.

their pension at age 60 may enjoy the unexpected “windfall” of their entire pension (including the part intended to be payable from age 65) being payable without any reduction from age 60. Again, trustees may wish to consider whether there are any issues for their scheme.

Trustees should satisfy themselves that they have legally robust advice on equalisation, and that their scheme is being administered in accordance with that advice.

### GMP equalisation

The previous government announced in February that it would introduce new legislation to require Guaranteed Minimum Pension (GMP) to be equalised between men and women (see our Spring 2010 Newsletter). There is no timescale yet for this legislation which was scheduled to be drafted “when Parliamentary time allows”. If it proceeds,

this will affect any GMPs earned from 17 May 1990 to 5 April 1997. Angela Eagle, the then Minister of State for Pensions and the Ageing Society, said that schemes should not wait for the new legislation and that trustees should behave as if the requirement to equalise GMPs was already in place.

Although both the Financial Assistance Scheme (FAS) and the Pensions Protection Fund (PPF) have issued some draft guidance on the method to be used for equalising GMPs, these both deal with schemes that are winding up and it is far from clear how an ongoing scheme should equalise GMPs. Trustees may wish to wait until further guidance is issued but, given the minister’s statement, it may be appropriate to check this approach with their legal adviser. In any event, trustees should be aware that it is looking likely that all schemes will need to equalise GMPs in the future, leading to increased pension costs.

# Employer Debt Regulations

## Internal Restructurings

When an employer ceases to participate in a multi-employer pension scheme it must generally pay a debt under section 75 of the Pensions Act 1995. This debt is calculated on the costly "buy-out" basis and reflects the employer's share of any shortfall in the scheme.

This requirement has caused angst in connection with certain corporate transactions, particularly in relation to internal restructuring within a group of associated companies. The regulations have recently been relaxed to deal with this. A debt need not now be triggered where a single exiting employer transfers all its assets and liabilities to a single receiving employer and either:

- the trustees are happy that the receiving employer is as at least as likely as the exiting employer to meet the relevant liabilities and is as least as likely to meet its own liabilities after the restructuring ("the General Easement"); or
- the number of members involved in the transaction is less than 3% of the scheme's membership (or two members if more) and the total accrued pension of members covered by the transaction is not more than £20,000 pa ("the De-Minimis Easement").

Transfer of the pension scheme assets and liabilities must occur within 18 weeks of transfer of the exiting employer's other assets and liabilities.

# 2011: Are you ready?

## A-Day Transitional Arrangements

The Finance Act 2004 introduced a new tax regime for occupational and personal pension schemes. Before "A-Day" (6 April 2006) benefits from and contributions to pension schemes approved by the Inland Revenue were limited. For some, the salary on which benefits and contributions were based was limited to the Earnings Cap.

Transitional arrangements allowed schemes to continue applying these

limits after A-Day without having to change their rules. This meant that scheme sponsors would not face a significant increase in liabilities by virtue of limits disappearing overnight.

The transitional arrangements come to an end on 5 April 2011, when any deemed limits will cease to be effective. Any scheme without explicit benefit limits could potentially face a large increase in its liabilities.



## Refunds of Surplus

Trustees will need to pass a resolution by April 2011 under section 251 of the Pensions Act 2004 to permit payment of surplus to the employer in future, even if scheme rules currently permit refunds of surplus. The resolution gives the trustees the right but not an obligation to make payments to the employer. If no resolution is made before 6 April 2011 the scheme may never be able to refund surplus to a sponsoring employer.

Other considerations, such as the interests of members, should still be taken into account. Indeed, the legislation, as drafted, requires members to be given three months' notice of any resolution and any such action will therefore need to be taken by the first week of 2011 at the latest.

There may also be a more immediate potential effect on employers that account for pensions under International

Accounting Standard IAS 19. Under IAS 19, employers may not need to recognise additional liabilities resulting from an agreed scheme funding plan if they have an unconditional right to any surplus under the scheme rules at some point in the future. This right could disappear if no effective resolution is passed.

Companies should engage with trustees on this issue to determine whether a resolution is appropriate, taking legal advice as necessary.

## STOP PRESS!

We understand that the DWP is reviewing the requirements of section 251. At the time of publication it is unclear what the outcome will be.

# Emergency Budget

On 22 June 2010, Chancellor of the Exchequer George Osborne unveiled the coalition government's "Emergency" Budget, which included several pensions-related measures:

- The Government expressed "concerns" over its predecessor's proposal to restrict tax relief on high earners' pension provision. Existing legislation will be repealed later this year.

An alternative approach suggested is a reduction in the Annual Allowance (the level below which full pension saving attracts maximum tax relief). In order to balance the books, the Annual Allowance would have to fall to between £30,000 and £45,000 (currently it is £255,000). A consultation will follow.

Anti-forestalling arrangements currently in place are expected to remain until April 2011.

- The Government will end the rules requiring compulsory annuitisation for money purchase funds at age 75. A consultation on the detail will be published shortly. Transitional arrangements, set out in the Finance Bill 2010/11, will effectively increase the age of compulsory annuitisation to 77.

- The Government will review the date from which State Pension Age will rise to age 66. This review will be "conducted quickly". The Department for Work and Pensions (DWP) has subsequently issued a call for evidence, asking for information to help them decide how soon the rise to 66 should happen.
- The Government will consult on how it will phase out the default retirement age from 2011.
- The Basic State Pension will rise, from April 2011, in line with the higher of earnings inflation, price inflation or 2.5% pa. The Consumer Prices Index (CPI) will be used as the basis for the inflation measure. Historically CPI has produced a lower measure of inflation than the Retail Prices Index (RPI), the measure used by most occupational pension schemes.
- John Hutton (the former Secretary of State for Work and Pensions) will lead a "fundamental structural review" of public service pension provision by the 2011 Budget.
- The Government is supportive of auto-enrolment and has subsequently launched a 3-month review into "making auto-enrolment work".
- The Government will shortly announce details of a review of private pension reforms.

