MAY 2015

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INTRODUCTION

Welcome to DLA Piper's Pensions News publication in which we report on developments in pension legislation, guidance and case law, as well as keeping you up to speed on what to look out for in the coming months.

This edition brings you the developments from May 2015 including the following.

- **2015 Parliament:** the appointment of a new Minister for Pensions; and a look ahead to potential pensions issues for the Summer Budget on 8 July.
- **The Pensions Regulator:** scheme funding statistics in relation to schemes with effective valuation dates between 22 September 2012 and 21 September 2013; the annual defined benefit funding statement 2015 which is primarily aimed at those undertaking valuations with effective dates in the period 22 September 2014 to 21 September 2015; and details of the regulatory action taken in a case where a Contribution Notice was issued against an individual who took control of the sponsoring employer and a settlement was reached with two other potential targets.
- **Case law:** a judgment looking at whether an employer breached implied terms in an employee's contract of employment when introducing a cap on pensionable salary by way of an extrinsic contract; further judgments in the IBM case concerning the employer's duty of good faith; the publication of two further determinations by the Pensions Ombudsman in relation to pension liberation; and the publication of a determination about the review of commutation factors.
- **Other News:** the publication by the PPF of FAQs concerning appeals against Experian insolvency scores; and the launch by EIOPA of a pensions stress test and a quantitative assessment on solvency for occupational pension funds.

If you would like to know more about any of the items featured in this edition of Pensions News or how they might affect you, please get in touch with your usual DLA Piper pensions contact or contact Cathryn Everest. Contact details can be found at the end of this newsletter.

ELECTION RESULT

Following the General Election on 7 May which resulted in a majority for the Conservative Party, appointments were made to Government.

Iain Duncan Smith continues as Secretary of State for Work and Pensions and Dr Ros Altmann was appointed as Minister for Pensions in place of Steve Webb. A DWP press release issued on 14 May quotes Dr Altmann as stating:

- that she will take forward work to bring in the new State Pension, help millions more to be enrolled into good quality workplace pension schemes, and safeguard new freedom and choice as to how people access their savings; and
- that her priorities are clear – "*to strengthen British pensions, improve later life incomes, and protect the pensioners of today and tomorrow*".

The State Opening of Parliament and the Queen's Speech followed on 27 May. The only reference to pensions in the speech concerned the State Pension. It was said that measures would be brought forward "*to secure the real value of the basic State Pension*", with the background briefing notes explaining that the triple lock (whereby basic State Pension increases by whichever is the highest of 2.5%, inflation or earnings) will continue to apply for the duration of this Parliament.

In terms of what new measures can be expected from the new Government, it is worth noting what pensions measures were referred to in the Conservative Party manifesto. As well as the retention of the triple lock for State Pension, the manifesto referred to tax relief and the new flexibilities.

- In relation to tax relief, the manifesto contained a proposal to reduce relief on pension contributions for people earning more than £150,000, with the reduction being used to pay for proposed changes to inheritance tax. Whilst not included in the manifesto, it has been reported that the Conservative Party proposed that the annual allowance would reduce to £10,000 once income reaches £210,000, meaning that fifty pence of allowance would be lost for every additional pound of income in a range between £150,000 and £210,000.
- In what appears to be a reference to the April 2015 reforms, the manifesto also stated that the Conservative Party would give people the freedom to invest and spend their pension however they like and let them pass it on tax-free.

In May it was also announced that there will be a Summer Budget on Wednesday 8 July.

It will be interesting to see whether the Summer Budget will announce final details of the proposed changes to tax relief including the date from which they will take effect. As well as the measures set out in the Conservative Party manifesto, changes to the lifetime allowance were announced in the March 2015 Budget and further detail of the transitional protections that will be introduced is awaited.

There are some other measures – most notably Defined Ambition and Collective DC, and automatic transfers of small DC pots – for which the last Parliament introduced the framework in primary legislation, but for which there is much detail still to come. It will therefore be interesting to see how these issues develop over the coming months.

THE PENSIONS REGULATOR

SCHEME FUNDING STATISTICS

In May the Regulator published an update to its annual funding statistics for UK DB and hybrid schemes. The update is based on tranche 8 schemes, that is, those with effective valuation dates falling between 22 September 2012 and 21 September 2013 inclusive.

The underlying data for the figures are sourced from valuations and recovery plans submitted to the Regulator. By January 2015, the Regulator had received over 1,800 valuations with an effective valuation date for tranche 8, and 83% of the schemes submitting these valuations had previously submitted valuations in respect of tranche 5 and tranche 2.

The analysis looks at market conditions, recovery plans, contingent security, funding, discount rates, life expectancies and mortality assumptions, and other financial assumptions.

Key findings include the following.

