MAYER • BROWN

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Bridging pensions and increases to state pension age

Proposed power to amend bridging pension rules to reflect increased SPA

Summary

The Department for Work and Pensions (the **"DWP"**) has published a consultation regarding possible changes to the law on bridging pensions. This follows the changes that have been made to state pension age (**"SPA"**).

Background

For men, SPA is currently 65. For women, SPA is an age between 60 and 65 depending on the woman's date of birth. SPA is being gradually increased for both sexes so that it is 66 by 2020. The Government intends to increase it further to 68 in the future.

If scheme rules allow, a "bridging pension" can be paid where a member retires before SPA. As the member will not be receiving a state pension, the scheme pays an increased pension to make the amount the member receives the same as they would have received had they been receiving the state pension. When the member reaches SPA and the state pension commences, the pension from the scheme is reduced.

Consultation

The consultation looks at whether s68 Pensions Act 1995 should be modified to give trustees the power to amend scheme rules by resolution to change the age until which bridging pensions are paid.

This is because scheme rules often state that bridging pensions are paid up to SPA and the possibility of state pension age increasing may not have been considered when the rules were drafted. As SPA increases, schemes face unexpected costs because bridging pensions have to be paid for longer.

The suggested amendments to s68 would allow trustees (with employer consent and subject to employee consultation) to either:

- freeze SPA at the age the member would have become entitled to a state pension had they been born on 5 May 1950 (i.e. 60 for women and 65 for men); or
- amend the rules so that the bridging pension is paid until the member's actual SPA.

(It was announced in the Budget 2012 that the Finance Bill 2013 would contain legislation making changes to the tax rules on the payment of bridging pensions to reflect the increase to SPA so that paying a bridging pension until SPA would not be an unauthorised payment if the member's SPA was greater than 60 (for women) or 65 (for men).)

Comment

The amendments would mean that trustees can amend their scheme either to protect the scheme against costs associated with a rising SPA or to pay a bridging pension until SPA even if SPA is higher than the age stated in the rules.

Devora Weaver

Record-keeping and data targets: Regulator reminder

Deadline for meeting Regulator data targets is imminent

Summary

The Pensions Regulator (the **"Regulator"**) has issued a timely reminder about the deadline for achieving the required standards for data quality by the end of the year. The Regulator expects schemes to have already taken significant steps to meet these targets.

Background

Back in 2010 the Regulator set two targets for schemes to achieve by the end of 2012: (a) for 100% of common data to be in place for post-June 2010 data, and (b) for 95% of common data to be in place for pre-June 2010 data. Common data is data which all schemes will hold in relation to members, irrespective of the type of scheme e.g. member names, addresses, dates of birth and National Insurance numbers.

Regulator reminder

In September this year, the Regulator issued a reminder about this deadline. The Regulator also published a checklist of specific tasks trustees will need to carry out to meet the targets and some FAQs about common data.

Key points in the checklist include the following:

- The Regulator expects schemes to have already taken significant steps to meet the targets or to approach the Regulator for support if meeting the targets is not possible.
- Checking and correcting data is not a one-off exercise, and trustees should engage with their administrators and put in place processes to monitor the quality of record-keeping on a regular basis.
- The checklist emphasises the potential consequences of incomplete data, such as paying out incorrect benefits and the significant cost implications that may arise.
- The Regulator may investigate and potentially take enforcement action against schemes with severe record-keeping problems, especially if the circumstances indicate a failure to maintain adequate internal controls.

Comment

Melissa Pullen

The Regulator's focus on data targets comes at a time when data security breaches are in the spotlight. The Information Commissioner's Office has recently released figures which reveal that personal data security breaches have increased ten-fold in the last five years, and one-third of these breaches involved sending data to incorrect email or postal addresses. These figures underline how important it is that trustees not only ensure that their scheme records are accurate, but also that scheme data is handled securely and processed in accordance with the requirements of the Data Protection Act 1998.

Maintaining contributions to DC schemes: revised code of practice

Regulator expands code of practice on late contributions

Summary

The Regulator is consulting on changes to its code of practice on reporting late payment of contributions to defined contribution ("**DC**") occupational pension schemes and new accompanying guidance. The consultation period runs until 6 December 2012.