## Pilots case: Who is an employer?

The recent judgment in the case of the Pilots' National Pension Fund (PNPF) v Geoff Taylor & others may have implications for companies who participate in multi-employer pension arrangements. In particular, the case considered when an employer is deemed to have exited a multi-employer scheme thereby triggering a debt under section 75 of the Pensions Act 1995.

Since April 2008, legislation deems an employer to have exited a scheme if it ceases to employ active members (whilst at least one other employer still has active members). However, before 2008, legislation referred to employing "persons in the description of employment" to which the scheme relates. In the PNPF case, the judge ruled that this includes eligible members as well as actual active members.

Employers who believed that they had properly exited a scheme and settled their debt before April 2008 may still actually be liable for a further debt if any of their employees were subsequently considered eligible to join the scheme. It has also been suggested that the ruling may leave these employers liable for scheme funding commitments.

Employers in multi-employer pension schemes may wish to discuss this ruling with their legal advisers.

## News in Brief

### Inflationary pension increases

The Government has announced that it intends to use the Consumer Prices Index (CPI) rather than the Retail Prices Index (RPI) when calculating the statutory minimum level of inflation-linked pension increases. The change could, depending on the wording in a scheme's rules, reduce benefit costs in the long run, as inflation measured by the CPI is typically lower than RPI inflation.

The announcement follows confirmation that public sector pensions would also increase in line with the CPI. The exact scope of the changes is still uncertain and we await further details, however it is understood that the change will apply to future increases in payment and deferment and that past increases will not be affected.

### Revisions to IAS 19

The International Accounting Standards Board (IASB) has published an exposure draft setting out proposed amendments to the accounting standard IAS 19 in an attempt to increase consistency of pension accounting between companies. If adopted in its draft form many companies may see the pension cost recognised in their profit and loss accounts increase, along with higher pension liabilities on the balance sheet.

Further details can be found in an information sheet on our website.

### DWP: Risk Sharing

The Department for Work and Pensions (DWP) has published an Information Note on Risk Sharing aimed at employers who are considering making changes to their defined benefit pension schemes. The Information Note includes case studies on five different employers' risk and cost sharing arrangements and sets out the type of issues employers will need to bear in mind if considering setting up risk-sharing arrangements - for example in relation to legislative consultation requirements.

# Assessing Employer Support

The Pensions Regulator (tPR) has recently published several documents on the importance of understanding and reviewing employer covenant (the ability and willingness of an employer to stand behind its commitments to its scheme). The Regulator has published:

- a statement, setting out tPR's expectation that trustees should monitor and review employer covenant regularly. TPR expects that trustees should:
  - o ask probing questions of employers, getting professional advice where necessary
  - o assess the covenant objectively, taking into account the scheme's exposure to risk, and
  - o plan for additional support in advance of it being needed.

- draft guidance setting out considerations to take into account when assessing an employer's financial position. The guidance also discusses how to go about deciding whether to appoint a professional covenant assessor and the alternative forms of scheme security (e.g. contingent assets).
- draft guidance on multi-employer schemes, focussing on how and when an employer can exit a scheme, the debts due on exit and the mechanisms for modifying any debt. The guidance also considers the exemptions on internal restructurings (see page 2) and emphasises the need for independent, professional advice when assessing covenant in a multi-employer scheme.

All three documents are available on the Regulator's website at: [www.tpr.gov.uk/strength](http://www.tpr.gov.uk/strength).

## First Contribution Notice

tPR has issued its first contribution notice to the Dutch parent company of Belgian textile group Bonas, ordering it to pay £5 million into its former UK pension scheme.

In 2006, the parent company placed Bonas into a "pre-pack" insolvency, without giving advance warning to the trustees of the pension scheme or tPR. Under the pre-pack agreement, Bonas was to be put

into administration and then immediately sold to another company (in this case another subsidiary). As a result, the parent company apparently intended to be able to walk away from the pension scheme, which entered a PPF assessment period in January 2007.

The parent company is appealing the decision.

## News in Brief

### DC Contracting Out

The Government has confirmed that contracting out on a money purchase basis will be abolished from 6 April 2012. From that date, employees who have contracted out via a Defined Contribution (DC) pension scheme will be automatically reinstated into the State system for future state pension benefits. Information for employers is set out in a factsheet available from the DWP's website.

### Trivial Commutation (GMPs)

In our Winter 2009/10 Newsletter, we noted that GMPs could not be commuted as part of a de-minimis trivial commutation lump sum owing to drafting errors in legislation. These errors have now been corrected.

### PPF Levy

A Pension Protection Fund (PPF) Steering Group has published a paper outlining proposals for the long-term future of the PPF levy. Changes would affect the 2012-13 levy at the earliest, and include a proposal that the calculation of each scheme's levy should be based on its own circumstances, rather than having the PPF set a levy target that is shared among levy-paying schemes.

This bulletin is a summary of some recent developments and not a comprehensive description. Although we try to ensure its accuracy, Barnett Waddingham LLP accepts no liability for any errors or omissions it may contain. Readers should take professional advice in relation to their own circumstances and/or refer to the original source material as appropriate. Barnett Waddingham LLP holds your contact details for their own communication purpose only. We do not disclose these details to third parties. If you would prefer us not to use this information for any purpose other than letting you receive this newsletter, or if you no longer wish to receive newsletters from us, please let us know.

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