- Relative to tranche 5, tranche 8 schemes have the same average funding ratio on a technical provisions basis, but have larger deficits on average and receive higher deficit reduction contributions in nominal terms.
- The average ratio of assets to technical provisions for schemes in deficit and surplus is 82.5%. If looking just at schemes in surplus, the average ratio is 109%. If looking just at schemes in deficit, it is 78.7%.
- Tranche 8 recovery plan end dates exceed that of tranche 5 by 2.9 years on average.
- The average recovery plan length for schemes in deficit is 8.5 years, which is unchanged (in absolute terms) relative to tranche 5. The median recovery plan length for tranche 8 schemes is 9 years compared to 8.3 years for tranche 5.
- About one fifth of tranche 8 schemes hold at least one contingent asset which typically, but not always, take the form of guarantees from a sponsor's parent or associated entity. About 13% of schemes have contingent assets that are formally recognised by the PPF and another 7% have contingent assets that are not recognised by the PPF but are reported as additional security in support of funding.

ANNUAL FUNDING STATEMENT

On 22 May the Regulator published its "*Annual defined benefit funding statement*" for 2015 which is relevant to trustees and employers of all DB pension schemes but is primarily aimed at those undertaking valuations with effective dates in the period 22 September 2014 to 21 September 2015 (referred to as "2015 valuations").

The Statement sets out key messages for these schemes and provides the Regulator's views on current market conditions and how trustees and employers can agree appropriate funding plans which protect members' benefits without undermining the sustainable growth of the employer. It also reinforces the key principles outlined in the revised Code of Practice on "*Funding defined benefits*" which came into force in July 2014 and explains how these can be applied in current market conditions.

The Statement has sections on: an integrated approach to managing risks; market conditions and impact on scheme funding; investment returns; setting appropriate recovery plans; managing deficits in the current market conditions; affordability and sustainable growth; recent developments; and what can be expected from the Regulator.
The messages in the Statement include the following.

- The Regulator's analysis suggests that many schemes with 2015 valuations will have larger funding deficits due to the impact of falling interest rates and schemes not being fully hedged against this risk.
- Given the uncertainty about future market conditions, it is important that trustees carefully consider the potential impact on their scheme of different scenarios for investment returns. The Regulator anticipates that most schemes will set funding strategies based on lower expected investment returns than at their last valuation.

- Some schemes will have capacity to take additional risk and should be able to address larger than expected deficits without taking excessive risk through appropriate changes to their funding strategy, such as a modest extension to their recovery plans, a modest increase in deficit repair contributions and/or changing assumptions relating to investment returns.
- The range of options to manage the risks flowing from larger than expected deficits will be more limited for schemes that have more limited capacity to take additional risk. Where there is affordability and the employer can accommodate more contributions without adversely affecting its sustainable growth plans, the Regulator expects trustees to seek higher deficit repair contributions with a view to maintaining the same recovery plan end date.
- Where the employer's affordability is constrained and trustees are faced with a lower level of deficit repair contributions than they think the scheme needs, they should undertake a higher level of due diligence on the employer's affordability (including any sustainable growth plans) and, in particular, understand why previous levels of contributions cannot be maintained if the deficit has increased. Trustees should understand the greater risk a lower level of deficit repair contributions may bring and seek to manage this risk, for example, by obtaining additional security, or structuring the recovery plan differently.

In terms of what employers and trustees can expect from the Regulator, the Statement notes that:

- the Regulator continues to use a broad range of risk indicators to identify those schemes with which it wishes to engage further;
- when the Regulator decides to engage with a scheme, it seeks to understand the trustees' decisions in relation to specific risks and the quality of their decision-making process; and
- the Regulator continues with its approach of selecting a number of schemes for proactive engagement ahead of their valuations being submitted, and has already contacted all the tranche 10 schemes (that is, those undertaking 2015 valuations) selected for this.

It is also worth noting that further guidance is due in the coming months, with the Regulator planning to publish additional practical guidance on an integrated approach to managing risk, covenant assessment and setting an investment strategy to complement the Code of Practice.

In order to provide further context, alongside the Statement, the Regulator published analysis of tranche 8 schemes (for which it provided guidance in the 2013 annual funding statement), and analysis of tranche 10 schemes which highlights the estimated impact of the changes in market conditions since the date of their previous valuations. This tranche 10 analysis provides the evidence base which underpins the messages in the 2015 Statement.

CONTRIBUTION NOTICE

On 28 May the Regulator published a press release announcing that a Contribution Notice for the sum of £382,136 had been issued in relation to the Carrington Wire Defined Benefit Pension Scheme (**"CW Scheme"**). The Regulator also published a report setting out the regulatory action taken in this case and a Determination Notice detailing the decision to issue a Contribution Notice.

Legislation in relation to Contribution Notices

The Regulator can issue a Contribution Notice to certain people if it is of the opinion that they were a party to an act or deliberate failure to act and either the "material detriment test" or the "main purpose test" is met. The Regulator must also consider that it is reasonable to impose the liability on them.

In summary:

- the "material detriment test" will be met if the Regulator is of the opinion that the act or failure has detrimentally affected in a material way the likelihood of accrued scheme benefits being received; and
- the "main purpose test" will be met if the Regulator is of the opinion that the main purpose or one of the main purposes of the act or failure was: (i) to prevent the recovery of the whole or any part of a section 75 debt which was, or might become, due from the employer; or (ii) to prevent such a debt becoming due, to compromise or settle such a debt or to reduce the amount of such a debt which would otherwise become due.

