SLAUGHTER AND MAY

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Pensions and Employment: Pensions Bulletin

Legal and regulatory developments in pensions

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Forthcoming Events

I. The Watch List

The Watch List is a summary of some potentially important issues for pension schemes which we have identified and where time is running out, with links to more detailed information. New or changed items are in **bold**.

No.	Topic	Deadline	Further information/ action
1.	PPF levy 2015/2016	31st March, 2015 for submission of information and documentation for mitigation	Action plan sent out on 7th January, 2015 available from Lynsey Richards
1.	Information to retiring DC members about the guidance guarantee	6th April, 2015	Pensions Bulletin 14/12
2.	Cap on charges in default fund for auto-enrolment qualifying scheme	6th April, 2015	Pensions Bulletin 14/16
3.	New governance requirements for all occupational DC schemes	6th April, 2015	Pensions Bulletin 14/16
4.	Abolition of refund of contributions for members of occupational schemes with at least 30 days' pensionable service who are just provided with money purchase benefits	1st October, 2015	Pensions Bulletin 14/13
5.	Proposed ban on corporate directors	1st October, 2015 but exception proposed for corporate trustees	Pensions Bulletin 14/18
6.	VAT recovery changes	31st December, 2015	Pensions Bulletin 14/18
7.	Abolition of DB contracting-out: managing additional costs	6th April, 2016	Pensions Bulletin 14/11
8.	Abolition of DB contracting-out: practicalities	6th April, 2016	Pensions Bulletin 14/08
9.	Automatic transfers of DC pots of less than £10,000	1st October, 2016	Pensions Bulletin 14/19
10.	Registration for Individual Protection 2014	Before 6th April, 2017	Pensions Bulletin 14/12

New Law

II. Abolition of DB contracting-out: Time is running out

DB contracting-out will end on 5th April, 2016, in 14 months' time, as a result of the introduction of the single-tier state pension.

Abolition of DB contracting-out will give rise to increased NICs. For employers, this equates to an increase of 3.4% of "band" earnings (earnings between the lower earnings limit and the upper accrual point). For employees, this equates to an increase of 1.4% of band earnings.

In recognition of the additional cost and administrative burdens of the abolition of DB contracting-out on employers, the Government is to give employers power unilaterally to amend scheme rules. Amendments may increase the level of employee contributions or alter the rate of future accrual, but only to reflect the increase in employers' NICs.

Note: Employers will need to comply with the minimum 60 days statutory consultation requirements if they choose to exercise the amendment power.

The legislation is in the Pensions Act 2014. Draft regulations containing details of the proposed statutory override were published on 8th May, 2014 (Pensions Bulletin 14/08) and final versions are expected shortly.

Action point: Employers with current COSRs should start to evaluate the position in good time ahead of the 6th April, 2016 deadline. A checklist of points to consider is available on request.

III. Banking reform: Pensions regulations laid

Draft regulations that prevent ring-fenced banks being responsible for group-wide pension liabilities have been laid before Parliament.

The regulations are being made under the Financial Services (Banking Reform) Act 2013, which provides for the ring-fencing of core banking activities from investment banking.

From 2026, a ring-fenced bank will only be allowed to participate in a non-segregated multi-employer scheme if the other participating employers are its wholly-owned subsidiaries or other ring-fenced banks in the same group (or their wholly-owned subsidiaries).

In the consultation paper accompanying the draft regulations published on 31st July, 2014, the Government suggested that most ring-fenced banks and trustees would use existing scheme amendment powers to implement the necessary changes. But, for schemes with restrictive powers of amendment, an overriding modification power will enable trustees to make amendments by trustee resolution.

The consultation draft also proposed that, if a corporate reorganisation was required to allow a ring-fenced bank to comply with either:

- the main requirements instituting ring-fencing, or
- the pensions related provisions

the bank must apply for clearance from the Pensions Regulator.

This requirement has now been modified so clearance will need to be sought only where the arrangements are likely to be "materially detrimental" to a pension scheme in respect of which the bank is an employer. "Material detriment" is assessed by reference to either "the ability of the relevant pension scheme to meet its pension liabilities" or "the benefits of the members of the relevant pension scheme".

The Government has established an industry working group comprising banks, trustees and Regulators to assist with implementation of the required segregation.

Action point: For noting, unless your scheme is likely to be affected, in which case please get in touch with your usual pensions contact at Slaughter and May.