The revised code focuses on maintaining contributions not just on reporting late payments, and includes new sections dealing with monitoring contributions and providing information to members.

Background

Trustees of DC pension schemes are under a statutory duty to report to the Regulator any failure on the part of the employer to pay contributions (whether employer or employee) which is likely to be of material significance to the Regulator.

Consultation

- The revised code of practice includes a new section on monitoring contributions and recovering unpaid contributions. Trustees must obtain sufficient information on contributions from the employer to enable them to reconcile the contributions to be paid under the payment schedule with the amounts actually paid to the scheme. If the employer does not provide this information, trustees should request it.
- The accompanying guidance recommends that where there is a payment failure, at least three attempts to contact the employer to recover the outstanding contributions should be made within 90 days of the due date for payment. At least one contact should be by telephone. An explanation of the cause and circumstances of the payment failure should also be sought and recorded to help the trustees assess whether the failure should be reported.
- The revised code of practice includes a new section requiring trustees to give members certain contributions-related information in a transparent and accessible form so that members can reconcile the contributions made to the scheme with the contributions to which they are entitled.
- The current code of practice states that a payment failure is likely to be of material significance to the Regulator where contributions remain unpaid for more than 90 days. The revised code, however, states that where there is reasonable cause to believe that the employer is unwilling to pay the outstanding contributions, or contributions remain unpaid for more than 120 days, this will be of material significance.

Ian Wright

Comment

Whilst the revised code focuses on the need to reconcile actual payments to the scheme with what is meant to be paid, it does not cover the need to reconcile where those payments are actually invested with where they are meant to be invested. Trustees should ensure that this equally necessary step is also carried out.

Rectification of trust documents: recent cases

Recent cases explore court's approach to rectification

Summary

Where a mistake is identified in a scheme's rules and either the scheme's amendment power or s67 Pensions Act 1995 prevents it from being put right by amendment, it may be possible to rectify the document. Two recent cases have explored the court's approach to granting rectification.

Background

The requirements for rectification are: (1) the parties to the deed or other instrument had a common intention when the instrument was executed; (2) this is established by reference to an objective observer; (3) by mistake, the instrument did not reflect that common intention.

Cases

- *Industrial Acoustics Company Ltd v Crowhurst and Others* - rectification was granted on an unopposed summary judgment application, thus avoiding the expense (and time) of a full trial; and
- *IBM United Kingdom Pensions Trust Ltd v IBM United Kingdom Holdings Ltd and Others* - the application was opposed by the sponsoring employer and the factual matrix was complicated. The High Court granted partial rectification in a lengthy 140 page judgment.

The following points came out of the cases:

- it is necessary to establish the parties' intention, but in the context of rectification of pension scheme trust documents there does not need to be evidence of agreement between the trustee and employer;
- where a mistake is repeated in subsequent deeds, those deeds may be rectified provided the parties intended that the substantive benefits should remain the same;
- it is desirable, but not necessary, to inform members of a rectification application;
- rectification can be granted even if this would breach non-overriding legal requirements which applied when the document was executed (where there is no breach of current requirements).

Comment

Where it is clear that a mistake has been made and the factual matrix is simple, unopposed summary judgment applications may be an attractive way to achieve certainty. The ability to rectify later deeds which inadvertently repeat a mistake is helpful, reflecting the fact that new trust deeds and rules are often only intended to amend certain provisions.

Olivia Mylles

Consultation on 2013/2014 PPF levy

Levy estimate for 2013/2014 shows 15% increase

Summary

In September 2012, the Pension Protection Fund (the **"PPF"**) published a consultation on its levy for 2013/2014. This is the first consultation since the new PPF levy framework came into effect (see our February 2012 Trustee Quarterly Review for more detail). The consultation closed on 2 November 2012.

Consultation

The consultation proposes to set the levy estimate (i.e. the amount which the PPF expects to collect) at £630 million, being a 15% increase on the 2012/2013 levy estimate of £550 million. The increase is largely due to non-recertification of contingent assets and market conditions.

