SPC news

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SPC in the Northwest and Yorkshire

The SPC Northwest Committee organised an evening meeting on **19th November** when about 50 people attended a session on the **British Vita case and its implications for funding**. The speakers were **Neil Brougham (Mercer)** and **Anthea Whitton (Pinsent Masons)**. The meeting was hosted by **Pinsent Masons** in Manchester.

The SPC Yorkshire Committee organised an evening meeting on **12th November** at **Hammonds** in Leeds. Around 35 people heard **David Arkenstall (Mercer)** on the subject of **The Changing Buy Out Market**.

Both committees are planning meetings in 2008. To join the mailing list for Northwest meetings, please e-mail stephen.scholefield@pinsentmasons.com. To join the Yorkshire list contact james.patten.2@hewitt.com. ■

SPC London Evening Meetings

The fourth SPC London evening meeting in the 2007-2008 season took place on **December 10th**.

The speakers were **Louise Inward** and **Jonathon Land** from **PricewaterhouseCoopers** and their subject was **Pensions and Restructuring**. For a copy of their handout please click here. ■

Comments on government response to DWP regulatory review

We have commented on the government's response to the DWP deregulatory review.

As a general comment, we agreed with the observation in the consultation paper that:

"The Government does not believe there is a single measure or even a series of measures which would guarantee that employers would continue to provide and even strengthen their existing pension provision."

However, we would also contend that the government, if it really does want to support and encourage good quality pension provision, must not underestimate the importance of its actions in this area.

To quote the recent Pensions Policy Institute paper on '**The changing landscape for private sector defined benefit pension schemes**':

"Although there is not a consensus about the future for DB schemes, there was a general agreement that how the sector evolves will largely depend on how employers and government respond to the underlying cost pressures, the introduction of Personal Accounts, and the possibility for deregulation."

Our comments in full are available by clicking here. ■

Pensions Bill 2007

The Government published the **Pensions Bill 2007** on 5 December 2007.

The main provisions are as follows:-

- Employers will have to make arrangements to automatically enrol employees who are between age 22 and State Pension Age into qualifying work place schemes. Such employees have a right to opt-out.
- The Personal Accounts Delivery Authority will be involved in setting up personal accounts, which could be used for the purposes of auto enrolment. A trustee corporation will be appointed as trustee.
- The above requirements do not apply to employees who are active members of registered pension schemes which satisfy certain requirements:-
  - money purchase schemes:
    - employer contribution of at least 3% of qualifying earnings, with the total amount paid by the employee and the employer being at least 8% of the amount of the employee's qualifying earnings
    - Qualifying earnings is defined as earnings between £5,035 and £33,540 (the personal allowance and upper earnings limit for 06/07 respectively). The figures are subject to increases in earnings and review)
    - In the case of a personal pension, there must be direct payment arrange-ments between the emp-loyee and the employer in respect of payment of employee contributions
  - defined benefit schemes - occupational schemes which are either contracted-out schemes or schemes paying pensions from age 65 of at least 1/120th of Qualifying Earnings in the last 3 tax years preceding the end of pensionable service, for each year of pensionable service (subject to a maximum of 40).
- The Pensions Regulator will oversee compliance with the auto-enrolment requirements.
- The requirement on employers to have a designated stakeholder pension scheme will be removed.

The main provisions not related to personal accounts are:-

- Accrued benefits arising from pensionable service on or after the date the legislation comes into force will be revalued by the rate of inflation (capped at 2.5%). The current cap is 5%.
- The abolition of safeguarded rights, so that shared rights which derive from contracted-out rights on divorce or dissolution of a civil partnership are treated in the same way as other shared rights.
- A mechanism under which PPF compensation will be shared on divorce or dissolution of a civil partnership.

Our initial comments on the bill were as follows:-

- The Bill contains relatively little detail and thus leaves large areas of policy detail open for further consideration. In most respects we welcome this approach because it is the one which is most likely to lead to what we view as a key goal, i.e. a system which starts on the basis of some simple, well thought through principles and only has further features added if these are proved to be necessary.