In relation to reasonableness, the Regulator must be of the opinion that it is reasonable to impose liability on the person to pay the sum having regard to: (i) the extent to which it was reasonable for the person to act in the way that they did; and (ii) such other matters as the Regulator considers relevant including, where relevant, a list of matters set out in the legislation.

Background facts

The sole sponsoring employer in relation to the CW Scheme was Carrington Wire Limited (**"CWL"**). In 2006, CWL was acquired by a subsidiary of PAO Severstal (the Russian parent company of the Severstal group). Severstal provided a guarantee to the CW Scheme covering all payments due to it from CWL, but this guarantee would fall away if Severstal ceased to be associated with CWL.

Having begun exploring possible routes to exit its investment in CWL in 2008, in early 2010 Severstal informed the trustees, employees and the Regulator that it had decided to commence a solvent wind-down of CWL. It assured the trustees that it would continue to honour the guarantee following the wind-down.

However, without informing the trustees or the Regulator, Severstal entered into negotiations with RW, the sole director and shareholder of a shell company, for the sale of CWL.

In June 2010 Severstal sold the entire shareholding in CWL to that shell company for £1, with a purported working capital adjustment of £400,000, the majority of which was received by RW personally. The trustees were not informed of the sale until it had completed. The sale meant that the Scheme lost the benefit of the guarantee and became solely reliant on CWL, which Severstal had already wound down.

On 30 November 2012 a warning notice was issued seeking the imposition of Contribution Notices on PAO Severstal, its subsidiary, and RW.

Settlement in relation to two targets

An oral hearing was scheduled for January 2015 but in advance of it, a settlement was reached with PAO Severstal and its subsidiary. Under the settlement, these targets would pay £8.5 million to the CW Scheme and the Regulator would withdraw the case from the Determinations Panel as far as it related to them.

Proceedings in relation to RW

A hearing in relation to RW was held on 11 March 2015 and, following that, the Determinations Panel decided that a Contribution Notice should be issued to him in the sum of £382,136 which is equal to the part of the purported working capital adjustment which RW personally received.

The Determinations Panel was satisfied that both the "material detriment test" and the "main purpose test" were met in this case. In addition, the Panel considered that it was reasonable to impose the liability to pay the sum in the Contribution Notice on RW, with its reasons for this including the following.

- RW's high degree of involvement in the events that took place – it was noted that he was "*pivotal*" to the events.

- It was not reasonable for RW to act in the way he did. For example, he knew that his offer to purchase CWL was not acceptable to the trustees, and he knew that the actions ran the risk of causing the Regulator to seek a Contribution Notice but he was prepared to take that risk.
- The personal benefit RW received as a result of the working capital adjustment.

Regulator's comments on the case

In its report on this case, the Regulator sets out some points of particular note in the Determination Notice.

- The Panel concluded that the "main purpose test" extends to acts which prevent recovery under a guarantee, including situations where the acts take place prior to liability under the guarantee being established.
- The "material detriment test" was met because of the effect of the acts on the "scheme obligations" under the guarantee.
- In relation to whether it was reasonable to impose the liability on RW having regard to his financial circumstances, it was argued that because RW's net asset position is in the order of £52,000, it would not be reasonable. On this issue, the Panel made the following points about the consideration of "financial circumstances".
  - The "financial circumstances" are not limited to the target's current financial worth but also include consideration of how the target has ended up in his current financial position. This includes taking into account monies the person has received and how they have been used. In this case, the Determinations Panel concluded that the fact that RW had spent the £382,136 for his own purposes did not diminish the reasonableness of issuing a Contribution Notice.
  - It was concluded that a distinction is to be drawn between the issue of a Contribution Notice and its enforcement. The Panel stated that questions about the ability to recover the amount and the costs and proportionality of doing so are far less relevant to the decision to issue a Contribution Notice than to decisions about whether and how it should be enforced.

Ultimately the regulatory action in this case will not lead to recovery of an amount in excess of the PPF deficit, so the CW Scheme will transfer to the PPF. However, the Regulator commented in its report that the regulatory action has significantly reduced the PPF's exposure in relation to the CW Scheme.

As well as noting that the case highlights the circumstances in which Contribution Notices may be pursued and provides useful clarity on the interpretation of the statutory tests, the Regulator states in its report that where appropriate it is willing to consider settlement proposals from targets and sets out factors it will consider in assessing proposals.

Cases in which actions have been taken that will result in the Regulator exercising its powers will be relatively unusual, but it is nevertheless interesting to see the approach that the Regulator takes to the exercise of its powers to issue Contribution Notices and to settlements.

SECTION 89 REPORT – SETTLEMENT

In April 2010 the Determinations Panel of the Regulator determined to issue Contribution Notices to two targets (Mr Desmond and Mr Gordon) for a total of £1 million in respect of the Desmond & Sons Ltd 1975 Pension and Life Assurance Scheme (**"Desmond Scheme"**).

The relevant act in relation to the Contribution Notice concerned the Desmond Scheme employer entering into Members' Voluntary Liquidation in June 2004 which

resulted in it being treated as insolvent for the purposes of calculating the employer debt payable (even though it was fully solvent) at a time when the debt was calculated using the Minimum Funding Requirement basis rather than the buy-out basis.