With a view to raising the increased amount, the PPF is proposing to change two components of the levy formula – the scaling factor and the levy multiplier.

Going forward, the PPF proposes to:

- relax slightly their requirements in relation to Type B (property) and Type C (credit/bank guarantee) contingent assets, to recognise the downgrading in bank credit ratings; and
- issue guidance which clarifies their position as to Type A (parent guarantee) contingent assets. (Last year the PPF introduced new requirements as to the strength of guarantors. It seems that some trustees may not have re-certified Type A contingent assets as they were nervous about satisfying those new requirements.)

The PPF has also agreed to extend the deadline for submitting deficit reduction contribution certificates until the last working day in April and sets out a helpful proposed timetable for schemes to submit information to the PPF.

Comment

Beth Brown

Employers and schemes will welcome the PPF's decision not to increase the levy estimate by the full 25% which it would have been entitled to impose. Similarly, the PPF's plan to issue further guidance on the guarantor strength certification requirements for Type A contingent assets and to slightly relax the credit rating requirements for guarantors and custodians of Type B and C contingent assets will be welcomed by schemes holding such assets.

Automatic enrolment finally starts

Automatic enrolment regime comes into force

Summary

The phased implementation of the automatic enrolment regime began on 1 October 2012.

Facts

Automatic enrolment officially began with the UK's largest employers, those employing over 120,000 people, becoming subject to the new duty to enrol their workers into a pension scheme on 1 October. 16 smaller employers accelerated their staging date to 1 October, including the Regulator.

The new regime will be implemented over a five year period with all existing employers being subject to the automatic enrolment duties by 2017.

Comment

Automatic enrolment will only affect trustees if the employer wishes to use their scheme as its automatic enrolment vehicle. As existing schemes may need to be amended to meet fully the automatic enrolment criteria and time may be running out, trustees may wish to ask the employer to confirm its intentions on this if they have not already discussed this with the employer.

Martin Scott

Consultation on changes to the Retail Prices Index

Proposed RPI changes may reduce scheme liabilities

Summary

The Office of National Statistics has begun a formal consultation on options for changing the way that the Retail Prices Index (**"RPI"**) is calculated. Any change could lead to lower pension increases and lower returns for index-linked investments.

Consultation proposals

RPI and the Consumer Prices Index (**"CPI"**) currently use different formulas to calculate average prices. This results in a difference of up to 1% between the two indices and is known as the "formula effect". The consultation paper identifies four different options for reducing the formula effect. These range from making no changes at all, to fully aligning the formulas of averaging prices in RPI with those in CPI.

Where benefits are linked to RPI, changes to the calculation of RPI are likely to reduce future increases to pensions in payment, and therefore decrease overall scheme liabilities.

Recommendations for change will be published in January 2013. The Bank of England will have to be consulted before any change can be made to RPI. If the Bank of England determines that the proposal constitutes a fundamental change that would be materially detrimental to index-linked gilt holders, the agreement of the Chancellor of the Exchequer will be needed. Subject to that, any change to RPI will be published by the Office of National Statistics on 19 March 2013.

Abigail Cohen

Comment

Should the calculation of RPI be amended, trustees of schemes where benefits are linked to RPI may wish to consider notifying members of the likely impact on their benefits to manage their expectations. Where trustees have an RPI hedge against CPI liabilities, they will also need to consider the implications for the assumed investment outperformance.

GMP equalisation: the current state of play

GMP equalisation likely to go ahead

Summary

Despite significant industry criticism, it looks like the DWP will go ahead with its plan to impose a statutory obligation to equalise guaranteed minimum pensions (**"GMPs"**).

Background

As reported in our February 2012 Trustee Quarterly Review, earlier this year the DWP published a consultation on legislative changes which would make it clear that schemes cannot get out of any duty to equalise GMPs accrued in the period between 17 May 1990[1] and 5 April 1997[2] merely on the basis that there may not be an opposite sex comparator with the higher benefit. The proposed changes would effectively impose a statutory obligation on schemes to equalise GMPs. The consultation also included a possible equalisation methodology under which schemes would have to carry out dual male and female calculations on an annual basis for each member, and then pay the higher benefit.

