



# Pensionline

A Newsletter for Pension Scheme Managers and Trustees

Winter 2006

**Also in this issue:**  
**Pension Challenges to Smaller Firms**  
**New Additions to Trustee Toolkit**  
**Age Discrimination Regulations Deferred**

In our Spring newsletter, we outlined the key features of the The Pension Regulator's planned future strategy as set out in its published strategy document. Within the report, The Pensions Regulator (TPR) has criticised the governance of many pension schemes and cited poor standards of trustee knowledge and understanding particularly in smaller schemes. Over the summer, the Association of Consulting Actuaries produced a report into pension provision among smaller employers which highlights some of the challenges faced by such employers. We take a look at the key findings below.

In the pensions news recently, there has been a deal of publicity surrounding potential new products designed to provide companies and trustees with new options as to how to manage their pensions risk. You can read below what TPR has to say about this and its concern that such products might lead to employers abandoning their pension schemes.

Following on from the issue of TPR's code of practice on trustee knowledge and understanding in the Spring, TPR has recently launched three new modules of the Trustee Toolkit. See below.

Also in this edition, we return to the complex topic of Age Discrimination and consider whether we are any nearer clarification of some of the issues relating to pensions.

## Regulator promises guidance for trustees on corporate transactions

Speaking at the European Pensions 2006 conference in London in October, Tony Hobman, Chief Executive of The Pensions Regulator (TPR) welcomed innovative thinking in pension scheme management, demonstrated by recent new product development, but voiced concerns that certain new deals may lead to employers abandoning their pension schemes.



Mr Hobman said that, while TPR welcomes innovation in the way pension schemes are managed, trustees should be able to secure innovation and improvement in the areas of administration and investment without breaking the link with the employer. TPR is starting to see proposed corporate transactions involving pension schemes where the primary intent behind the transaction appears to be for the employer to abandon the pension scheme without paying the full buy out cost of the benefits.

These transactions would transfer pension schemes to new vehicles involving a nominal sponsoring employer and effectively leave the scheme without the support of a substantive ongoing employer. Once the link to any employer is removed the trustees will have lost an important backstop to protect scheme members if the pension fund runs into difficulties in the future.

Mr Hobman said that "Trustees should apply a high level of scrutiny to any such transactions which are brought to them." He warned that promises of access to better services are not of themselves seen as relevant factors for trustees to consider in making decisions on transaction that break the link with the employer. They should presume from the start that it is unlikely to be in the best interests of their members to break the link with an employer of substance, except by paying the cost of buying out the benefits with a regulated insurance company.

TPR promises new guidance to help scheme trustees weigh up the proper value of the support given to a fund by an ongoing employer when considering corporate transactions which would remove that support. Consultation will begin early next year.

## New additions to the Trustee Toolkit

Three new modules relating to funding defined benefit pension schemes have been issued by The Pensions Regulator (TPR) and are now available online as part of the e-learning programme, the Trustee Toolkit. Aimed specifically at trustees of defined benefit schemes, these modules are:

### How a defined benefit scheme works

This explains how benefits accrue, how they are calculated and what trustees should consider if their scheme is in deficit.

### Funding your defined benefit scheme

This covers the implications of the statutory funding objective, different ways to measure liabilities and the funding position of the scheme.

### Defined benefit recovery plans

This third module covers accrued benefits, future service funding methods, recovery plans, setting the contribution rate and the statement of funding principles.

This trio of scheme funding toolkits explores a number of issues surrounding scheme funding and invites the trustee to complete a series of exercises covering scenarios they are likely to face in their own schemes. By completing the e-learning programme, TPR hopes that the majority of trustees will be able to bring their knowledge and understanding up to date in a convenient way that encourages them to become familiar with their own scheme.

## Pension challenges for smaller firms



Earlier this year the Association of Consulting Actuaries (ACA) conducted a survey of pension trends among smaller firms. The survey covered over 460 firms, all with 250 or fewer employees. Such firms employ 58% of the UK workforce and produce over half of UK business turnover so represent a very important sector of our economy. The survey found a worrying deterioration in occupational pension schemes within this sector. There has been a steep decline in the number of defined benefit (or final salary) schemes which remain open to new employees compared to previous surveys and evidence of levelling down of defined contribution (or money purchase) schemes.

### The main findings were as follows:

- Over 80% of firms in this sector provide no pension arrangements whatsoever so the government's proposals for a compulsory National Pension Savings Scheme will have real impact. Most firms support the proposals but are concerned about cost and complexity.

- Except in the smallest firms, employing less than 50 people, a pension scheme is not seen as an important factor in recruitment or retention of staff.
- Over 70% of defined benefit schemes are closed to new members and over 40% have ceased future accrual for existing members
- The funding levels of these schemes are now on average only 69% compared to 80% in 2004.
- Occupational trust based defined contribution schemes are being closed in favour of lower cost Stakeholder plans.
- The cost of management time spent in running pension schemes and the cost impact of legislation are the two greatest concerns of firms in this sector.

## Age discrimination regulations deferred



When the pensions aspects of the new age discrimination rules were deferred from 1 October to 1 December 2006, it was hoped that the additional time being allowed for consultation would bring clarity to a number of the issues employers and trustees face in seeking to comply with the regulations. It seems such hope may have been misplaced.

Age discrimination in relation to pensions was always likely to be a minefield in that pensions are essentially age discriminatory. However, early indications of widespread exemptions led most people in the industry to relax – mistakenly it appears. While there are some specific exemptions, others need to be justified as a proportionate means of

achieving an equitable aim. Some now argue that, in fact, the UK government has gone much further than originally intended by the European directive. As a result, sponsors and schemes face significant additional costs, as a minimum from the need to seek complex legal advice on the issue, possibly through the need to level up benefits or contributions in certain areas and ultimately perhaps through having to seek determinations through the courts. Who could blame an employer for seeking to level down benefits or contributions where he can? Once again the likely outcome can surely only be to further worsen the state of UK occupational pension provision, which was once the envy of Europe.

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