  We would therefore like to see relatively little detailed amendment of the Bill during its Parliamentary passage.
- The monetary limit on contributions to personal accounts is an important element in ensuring that personal accounts remain focused on their target market of moderate to low earners with little or no current pension provision. This cap should therefore be included in the Bill.
- Our next comment relates to the qualifying earnings clause in the Bill (clause 11). The position here is far from as simple as we would like.

  In respect of both an occupational money purchase scheme and a group personal pension, an employer must pay at least 3% of 'qualifying earnings' in a 'pay reference period' into the scheme, and the total amount of contributions paid by the employer and employee combined must be at least 8%.

  Qualifying earnings in a pay reference period are gross earnings

DWP update on the Proposed Portability Directive

DWP has provided us with several updates on the proposed EU portability Directive, following meetings of the EU's social questions working party on the subject.

You can view the updates by clicking here and here. ■

between £5,035 and £33,540 (limits revalued in line with earnings increases). A pay reference period is 12 months unless a different period is prescribed. This can be more or less than 12 months. If a pay reference period other than 12 months is prescribed the limits of £5,035 and £33,540 are reduced or increased proportionately. Earnings include salary, wages, commission, bonuses and overtime.

Unfortunately the pay reference period has a dual purpose. It is used for determining contributions, as outlined above, and is also used to determine whether an employee meets the conditions for automatic enrolment or re-enrolment. From the Bill's Explanatory Note, this latter purpose appears to be the reason for the power to set pay reference periods of other than 12 months. *"Because of the different types of workers and different pay periods used by employers, there is a need to enable the pay reference period to be tailored to specific worker and payment type. For example, agency workers might require a much shorter calculation period than salaried employees."*

So, although there is power to set a monthly pay reference period for salaried workers, the indication is that this is unlikely. This would therefore suggest that, whether the minimum contribution requirement is met, is tested on a cumulative basis, i.e. against whether, at the end of a pay reference period, the contributions paid by an employer were equal to or more than 3% of gross earnings between £5,035 and £33,540.

We would have expected the wording of the Bill to be clear about whether the contribution test is on a cumulative basis or a month by month basis. **If the contribution test is on a cumulative basis, this causes additional work for employers with regards to employees who have variable earnings.** Employers operate PAYE on a cumulative basis with no upper limit on earnings, and they operate NI on a month by month basis with a monthly limit for 11% of NI-able earnings. Now they may be asked to operate pension contributions on what are essentially NI-able earnings but on a cumulative basis. There does seem to be scope under the Bill for regulations to cater for various circumstances, but experience strongly suggests that this would lead to a set of very detailed regulations, with a high risk of mis-understanding and unintended non-compliance.

We do not know when a pay reference period starts and ends. Is it a scheme year, a tax year, or is it the last 12 months on a rolling basis? It is disappointing that the Bill provides no clarity on this point. Perhaps the problem lies in the fact that 'pay reference period' has a dual purpose.

While some employers do pay pension contributions on more elements of an employee's remuneration than just basic pay, many simply use basic pay. An employer currently paying contributions of 3% (or even 4%) of basic pay could fall foul of the new contribution test. 3% of basic pay for a high earner might be more than 3% of gross band earnings, but 3% of basic pay for a lower earner would probably not be higher than 3% of gross band earnings. The position under the stakeholder designation requirements is more straightforward. An employer only has to contractually provide 3% of basic salary as a GPP contribution. Also, under quite a number of occupational money purchase schemes the employee and employer contribution amounts are fixed at the start of a scheme year, e.g. a contribution of 5% of pensionable pay is payable each month, where pensionable pay is defined as the annual rate of pay on the previous 1 April, or sometimes even gross pay received in the 12 months up to the previous 1 April. Both types could fall foul of the new contribution test. If a pay reference period is a tax year, but a scheme year is different, this too could lead to a breach of the minimum contribution requirement. There are many existing designs of scheme, and a large number of employers will find they have to revisit their scheme design to ensure compliance. This may mean end-of-year top-ups or higher contribution rates; or perhaps even a change of rules so as to match the minimum contribution requirement.