Current position

The consultation closed in April 2012 and met with significant criticism from the pensions industry. However, comments from the Pensions Minister, Steve Webb MP, indicate that the proposed changes will be introduced, although the DWP is looking at ways of minimising the burden on schemes such as trying to make GMP conversion a more viable alternative.

Katherine Dixon

Comment

Trustees may wish to start discussing with their advisers and administrators what action they should take if the proposed changes requiring GMP equalisation are introduced.

1 The date of the *Barber* decision which introduced the requirement to equalise pension benefits.

2 GMP accrual ceased with effect from 6 April 1997.

ECJ hears the *Wheels* VAT case

Final decision in *Wheels* case in sight

Summary

The European Court of Justice (the **"ECJ"**) has finally heard the *Wheels* VAT case and its decision is expected next year.

Background

The ECJ heard the case on 12 September 2012. The case concerns whether pension schemes should pay VAT on their investment management services, and the matter had been referred to the ECJ by the First-Tier (Tax) Tribunal.

ECJ hearing

The pensions press has reported that the European Commission (the **"EC"**) intervened at the ECJ hearing to express its view that schemes should pay VAT. Whilst the EC's view is certainly not determinative, some commentators have expressed the view that it makes it more likely that the ECJ will hold that VAT should be paid. On the other hand, the ECJ is often concerned with a level playing field; it will be reluctant to have some investment management services subject to VAT and others not.

Peter Steiner

The opinion of the Advocate-General will be the first thing that we can expect to hear. This is an opinion and will not bind the ECJ, although the ECJ tends to follow the opinion of the Advocate-General. The ECJ's ruling is expected next year (2013).

Comment

Assuming that they have made protective claims to recover VAT previously paid, trustees do not need to do anything at this time, but may need to take action if the ECJ rules that schemes should not pay VAT.

FATCA: intergovernmental agreement

Registered pension schemes in UK should be exempt from FATCA

Summary

HM Treasury and the US Internal Revenue Service (the "IRS") have signed a intergovernmental agreement which is designed to exempt most UK pension schemes from the Foreign Account Tax Compliance Act ("FATCA").

Background

As reported in our May 2012 Trustee Quarterly Review, earlier this year the IRS published draft guidance on FATCA, a piece of American legislation which could have material implications for the investments of UK pension schemes.

FATCA imposes a 30% withholding tax on US income earned by a non-US "financial institution" unless that institution agrees to give information to the IRS about US citizens and taxpayers who have an interest in it. As FATCA is very widely drafted, it could treat UK pension schemes as financial institutions – and impose the 30% tax on their US investment returns – if any scheme member, or even any dependant of a scheme member, is a US citizen or taxpayer. This would have created real difficulties for schemes with US investments: they may not hold information about which members – let alone their dependants – have US citizenship, and UK data protection rules might have stopped them giving the IRS the information that FATCA required.

Intergovernmental agreement

Whilst the IRS' draft guidance earlier this year would have exempted certain non-US pension plans from FATCA, it was not clear that the wording of the exemption would cover all UK occupational pension schemes.

In September 2012, however, HM Treasury and the IRS signed an intergovernmental agreement on improving international tax compliance and the implementation of FATCA. The intergovernmental agreement seeks to exempt all UK registered pension schemes, and some unregistered schemes, from the scope of FATCA.

Comment

The signing of the intergovernmental agreement is good news. However, schemes with US investments (whether held directly or through a pooled vehicle) may be asked to provide evidence to the managers of those investments that they are entitled to benefit from the exemption.