The determination was the subject of references to the Upper Tribunal by:

- Mr Desmond and Mr Gordon, who argued that no Contribution Notice should be issued to them; and
- the trustee of the Scheme, who argued that a Contribution Notice should be issued to one additional target (Mrs Desmond) and that the sum sought in the Contribution Notices should be higher.

The Upper Tribunal proceedings were stayed while a number of legal challenges made by the targets were dealt with. The stay was lifted on 8 November 2013 and the hearing of the references was due to take place in May 2015.

However, in May 2015 the Regulator issued a report stating that, in advance of the hearing, an agreement was reached between the trustee and Mr and Mrs Desmond and Mr Gordon under which a payment will be made by Mr Desmond to the Desmond Scheme. The Regulator will therefore not be issuing Contribution Notices to Mr or Mrs Desmond or Mr Gordon.

The report notes that the payment being made to the Desmond Scheme will assist the Financial Assistance Scheme in providing member benefits. The report explains that the references have been settled on terms of no admissions of liability, and as a result of the settlement, the allegations made by all parties in the proceedings are not maintained. However, it reports that the remaining terms of the agreement are confidential to the parties.

CASE LAW

DUTY OF TRUST AND CONFIDENCE AND GOOD FAITH

Background

In 2010 as part of a project to reform the BBC's pension arrangements, members were given a choice of: (i) remaining in one of the two final salary sections or the career average sections of the BBC Pension Scheme with a 1% cap on increases in pensionable salary imposed by way of extrinsic contract; (ii) joining a new career average section with no cap; or (iii) opting out of the Scheme altogether and joining a new DC scheme.

The changes have been subject to challenge on various grounds but this case concerns the claim of an employee (Mr Bradbury, referred to in this article as **"JB"**) that the BBC's conduct in seeking to impose the cap on increases to pensionable salary through the mechanism of his pay award was in breach of the implied term of trust and confidence and/or the implied term of good faith contained in his contract of employment (the **"Implied Duties"**).

In December 2013, the Pensions Ombudsman (**"PO"**) issued a determination on this point concluding that, in light of the scheme deficit, the BBC's potential future liability, its resources and overall obligations and the steps taken by it to address the problems it faced in relation to the scheme, the BBC did not breach the Implied Duties in seeking to impose the cap. This latest judgment relates to JB's appeal against the December 2013 decision of the PO.

May 2015 judgment

Was it possible to impose the cap by contractual means?

The High Court first looked at whether, as a matter of principle, the BBC was in breach of its Implied Duties in seeking to impose the cap, that is, whether the very structure of the proposals gave rise to improper coercion to accept the cap.

Before the High Court, it was argued that JB had certain Reasonable Expectations which had been disappointed, including that if the BBC wished to amend the pension scheme rules it would do so by following the procedure set out in the rules. In this context, a Reasonable Expectation means an expectation as to what will happen in future that has been engendered by the employer's actions which gives employees a positive reason to believe that things *will* take a certain course. The High Court concluded that it was not open to JB to make an argument in relation to Reasonable Expectations because it had been raised too late, and in any event, thought that the evidence before the PO did not establish Reasonable Expectations.

In the absence of Reasonable Expectations, the High Court decided that the PO was correct that presenting JB with hard choices did not of itself amount to improper coercion, and it was open to the BBC to seek to impose the cap, provided it was done properly.

Was the process defective?

The High Court therefore went on to consider whether the cap was introduced properly or whether the way in which it was introduced gave rise to a breach of the Implied Duties.

Three factors had been raised by JB on this point – that the BBC acted with an alleged collateral purpose of achieving a more "agile" workforce, that there was age discrimination, and that the consultation was inadequate. Considering each factor, the High Court concluded that:

- it is clear that what the BBC did was clearly, and primarily, a response to the deficit, and the BBC was entitled to choose the course it did to address this rather than an alternative course of action suggested by JB;
- it is a "*hopeless suggestion*" that, by virtue of the alleged age discrimination alone, the BBC was in breach of the Implied Duties owed to JB (the alleged discrimination was that the cap discriminates indirectly against younger members, although it was common ground that JB is not in the disadvantaged class); and
- the PO was entitled to reach the conclusion that the consultation as carried out did not, of itself, give rise to a breach, albeit that the PO's reasoning was limited.

Having decided that the PO reached conclusions that he was entitled to reach on each of these factors, the High Court went on to look at the position when the factors are taken together.

Whilst the High Court judge acknowledged that the duty of trust and confidence can be breached by an employer's actions cumulatively, he stated that he found it hard to envisage a case where a breach of duty could arise out of an accumulation of acts where it was necessary to rely on an act which was not of a type which could in principle give rise to a breach by itself.

In this case the High Court stated that the three factors relied on – collateral purpose, age discrimination and consultation – are disparate, with no obvious connection between them, and it would require a very strong case for a number of disparate objections to give rise, when taken together, to a breach of the Implied Duties when none of the objections by itself gives rise to such a breach.