It is important that the government start talking to employers now about how the contribution conditions attaching to personal accounts will work. This should help to nip in the bud further over-complexity such as this.

- There should be an additional explicit principle in clause 62, embodying a duty to achieve delivery of a simple system of personal accounts.
- Personal accounts will be regulated by the Pensions Regulator as an occupational pension scheme and should therefore be subject to the same pensions levies as other occupational money purchase schemes. If personal accounts attract substantial numbers of members in their early days this implies a substantial levy burden on them, at a time when they will have relatively few resources from which to meet them. It is important that there is explicit provision that other schemes paying the levy do not effectively subsidise this element of personal accounts costs in their early days.
- We would strongly urge that the government makes a commitment to conclude its consideration of any measures needed to make risk sharing schemes a realistic option in time for their inclusion in a Pensions Bill in 2008.
- DWP and HMRC must work together to find a workable alternative to the current restrictive rules on trivial commutation. ■

Applying child maintenance deduction from earnings orders to pension schemes

The Child Maintenance and other Payments Bill, currently going through Parliament, includes provisions to extend deduction from earnings orders, in respect of child maintenance, to personal pension arrangements. They can already be applied to occupational schemes. Royal Assent for the Bill is expected in 2008.

The SPC Money Purchase Committee has met DWP to discuss the implications of the legislation.

The government's overall aim is to give better support to couples, who wish to reach their own settlement on child maintenance, but to take a stronger approach to parents who will not meet their child maintenance responsibilities. A major area of emphasis is on parents who are not resident in the household in which the child or children live.

One proposed stronger measure is the extension of deduction from earnings orders, in respect of child maintenance, to personal pension arrangements. DWP believes that only a tiny proportion of its case load (0.1% or approximately 1,000 cases) would be suitable for deductions from earnings orders on personal pension schemes.

DWP does not intend to use its new enforcement powers until it is satisfied that it is properly set up to do so. On current planning this might suggest that new powers would start to be used in mid to late 2009.

DWP recognises that the practicalities of doing so needed to be carefully thought through.

The attraction from DWP's point of view of being able to operate deduction orders is that it avoids the need to involve bailiffs and court procedures in extracting child maintenance.

Under current powers DWP can deduct up to 40% of net monthly income. The percentage is set this high to give it scope to claw back arrears of child maintenance. Generally deduction orders are expressed as fixed monthly amounts, rather than as percentages of earnings. The range of payments which could be required is between £5 and £210 per week.

DWP recognises that it will need to tread very carefully in putting into practice any power to apply deduction orders to personal pensions. It recognises the potential for significant systems changes, both for itself and for schemes/employers/providers to deal with what is expected to be a very small number of cases. DWP recalls how difficult it has been to properly put into practice the superficially simple concept of pension sharing on divorce.

However, it is important to bear in mind that deduction orders would only be contemplated in cases where a parent had already demonstrated an unwillingness to comply with his or her child maintenance duties. DWP's experience is that the most determined non-payers are frequently people who have the means to meet their obligations, but are determined not to do so.

In principle DWP could apply a deduction order to a pension scheme in respect of a maintenance liability, which the individual had incurred perhaps 20 years ago, if all other avenues to obtaining payment had been exhausted.

Following this meeting DWP has asked us for a note on the practical implications of applying child maintenance deduction from earnings orders to pension schemes.

For a copy of the note, please click here. ■

SPC response to DWP consultation on the success of the cross-border activities regulations

We have now responded to DWP's consultation on the success of the UK cross-border regulations 2005 in implementing the cross-border provisions of EU Directive 2003/41, referred to in **SPC News No. 5, 2007**.

The response confirmed our initial view, that (a) relatively little use has been made of the regulations in the UK, (b) they have probably caused some schemes, which used to be cross-border, to cease being so and (c) have provided an unintended incentive to schemes, which are not currently cross-border, to avoid becoming so.