Jonathan Moody

Upcoming Pensions Group events at Mayer Brown

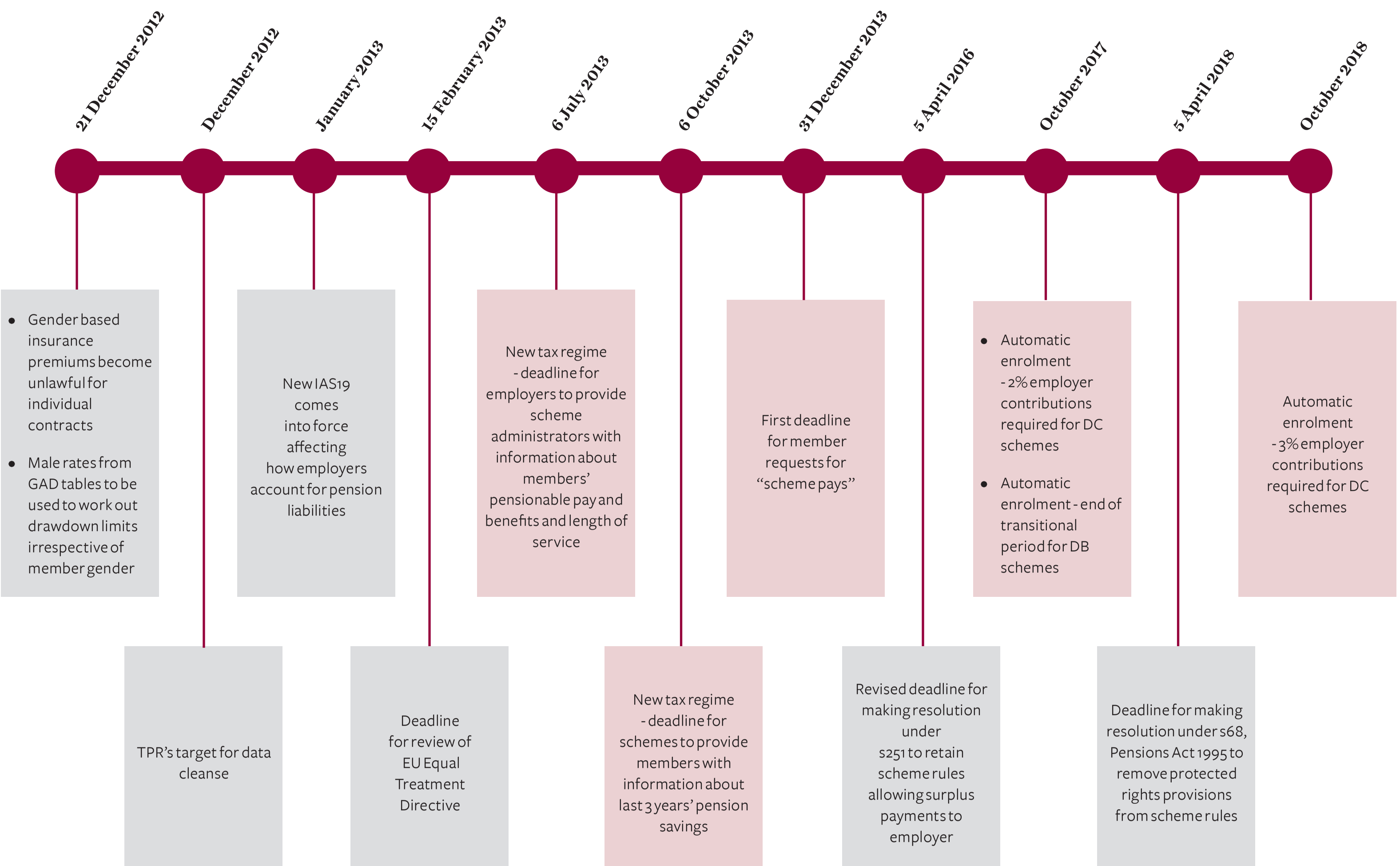
If you are interested in attending any of our events, please contact Katherine Dixon (kdixon@mayerbrown.com) or your usual Mayer Brown contact.

Trustee Foundation Course

- Tuesday 4 December 2012 10.15am – 1.45pm (including lunch)
  201 Bishopsgate, London EC2M 3AF
- Tuesday 26 February 2013 10.15am - 1.45pm (including lunch)
  201 Bishopsgate, London EC2M 3AF

Our foundation course aims to take trustees through the pensions landscape and the key legal principles relating to defined benefit funding and investment matters in a practical and interactive way.

Dates and deadlines



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