The High Court disagreed with JB's argument that the PO had failed to consider the question of breach in the round in addition to looking at each of the factors. The High Court also held that the only overall conclusion the PO could have reached in light of his decisions on each of the factors was that there was **no** breach of the Implied Duties, and that a conclusion that there **was** a breach would have been one which no reasonable PO could have reached. The appeal was therefore dismissed.

This case is likely to be of comfort to employers who wish to cap pensionable salary by the use of extrinsic contracts. It demonstrates that it is possible to make the changes in this way and that, provided the process is conducted properly, the employer will not be in breach of its Implied Duties.

IBM – FURTHER JUDGMENTS

Background

In the April 2014 edition of Pensions News we reported on a case about whether IBM had breached its duty of good faith in making changes in respect of certain of its pension plans (**"Plans"**) including closure to future accrual, procuring that members enter into non-pensionability agreements in 2009, and changes to the early retirement policy. In summary, the court held that no reasonable employer in the position of IBM in 2009 would have adopted the proposals in the form that they took and, viewed as a whole, the changes gave rise to a breach of the *Imperial* duty (the term often used to refer to the duty of good faith in a pensions context) and the contractual duty of trust and confidence.

A judgment about the remedies available to members in relation to these breaches followed in February 2015 (as reported in the March 2015 edition of Pension News). The February 2015 judgment was subject to a caveat in relation to certain matters of contractual liability, and also noted that there were a number of outstanding issues that would be the subject of a further hearing in late April.

Three further judgments were issued in this case in May. One dealt with the question of the conduct of matters on which permission to appeal is being sought, the other two addressed the following matters.

The relevant IBM entity

The caveat to the February 2015 judgment was that it was stated to be provisional insofar as it relates to certain matters of contractual liability. The caveat was included because Counsel for IBM had raised the question of which IBM entity has the contractual duty to members, given that the relevant members of the Plans were employed by IBM United Kingdom Limited (**"UKL"**) and not by IBM United Kingdom Holdings Limited (**"Holdings"**).

In summary, it was concluded that both the April 2014 and February 2015 judgments should, in principle, be corrected with the effect that UKL is to be substituted for Holdings as the party contractually liable, save in relation to the Exclusion Notices by which the Plans were closed to future accrual, the early retirement window and the change in early retirement policy where the only breach is by Holdings of its *Imperial* duty. The corrections are "in principle" because the judge stated that a full textual rewriting of the judgments would be onerous and he would not be able to complete it within any sensible timescale.

The early retirement policy

Among the Plan changes that were the subject of challenge was the introduction of a new early retirement policy on 6 April 2010 whereby IBM would only consent to early retirement on terms more favourable than cost-neutral in exceptional circumstances.

In short, it was concluded that the old policy in fact applies to all members who left service prior to 31 March 2014 and does so in relation to all of their pension, but after 31 March 2014 IBM was entitled to adopt a new policy. The questions of whether IBM needs to give notice before adopting a new policy and, if so, the duration of notice required, were left to the hearing in April and on 19 May judgment was given on these points.

The court considered the question of whether notice is required as a general matter, and its conclusions included the following.

- There is no implied restriction on the exercise of the discretion to determine an early retirement policy to the effect that it can only be exercised upon giving some reasonable period of notice. Rather, the exercise of the discretion could be challenged only on the basis of a breach of the *Imperial* duty, but that duty does not result in any requirement to give notice in this case.
- However, an announcement must be made informing members of the relevant change.
- In relation to the facts of the IBM case, such an announcement has not yet been made. The judge was not satisfied that an email that purported to change the policy with effect from April 2010 amounted to an appropriate announcement. Neither was he satisfied that the service of the skeleton argument for the hearing to which the February 2015 judgment related, or the hearing itself, amounted to an appropriate announcement. (In addition, the judge stated that if he is wrong and a period of notice **is** required, neither do these actions amount to sufficient notice.) In the absence of a satisfactory announcement having been given, the current position is that no new early retirement policy has yet been validly introduced. However, the judge acknowledged that what the pre-existing policy actually is will depend on the outcome of any appeal about the question of whether there was a breach of duty in purporting to change the policy in 2010.

Whilst we would expect employers to welcome the conclusion that notice does not have to be given before adopting a new early retirement policy, they should nevertheless note the conclusion that the change must be announced.

PENSION LIBERATION

In May two further determinations were issued by the Pensions Ombudsman (**"PO"**) in relation to pension liberation.

Alleged failure to complete sufficient checks

The Applicant in this case contacted his personal pension provider on 11 January 2013 to request a transfer to the Capita Oak Pension Scheme. The provider sent the transfer paperwork to the Applicant and a warning that

they strongly recommended that he seek financial advice before making any decisions. The transfer was processed on 19 March 2013.

The Applicant argues that the provider made this transfer without completing sufficient checks on the receiving scheme and he is now unable to locate his pension. As redress, he wants the provider to reimburse him the amount transferred plus the additional funds which would have accrued had his pension remained invested with them.

The complaint was not upheld with the PO stating that he did not consider that there was an administrative failure by the provider in complying with the transfer request.