Our full response is available here. ■

PPF levy consultation for 2008/09 - 2010/11 levy years

The Pension Protection Fund has published proposals for how its levy will be calculated for levy years 2008/9 to 2010/11 inclusive. There are two main changes:

- PPF will use the scheme and company data available to it at 31 March 2008 for levy calculations in both 2008/9 and 2009/10.
- The formula for the risk based levy has been adjusted. Some better funded schemes could find their exposure to the levy considerably increased (assuming the employer's insolvency risk has not improved).

The total amount PPF expects to collect will remain stable, at £675 million each year, indexed to increases in earnings. However, the way in which the levy is shared across all schemes will change. To achieve what PPF considers to be a better balance of risk between different eligible schemes, the level of funding, above which no risk based levy is required to be paid, will be increased from 125% to 140%. The maximum levy a scheme is expected to pay will be capped at 1% of section 179 liabilities (compared with 1.25% in 2007/8). The scaling factor is expected to be 1.6. The effect of these three changes, assuming no other changes (that is, assuming the level of underfunding and the insolvency risk posed by the sponsor are the same in 2008/9 as they were in 2007/8) is to re-distribute the levy from less well funded schemes to better funded schemes (those with section 179 funding levels greater than 73%).

Trustees will be expected to submit section 179 information to the Pensions Regulator (TPR), via their scheme return, by 31 March 2008, to enable PPF to calculate the levy. Trustees still have a duty to submit s179 certificates no later than 15 months after the effective date of the s179 valuation. Provided the scheme return is completed and submitted to the Regulator within 15 months of the effective date, this will be sufficient. Otherwise trustees must ensure that the s179 certificate is submitted to PPF within this time. Schemes which have not submitted a section 179 certificate must ensure they do so by 31 March 2008. ■

IFRIC 14

The International Financial Reporting Interpretations Committee has issued Ruling 14 (IFRIC14).

The Ruling considers the interaction of "minimum funding" rules and the maximum amount of surplus, which can be recognised in company accounts (the "surplus cap"). It also considers how a deficit, which has been measured using "minimum funding" rules, can impose an additional liability on the company.

There is uncertainty over how IFRIC14 applies in the UK. It might lead to an increase in liabilities even where the surplus cap does not currently apply.

The Ruling is likely to increase balance sheet liabilities where the "minimum funding" basis is stronger than the IAS 19 basis.

IFRIC 14 is effective for accounting periods beginning on or after 1 January 2008.

Reactions to IFRIC 14 might include:-

- Considering the potential impact on a company's accounting figures.
- Reviewing scheme rules to identify whether there is an "unconditional right" to a refund.
- Considering how the scheme statutory funding process might affect the company, due to IFRIC14.

You can obtain IFRIC 14 by subscription only. For details please click here. ■

Conference discount for SPC members

SPC Members qualify for a 20% discount at the Henry Stewart Annual SSAS briefing on February 21st, 2008. For details, click here.

Please mention SPC membership and quote **"SPC 08"** when booking. ■

General Register Office update on its Disclosure of Death Registration Information Scheme

The General Register Office has sent us an update on its Disclosure of Death Registration Information Scheme, which will probably be of interest to some SPC members and their clients as a source of verification of deaths.

We have placed details of the link at http://www.spc.uk.com/2007/ADC159.pdf ■

About SPC

SPC is the representative body for the providers of advice and services needed to establish and operate occupational and personal pension schemes and related benefit provision. Our Members include accounting firms, solicitors, life offices, investment houses, investment performance measurers, consultants and actuaries, independent trustees and external pension administrators. Slightly more than half the Members are consultants and actuaries. SPC is the only body to focus on the whole range of pension related functions across the whole range of non-State provision, through such a wide spread of providers of advice and services. We have no remit to represent any particular type of provision.

The overwhelming majority of the 500 largest UK pension funds use the services of one or more of SPC's Members. Many thousands of individuals and smaller funds also do so. SPC's growing membership collectively employ some 15,000 people providing pension-related advice and services.

SPC's fundamental aims are:

(a) to draw upon the knowledge and experience of Members, so as to contribute to legislation and other general developments affecting pensions and related benefits, and

(b) to provide Members with services useful to their business.

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