Tax

IV. Open market option post-5th April, 2015

A. Current position

1. The Finance Act 2004 currently contains a requirement that, in order for an annuity to be a "lifetime annuity" and hence an authorised payment, a member has to have had an opportunity to select the insurance company.
2. So, when a pension scheme is providing a lifetime annuity by purchasing an annuity with an insurer of its choice, the trustee must, prior to purchase, ensure that the member has been given the chance to select an insurer of the member's choice (the "**open market option**").
3. If the trustee fails to do this, the annuity purchased will not fulfil all the statutory

requirements and will result in unauthorised payments and tax charges on the member (and the pension scheme).

4. This requirement remains in force for annuities to which the member **becomes entitled before 6th April, 2015**.

   Comment: Where an annuity is being purchased from an insurer, entitlement to the lifetime annuity arises on the date on which moneys are passed to the insurance company to purchase the annuity. So schemes will need to continue to offer the open market option in retirement packs for members with money purchase benefits for the time being.

B. Post-5th April, 2015 position

This Finance Act 2004 requirement is removed for annuities to which the member becomes **entitled on or after 6th April, 2015**.

Comment (1): The new version of the "open market option" is expected to be a new requirement, to be imposed by amending the Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013. It is expected this will be a requirement to inform members with uncrystallised money purchase benefits who are coming up to retirement that they have a (proposed new) right to transfer those benefits to different pension providers, who may offer different options for using those benefits. Breach of this requirement would result in penalties on schemes rather than members.

Comment (2): Although the amendments to the Disclosure Regulations have yet to be published the requirements are likely to mirror the signposting requirements for personal pension schemes, currently in draft FCA rules published on 27th November, 2014 (Pensions Bulletin 14/18).

Cases

V. Pensions Ombudsman Liberation Cases

A. Overview

1. On 9th January, 2015, the Pensions Regulator published 3 further determinations connected with pension liberation.

2. In all 3 cases, the complainants had wanted to transfer out of personal pension schemes to possible pension liberation schemes, each of which was said to be an "occupational pension scheme" registered with HMRC. The personal pension providers had declined to make the transfers.

3. The 3 cases are similar, and each determination sets out the regulatory, legislative and tax background in detail. They share some analysis and observations in common.

4. In each case, the Ombudsman considered whether the scheme members had a legal right to transfer, either by virtue of statute or under the transferring scheme's own provisions. The Ombudsman found that there was no statutory right to a transfer in any of the cases but that in none of them had the provider carried out the analysis to establish that.

5. However, the Ombudsman acknowledged that schemes and pension providers "find themselves in a highly unenviable position". He said that suspicions about pension liberation may justify delay in the asking of relevant questions. Strictly though, a transfer could only be withheld beyond the statutory period for payment if there was no right to it. If, after enquiry, the trustees or providers concluded there was no right, they should be able to justify that.

6. The cases reflect the tax registration and regulatory guidance applicable at the date the applications to transfer were made. HMRC has changed its registration requirements since then.

B Background

1. A member of an "**occupational pension scheme**" has a statutory right to a CETV if, among other things, he has at least 2 years' pensionable service and is more than 12 months away from his scheme's NRA.

2. An "occupational pension scheme" is a pension scheme established

   - for the purpose of providing benefits to, or in respect of, people with service in employments of a description, and

   - by employers of people in an employment of that description.

3. The CETV must be used to acquire "transfer credits" in another occupational pension scheme". "Transfer credits" are "rights allowed to an earner under the rules of an occupational pension scheme". An "earner" is defined by reference to employment.

3. If trustees receive an application for a CETV, they must effect the transfer within 6 months of the date they receive the application.

C. Determination in relation to Stobie

1. In this case, PO – 3105, the Ombudsman held that a member of a Standard Life Self-Invested Personal Pension Scheme ("**SIPP**") did not have a statutory right to transfer to a scheme which Standard Life suspected to be a pension liberation vehicle.

2. The Ombudsman held that, although the receiving scheme was an "occupational pension scheme", the transfer would not have secured "transfer credits" since the member was not an "earner", in relation to the receiving scheme. Although there is nothing in the legislation that expressly states that the member's status as an "earner" has to be in relation to a scheme employer, the Ombudsman found that it did. "*It would give the reference to "earner" arbitrary consequences if it just means a person with earnings from any source.*"

3. As a consequence, the member's request for a CETV was not for securing transfer credits and so he had no statutory right to it.

4. However, the Ombudsman partially upheld the member's complaint that Standard Life refused to make the transfer, holding that Standard Life had failed properly to consider exercising its discretion under the SIPP's rules to pay a transfer value on written request when there was no statutory right to a CETV.