In his conclusions, the PO noted that the transfer application appeared to comply with the requirements for a statutory transfer and that the Pensions Regulator did not issue guidance to providers about pension liberation until February 2013 (that is, after the Applicant made his transfer request but before the transfer was completed). The PO thought that it would be reasonable to expect that some time would be required for procedures to be updated and new literature prepared to reflect the guidance. He therefore did not regard it as maladministration that the provider had not (at the relevant time) yet amended its procedures.

As with other cases on pension liberation, the PO once again took the approach that the Applicant could not be deprived of a statutory right to transfer by regulatory or other guidance.

The outcome here is similar to some cases determined in April (reported in our Pensions Alert dated 30 April 2015) where the transfers were made before the Regulator issued its guidance in February 2013. On the question of levels of due diligence, this case provides some comfort for trustees in relation to historic cases in that the PO effectively concluded that it is reasonable for providers to take some time to update their processes. However, it is not clear exactly how long they could reasonably take to do so and it will be interesting to see whether any future cases look at different timescales and the impact this has on the outcome. In any event, if a scheme proceeded with a transfer now without flagging the risk of pension liberation, the outcome may well be different.

Member seeking further transfer

The other case concerns a member who transferred two pensions to the Henley Retirement Benefit Scheme (**"Henley Scheme"**) in February 2013. The complaint does not relate to those transfers, but to the Applicant's inability to now get the money out of the Henley Scheme.

The Applicant has told the Ombudsman Service that he has never seen the Henley Scheme's governing documents. The Respondent to the complaint (Omni Trustees Ltd) has not given any detailed response to enquiries from the Ombudsman Service.

The PO noted that in the information provided to the Applicant, the Henley Scheme is referred to as an occupational DC scheme, and correspondence from Omni is addressed either to the Applicant by name or 'Member'. On Omni's own account, the Applicant is therefore a member of an occupational scheme.

Whilst the requests made by the Applicant to transfer out of the Henley Scheme did not strictly meet the requirements for statutory transfer requests, the PO concluded that it was unquestionably maladministration that Omni did not respond and it was the lack of response that stopped the process.

The PO therefore directed that, within 14 days of the Applicant requesting a transfer value to a named scheme that meets the prescribed requirements under the legislation and is prepared to accept it, Omni are to pay the transfer value to that arrangement.

COMMUTATION FACTORS

For some time now, a number of complaints against the Government Actuary's Department (GAD) have been before the Pensions Ombudsman Service concerning the review of commutation factors in the firefighters and police pension schemes. The consideration of the complaints was placed on hold when, in 2012, GAD challenged the Ombudsman's jurisdiction to consider complaints against it. The High Court, and subsequently, in 2013, the Court of Appeal, held that the PO has the relevant jurisdiction.

The PO proceeded to consider a lead complaint and on 15 May 2015 issued a determination in that case which concerns the Firefighters' Pension Scheme and an Applicant who was employed in Scotland and retired in 2005. However, the PO notes that firefighters are similarly affected by the issue, whether they retired from employment in England, Northern Ireland, Scotland or Wales, and that a connected issue arises in relation to the Police Pension Scheme.

Whilst the outcome of this case is specific to the role of GAD and the drafting of the relevant rules, it serves as a reminder of the importance of properly adhering to scheme rules about commutation factors.

Facts

The Applicant retired in November 2005 and chose to commute the maximum amount of pension. The calculation was completed on the basis of commutation tables which had been in use since 1998.

The relevant scheme rules (set out in regulations) provide that a person may commute a portion of their pension for a lump sum, and that the "*lump sum is the actuarial equivalent of the commuted portion at the date of retirement, calculated from tables prepared by the Government Actuary*".

Until the early 1990s GAD instigated the review of the commutation tables. However, the relationship between GAD and other government departments changed when new funding arrangements were introduced – they became clients of GAD, commissioning work and paying fees. From the early 1990s until 2009 GAD wrongly acted on the basis that it was the responsibility of the relevant department to commission reviews and instigate revisions of the tables. Following the 1998 review, the next review by GAD took place in 2006.

A High Court judgment from 2009 found that in the Police Pension Scheme, GAD had a statutory duty to produce tables that resulted in actuarial equivalence and to review those tables on a periodic basis as appropriate. However, the 2009 judgment did not deal with periods before 2006. The Applicant in this case complains that GAD failed to review the commutation tables from 1998 to 2006 and that, if they had been updated, the lump sum he received would have been greater.

PO's conclusions

The PO noted that the pure dispute of law at the heart of this matter had already been decided by the 2009 judgment. He went on to state that the complaint under consideration in this determination follows the 2009 finding. In this case, the PO looked at the question of whether there had been maladministration by GAD.

The PO stated that GAD changed from instigating reviews to waiting to be asked to do so without considering whether it could or should do so. He concluded that there was maladministration by GAD in acting inconsistently with the scheme's rules without having first properly considered whether it was permitted to act as it was. The PO highlighted a number of opportunities which GAD missed to review the tables.

PO's directions

The PO stated that the obvious remedy is that the Applicant should be put in the position he would have been in had the missed reviews taken place, that is, had his cash lump sum been calculated using the commutation factor that would have applied on his retirement. The PO directed GAD to notify the scheme administrator of the factor that would have applied to the Applicant if the tables had been reviewed in December 2004. He stated that if the factors are changed in the Applicant's favour, unless the relevant authority resists, this will result in an automatic payment.