5. The Ombudsman noted that Standard Life had not followed the recommended steps in the Pensions Regulator's guidance on pension liberation. If it had done so, it would have itself established that the member did not have a statutory right. If there had been a statutory right, Standard Life's suspicions about pension liberation might have justified a delay whilst it asked relevant questions during the statutory period allowed for the transfer. This might have led to the application being withdrawn, potentially the "right" outcome. However, the Ombudsman stressed that a statutory right could not be removed by regulatory or other guidance, nor withheld beyond the statutory period for payment.

6. The Ombudsman was critical of the fact that Standard Life asked the member to demonstrate he had a statutory right. "*Reflecting the different balance of power between the parties, Standard Life needed to satisfy themselves that he did not have a right to transfer*".

7. The Ombudsman directed Standard Life to consider agreeing to a request to pay the transfer value under its discretion and, if it agreed, to

pay the higher of the transfer value backdated to 3 months from the member's original written request, or the current transfer value.

C. Determinations in relation to Mrs. Kenyon (Zurich) and Mrs. Jerrard (Aviva)

1. In these cases (PO – 1837 and PO – 3809 respectively), the Ombudsman found that there was no statutory right to transfer because the intended receiving schemes were not "occupational pension schemes".

2. In **Jerrard**, although the transferee scheme required that the member be an "employee", "employee" was defined so as to include "with the agreement of the Principal Employer, an employee, director or partner of any other firm, company or organisation". The uncertainty created by the breadth of this wording meant that the employments were not "of a description". It should be possible to identify a closed list of classes of employment to which the scheme related. That was not the case here. The transferee scheme was not an "occupational pension scheme".

3. In **Kenyon**, "Employer" was defined as any company of whom the member was an employee or director. The Ombudsman found as a consequence that the scheme did not provide benefits to people with service in "employments of a description": there was no description of employments, and so the scheme was not an "occupational pension scheme".

C. Action points

1. The Ombudsman makes it clear that the burden of proving there is no right to a statutory transfer falls on the transferring scheme.

   Comment: This is an odd conclusion: one would expect that the party seeking to exercise the right would have a duty to demonstrate that they have that right, particularly if the trustees would not otherwise get a valid discharge and would be required to reinstate the member's benefits with no right of recovery.

   Readers with long memories will recall the Hill Kestrel "scam" of the early 1980s. There, the Pensions Ombudsman ruled that transfers to the Hill Kestrel scheme, from which funds were fraudulently withdrawn, constituted maladministration, and the transferring schemes (and ultimately their participating employers) had to pick up the cost of the fraud.

2. Where trustees suspect pensions liberation activity, they should request evidence of "employment" with an "employer" under the receiving scheme to ensure that the transfer will secure "transfer credits".

3. Trustees should also check the registration status of the transferee scheme with HMRC: HMRC will now give confirmation only if it has no information to suggest there is a risk of pension liberation.

4. Please get in touch with your usual pensions contact at Slaughter and May for more information on the precautions trustees should take to ensure they get a good discharge on a transfer.

VI. Benefit changes: Entitlement to fixed rate revaluation: Pensions Ombudsman's determination in relation to Pusinelli

A Overview

1. On 29th November, 2014, the Deputy Pensions Ombudsman held in this case (PO-2591) that P, a deferred member of the Close Brothers Pension Plan (the "**Plan**"), had no right to fixed rate revaluation of his deferred benefits at 5%, either under an alleged oral contract with his employer, Close Brothers, or as a result of a long-standing practice outside the scheme rules.

2. Even if P had had a valid claim against his employer, the Deputy Ombudsman found that

Close Brothers would have been protected by a compromise agreement waiving all claims, including “in relation to accrued pension entitlements”. Although P could not have waived a claim to accrued rights, according to the Deputy Ombudsman a claim for revaluation of deferred pensions was not an accrued right.

Comment: The reasons given by the Deputy Ombudsman for concluding that the right to revaluation at 5% (assuming that P had a right to revaluation at that rate) was not an accrued right appear to be based on a misunderstanding of the High Court decision in **Danks v Qinetiq** in 2012 and should be treated with caution.

B. Facts

1. P was employed by Close Brothers and, since 1988, was a member of the Plan. In 2002 he was made group executive director of Close and received a large pay increase. He and two other senior executives consented to their pensionable salary in the Plan being frozen and to joining a top-up DC scheme for salary over the frozen amount. P later claimed that, in accepting this arrangement, he orally agreed with the finance director that any deferred pension in the Plan (excluding GMP) would be revalued by 5% a year.

2. P left Close in 2008 after entering a compromise agreement in which he waived any employment claims against Close, including “in relation to accrued pension entitlements”.

3. The Plan rules did not provide for any revaluation, but the trustees had routinely increased deferred benefits by 5% a year. The Plan’s 1995 explanatory booklet stated that non-GMP deferred pensions would be revalued by 5%. As part of a review of the Plan, and after consulting Counsel, the trustees and Close agreed to leave past revaluation unchanged, but to apply future increases from 31st July, 2011 on the statutory LPI basis. The scheme rules were amended to reflect this.

4. P complained to the Ombudsman that Close had failed to observe the oral agreement with him. Further, the trustees’ failure to enshrine in the Plan rules the longstanding practice of revaluing deferred pensions at 5% per year was maladministration.

C. Determination

1. The Deputy Ombudsman dismissed P’s complaint. P’s rights under the Plan were set out in the trust deed and rules, which could not be overridden or altered by an agreement between him and Close, by any statement in an explanatory booklet (except in very limited circumstances), or by benefit statements provided in the years before the review.

2. Although the alleged oral agreement could have given P benefits in addition to those under the Plan if all the elements of a contract were present, including clear evidence as to its terms, here there was no written evidence supporting P’s claim, set against the “wealth of evidence” detailing P’s pension arrangements after his promotion in 2002.

3. As the rules were silent on revaluation, statutory revaluation applied in the years prior to their amendment. P did not suffer any loss from any maladministration by the trustees in their past practice before 2011 because he received revaluation above the statutory level during that period.

4. Nor could P claim that the trustees or Close should be estopped from going back on earlier representations, for example in the scheme booklet. The requirements for estoppel (that there should be a clear and unequivocal statement and detrimental reliance on that statement) had not been established.

5. Further, in **Grievson** [2011] EWHC 1367, the High Court had held that "*where the persons claiming to have been deceived by a statement are in effect the same as those who are alleged to have made it, there is no representation which the law can recognise*". P's roles as a trustee and senior board member at the relevant times undermined any argument that it would be unconscionable or unjust for either the trustees or Close to go back on any representations they had made.

6. Rectification required proof of a common intention that a deed of amendment should give effect to the 5% rate of revaluation P was seeking. But whatever the evidence, the Deputy Ombudsman could not properly direct the rules to be rectified as this could adversely affect other members of the Plan who had no opportunity to make representations and who were not bound by her determination.

Points in Practice

VII. Guidance guarantee: Branding and update

A. Overview

1. On 12th January, 2015, HM Treasury launched its "Pension Wise" service, the gateway to the guidance guarantee which takes effect on 6th April, 2015 in relation to DC pension savings.

2. Also on 12th January, 2015, HM Treasury published an update on delivery of the guidance.

B. Update

1. The update includes a chart showing the "customer journey" through the guidance service.

2. It notes the intention that the requirement under the FCA rules (applicable to contract-based personal pension schemes) for signposting to the guidance will apply immediately following Royal Assent to the Pension Schemes Bill, expected to be in early February, 2015.

3. An interim standardised letter is being developed by HM Treasury to be included in retirement packs and other communications to members about accessing pension savings. The update suggests that trust-based schemes will be able to draw on the letter to inform their communications with scheme members approaching retirement.

4. The Government says that the Pensions Regulator will make available to schemes information and materials to support signposting, including agreed templates, and will encourage schemes to make use of these in their customer communications to satisfy the new signposting requirements.

C. Guidance

1. The telephone and face-to-face guidance sessions will initially be designed as a single session per consumer, although this will be kept under review. The service will provide reminders to people who have booked an appointment, and, for telephone guidance, ways of ensuring that the consumer receiving the booked call can be confident that it is from the genuine guidance service. Initial research indicates an optimum length of session of around 45 minutes. The guidance service will provide users with a summary document that will include a record of their options and what action they might choose to take. It will not recommend particular products.

2. The ongoing cost of the service is to be funded by an FCA-administered levy on regulated financial services firms. The initial estimate of the cost in 2015/16 is £35 million but this will be confirmed in March, 2015.

3. Any additional costs over the levy value will, in the first year, be covered by HM Treasury, which will reclaim these from the subsequent year's levy.

D. Next steps

1. Users of the Pension Wise webpages can now register their interest in the service. A public pilot of the online guidance service is planned

to start in February, 2015: the Government says this may be of particular interest to those who have deferred their pension choices since the Budget 2014. The contact centre, through which telephone and face-to-face appointments can be booked, will be available from March.

2. A formal service evaluation will be run later in 2015 to check that the guidance service is working effectively, delivers value for money and meets user needs.

The update is on the Gov.uk website.

The Pension Wise webpages are here

VIII. Are you interested in CDC schemes?

Since 2013, the DWP has been actively exploring the possibility of a "third space" in pensions where:

- employers are not exposed to the risks associated with defined benefit plans,
- but members can expect better outcomes than they would achieve under conventional individual defined contribution arrangements.