The PO also directed that certain payments be made by GAD: if HMRC states that any additional lump sum will not be tax free, GAD should pay the Applicant a sum equivalent to the tax liability; and GAD should pay the Applicant simple interest on any additional lump sum.

Having noted that the relevant authority in this or other cases may resist payment, the PO stated that there "*simply is no tidy solution*" that would place undisputable liability for any additional lump sums across the four national jurisdictions exactly where it would have been. However, he expressed the hope that the relevant bodies will swiftly take steps to deal with the position of other affected retired firefighters and police so that it will not be necessary for their complaints to be pursued. He noted that this may involve discussion as to where liability ends up but strongly recommended this question be regarded as secondary to members receiving payments they will be due as soon as possible.

Schemes should consider checking their rules in light of this determination and ensuring that processes for reviewing commutation factors comply with the rules. If you would like assistance with this, please get in touch with your usual DLA Piper pensions contact.

OTHER NEWS

LEVY FAQs

The Pension Protection Fund added some further Frequently Asked Questions to its website in relation to the PPF levy in May. One of the issues covered is appeals against the Experian insolvency score with the FAQs covering the following points.

- Appeals can be made to Experian against "Appealable Scores", that is, the Mean Score (for 2015/16, this is the mean average of Monthly Scores from October 2014 to March 2015), Levy Band or Levy Rate calculated for an employer or guarantor. A trustee can make such an appeal in relation to any Appealable Score and an employer or guarantor can make such an appeal in relation to its own Appealable Score. The FAQs also look at the timing of such appeals.
- Scheme trustees who are dissatisfied with Experian's decision about whether to change the Mean Score, Levy Band or Levy Rate, can ask the PPF to informally review the circumstances of the appeal. Employers or guarantors will need to show that the trustees have authorised them to take this step.
  - If the PPF agrees that a change should be made, it will ask Experian to do so ahead of issuing the scheme's invoice.
  - If the PPF does **not** make a change, the entitlement to request a formal PPF review within 28 days of the levy invoice being issued will remain. However, the PPF will explain why, on the basis of the information they have seen, they think it unlikely that a formal Levy Review would be found in the scheme's favour.
  - The PPF positively encourages schemes to make an informal query rather than wait for their invoice – for the PPF, this can avoid issuing unnecessary invoices and credit notes, and for schemes it avoids having to choose between paying a levy they believe will be reduced or facing a charge for late payment.

The other area covered by the FAQs is mortgage certification, with questions looking at: whether Mortgage Exclusion Certificates need to be re-submitted for 2016/17 Monthly Scores to benefit from them; and why the mortgage element of a Monthly Score may have worsened following the Experian Portal refresh in May 2015.

DEVELOPMENTS FROM EIOPA

On 11 May the European Insurance and Occupational Pensions Authority (EIOPA) announced the launch of a pensions stress test and a quantitative assessment on solvency for occupational pension funds. EIOPA states that the selection of IORPs to be involved will be made by national supervisors, and that the stress test and the quantitative assessment will be conducted in parallel to minimise the burden on IORPs, with both exercises running until 10 August 2015.

Stress test

The stress test will assess the resilience of IORPs and their pension schemes to adverse market scenarios and a longevity scenario, and covers both DB and DC plans. EIOPA's press release explains that the stress test will provide insight and raise awareness of the occupational pensions sector risks and vulnerabilities.

The timeline for the stress test gives December 2015 as the date for the disclosure of the results of the stress test analysis.

Quantitative assessment

Background

The preliminary results of a previous Quantitative Impact Study (QIS) were published in April 2013. The QIS looked at proposals for a "holistic balance sheet" and the calculation of assets, liabilities and capital requirements. The aim of the holistic balance sheet was to make the valuation of assets and liabilities more comparable and transparent across Europe rather than the current system where schemes are subject to different national rules.

The preliminary results of the QIS were heavily caveated but included that the potential impact of the introduction of the holistic balance sheet was, for a benchmark scenario, a shortfall for UK schemes of around £450 billion. It was therefore welcome news for sponsoring employers of UK schemes when in May 2013 the European Commission announced that provisions on solvency would not feature in its proposals for a revised IORP Directive.

However, when the draft revised IORP Directive was published in March 2014, accompanying FAQs reported that EIOPA was carrying out detailed technical work in the area of solvency. In October 2014 EIOPA published a consultation paper on its "*Further Work on Solvency of IORPs*" which was the first step of the further work on solvency of IORPs that EIOPA is "*undertaking on its own initiative*". EIOPA stated that it expected to publish draft technical specifications by early 2015 for a quantitative impact assessment.

May 2015 quantitative assessment

In its press release issued on 15 May EIOPA states that following the October 2014 consultation paper, it has now launched a quantitative assessment on solvency for occupational pension funds and published the feedback of stakeholders to the consultation.

EIOPA explains that the quantitative assessment will gather data of IORPs on potential uses of the holistic balance sheet within an EU-wide supervisory framework, and that the outcomes will support EIOPA in further developing its advice to the European Commission on EU solvency rules for IORPs, which EIOPA expects to deliver in March 2016.