In response to industry demand, Part 2 of the Pension Schemes Bill 2015 is devoted to opening up a space for collective benefit schemes (also known as collective defined contribution ("**CDC**") schemes).

In early 2014, we published a "straw man" discussion paper for a possible framework for CDC schemes. The paper, updated in June, 2014 to reflect extensive and constructive feedback from other legal commentators and industry observers, and links to Government papers and other relevant materials, are in a new CDC area of our website.

Two of our partners, Philip Bennett and Sandy Maudgil, have spoken or are due to speak about CDC at a number of conferences, the most recent being the TUC conference "The ABC of CDC" on 21st January, 2015. Details are on our website.

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This Bulletin is prepared by the Pensions and Employment Group of Slaughter and May in London.

We advise on a wide range of pension matters, acting both for corporate sponsors (UK and non-UK) and for trustees. We also advise on a wide range of both contentious and non-contentious employments matters, and generally on employee benefit matters.

Our pensions team is described in the 2015 edition of Chambers as follows:

- "*they employ professional and personable members of staff with a great depth of knowledge and practical know how*", and
- "*their ability to organise a transaction and make sure all things come into action is very, very good and they are incredibly thorough*"

Our recent work includes advising:

- Imperial Chemical Industries Limited and Akzo Nobel N.V. on the de-risking of the ICI Pension Fund by way of a circa £3.6 billion transaction. The transaction, which was announced on 26th March 2014, involved the Trustee of the ICI Pension Fund entering into bulk annuity buy-in policies with Legal & General Assurance Society Limited and Prudential Retirement Income Limited respectively in relation to in aggregate circa £3.6 billion of liabilities of the ICI Pension Fund (which comprise approximately one quarter of the Akzo Nobel pension liabilities). The Legal & General buy-in is the largest ever bulk annuity policy arranged by a pension scheme in the UK
- BBA Aviation plc on the pensions aspects of its disposal of the APPH entities and a "section 75 debt" apportionment arrangement with the trustees of its defined benefit pension scheme, the BBA Income and Protection Plan (the "IPP"), and thereafter on the structuring and implementation of an asset backed funding arrangement with the trustees of the IPP. The asset backed funding arrangement replaces a previously agreed schedule of contributions and is designed to generate an annual income stream of approximately £2.7 million for the pension scheme whilst minimising the risk of scheme over-funding in the future
- Aviva on the de-risking of the Aviva Staff Pension Scheme by way of a circa £5 billion longevity swap transaction involving insurance and re-insurance arrangements. The transaction is the largest of its type to date and allows the defined benefit scheme to re-insure the longevity risk relating to approximately 19,000 of its members (roughly a third of its total longevity risk). Aviva's in-house legal team also advised.
- Premier Foods, on a revised funding arrangement with the group's defined benefit pension schemes as part of Premier Food's refinancing plan. Revisions to the funding arrangements included reduced pension deficit contributions and the granting of additional security to the pension schemes
- Unilever Plc on the creation of an innovative pension funding vehicle under which a unit-linked life policy was established to fund centrally certain overseas unfunded retirement benefit obligations
- General Motors, on the pensions aspects of the sale of Millbrook Proving Ground Limited (the test and engineering technology centre). The sale was dependent on structuring a pensions reorganisation so that the Millbrook Pension Plan and all pension liabilities were retained in the General Motors group
- ConocoPhillips, on complying with its auto-enrolment duties, including analysing how different categories of employees would be provided with pension benefits in compliance with those duties and setting up a new DC pension plan and a new registered life cover pension plan
- Royal Mail on a benefit change exercise which enabled Royal Mail to use some of the c£2bn of assets remaining in the Royal Mail Pension Plan following the 2012 transfer of its pension liabilities to HM Government to fund a £300 million a year gap which would otherwise have opened up between the pension contributions which it could afford and the amount which was required to keep the Plan open for the future accrual of benefits. We had previously advised on the 2012 transfer of approximately £30 billion of Royal Mail's historic pension liabilities to HM Government
- The Trustee of the General Motors UK Retirees Pension Plan, on the surrender in October, 2012 of 2 insurance policies and the purchase of a bulk purchase annuity policy with Rothesay Life. The transaction covered all or substantially all of the Plan's benefit obligations and had an aggregate value of approximately £230 million

If you would like to find out more about our Pensions and Employment Group or require advice on a pensions, employment or employee benefits matters, please contact **Jonathan Fenn** jonathan.fenn@slaughterandmay.com or your usual Slaughter and May adviser.

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