ON THE HORIZON

- **Equalisation for GMPs.** It had previously been expected that guidance on conversion of GMPs would be published in spring 2014 but, as at the end of May 2015, this had not been published. An HMRC Bulletin on the end of contracting-out issued in July 2014 reported that the DWP understands that schemes are waiting for GMP conversion guidance but it thinks it is important to develop fully considered proposals, and guidance will be published when this critical work is completed.
- **DC reform guidance.** The Regulator intends to publish more detailed guidance on the charges and governance regulations which came into force on 6 April 2015 and to update its DC code of practice to reflect the April 2015 legislative changes.
- **DC regulation.** The Regulator expects trustees of occupational pension schemes to assess the extent to which their scheme complies with the DC quality features and publish a governance statement in relation to this assessment at the end of the 2014/15 scheme year.
- **Summer budget.** In May 2015 it was announced that a Summer Budget will take place on 8 July 2015.
- **The end of contracting-out.** The response to consultation on the regulations about how to administer accrued contracted-out rights will be published in summer 2015.
- **Pensions Tax Manual.** In March HMRC published a draft version of the Pensions Tax Manual (PTM) which will replace the current Registered Pension Schemes Manual. The PTM is currently in draft form and HMRC intends to incorporate comments on it with a view to the guidance being updated in summer 2015.
- **Review of survivor benefits.** The review of different treatment of survivor benefits under occupational pension schemes required to be completed under the Marriage (Same Sex Couples) Act 2013 has been published, although no date has been given for when the Secretary of State will announce whether or not any amendments will be made to the legislation. The Employment Appeal Tribunal's judgment in the *Walker v Innospec* case concerning the restrictions placed on benefits payable to civil partners is the subject of an appeal to the Court of Appeal, with a hearing due to take place in summer 2015.
- **DB guidance.** On 22 May 2015 when the Regulator published its annual defined benefit funding statement, it reported that in the coming months, it plans to publish additional practical guidance on an integrated approach to managing risk, covenant assessment and setting an investment strategy to complement the Code of Practice.
- **Review of consumer price statistics.** Following the report of an independent review, a public consultation on the consumer price statistics is expected to be published in summer 2015 with the response to follow later in the year.
- **Transparency of DC charges.** The April 2015 measures on charges include some reporting requirements in relation to charges and transaction costs. The DWP intends to build on this and on 2 March published a joint Call for Evidence with the FCA which closed for comments on 4 May 2015.

PENSIONS NEWS

- **Short service refunds.** Short service refunds will be withdrawn from money purchase schemes from 1 October 2015.
- **Solvency.** Following its October 2014 consultation on further work on solvency of IORPs, on 15 May 2015 EIOPA published the feedback to the consultation and launched a quantitative assessment on solvency for occupational pension funds. The outcomes of the assessment will support EIOPA in further developing its advice to the European Commission on EU solvency rules for IORPs, which EIOPA expects to deliver in March 2016.
- **Transfers guidance.** In the response to consultation on the DB to DC transfers guidance, the Regulator stated that it will review its guidance on transfers in 2016 in light of experience and agrees that, through this process, the consolidation of material will be beneficial to trustees and their administrators.
- **Investment regulations.** A consultation in relation to some amendments to the investment regulations following recommendations made by the Law Commission in July 2014 closed in April 2015. It is expected that any changes to the legislation arising from the consultation would be made in 2016.
- **DC charges.** From April 2016, it is proposed that member-borne commission payments and Active Member Discounts will be banned from DC qualifying schemes.
- **End of contracting-out.** The reform of state pension which will result in the end of contracting-out is due to take effect in April 2016.
- **Defined ambition.** During the progress of the Pension Schemes Act 2015 through Parliament it was stated that it is envisaged that the provisions of the Act on Defined Ambition and collective schemes will be available in time for the end of contracting-out in April 2016.
- **Lifetime allowance.** In the March 2015 Budget it was announced that the Lifetime Allowance will be reduced from £1.25 million to £1 million from 6 April 2016 and transitional protection will be introduced.
- **Flexibility for existing annuity holders.** In the March 2015 Budget it was announced that from April 2016 the Government will change the tax rules to allow people who are already receiving income from an annuity to sell that income to a third party, subject to the agreement of the annuity provider. A consultation in relation to these proposals closes on 18 June 2015.
- **Automatic transfers.** The system of automatic transfers is intended to be launched in October 2016. Following the publication of a framework document in February, further detail and a consultation are expected to be published later in 2015.
- **IORP II.** The draft updated IORP Directive published in March 2014 proposed that Member States would have to transpose the new IORP Directive into national law by 31 December 2016. An updated draft published in September 2014 deleted this date and did not replace it with a new date. A further draft published in December 2014 stated that Member States would have two years after the entry into force of the Directive to transpose it into national law.
- **DC charges.** In 2017 it is proposed that the measures on DC charges and governance standards will be reviewed, in particular, the level of the charge cap and the question of whether any transaction costs should be included in the cap.
- **Lifetime allowance.** In the March 2015 Budget it was announced that the Lifetime Allowance will be indexed annually in line with inflation from 6 April 2018.

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