PPF TN Technical News

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Pension Protection Fund

In this issue

Welcome...

...to Technical News, the Pension Protection Fund's (PPF) newsletter on topical issues including practical guidance for schemes in PPF assessment periods.

In this edition we'll be looking at the implications of the February 2018 legislative changes concerning the PPF's treatment of step-down pensions and the introduction of regulations about the FAS long service cap. We'll also be looking at our role in supporting schemes in assessment meet their obligations under the Audited Accounts Regulations.

If there are any technical issues about which you would like to hear from us, please do submit a comment via our website here and where appropriate we will consider including an update in a future edition.

Step-down Regulations

OVERVIEW

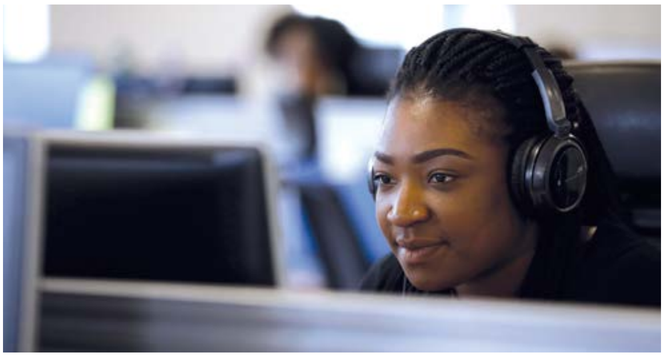
On the 24 February 2018 new regulations (SI 2018/95 PPF (Compensation) (Amendment) Regulations 2018) came into force about the treatment of step-down pensions for PPF schemes. Before this time there was no mechanism in the PPF legislation to reduce, or step-down, PPF compensation.

Going forward the PPF will be able to reduce step-down pensions where the pension would have reduced under the scheme rules. The new regulations will help to ensure PPF compensation is consistent with the provisions of the former scheme's rules.

A scheme's rules will specify if step-down pensions are payable. Step-down pensions are normally designed to smooth pension income throughout a member's retirement after taking account of state benefits payable from state pension age (SPA). It is sometimes the case that a scheme's rules provide that on a member's retirement before SPA, they are entitled to:

- a main pension which is payable for life; and
- a "bridging pension" which is payable until the member's state benefits come into payment at SPA.

The new regulations identify two distinct elements of the member's step-down pension; the main portion, payable for the member's lifetime ("the basic element"), and an additional amount payable only until the decrease date ("the bridging element"). These elements must be treated as two separate pensions, allowing the PPF to cease payment of the bridging element, at the bridging end date, and continue to pay the basic element for the lifetime of the member.



Where the portions of the member's step-down pension which constitute the two elements or the decrease date cannot be identified from the scheme rules, the regulations give the Board of the PPF the discretion to treat these elements as such portions of the member's step-down pension, or the decrease date as such a date, as it considers appropriate.

Below, you will find further information on how the step-down regulations interact with existing PPF legislation.

COMPENSATION CAP

Both the basic and bridging element should be taken into account when testing against the compensation cap. If the bridging element was not included for the purpose of applying the cap, then a member with a single rate pension would be disadvantaged as compared to a member with a step-down pension of the same lifetime value. As such, the bridging element should always be taken into account when testing against the cap. The compensation cap must be compared with an annual value of benefits. PPF actuarial factors are available for determining the annualised whole-life equivalent of the bridging element. These factors will be reviewed from time to time.

SURVIVORS' ENTITLEMENT

A surviving spouse or civil/relevant partner of a member who died before reaching Normal Pension Age (NPA) will receive compensation in respect of the bridging element, payable immediately, for the same period of time as the member would have been entitled to receive it. Where a member dies part way through receiving their bridging element, the survivor would receive compensation in respect of the bridging element for the remaining period of time it is due to be paid. Where a member dies after the bridging element end date, there would be no survivor entitlement due in respect of the bridging element. Survivor compensation payable in respect of the basic element would be payable for life.

EARLY RETIREMENT

Where a member takes early retirement, the bridging element of their compensation is paid at an actuarially reduced rate to take account of it being paid for a longer period. The regulations require the bridging element paid to the survivor, in the event of their death, also to take account of the actuarial reduction in the rate of compensation payable. PPF actuarial early retirement factors are available for the bridging element of compensation, which take into account that the bridging element is only payable until the bridging end date. The early retirement factor is applied to the compensation before the compensation cap is applied. Early retirement factors will be reviewed from time to time and may be changed without notice.

LATE RETIREMENT

Where a member takes late retirement and delays receiving their compensation until after their NPA, the regulations do not provide for a late retirement factor to be applied to the bridging element of the compensation. Members who opt to retire late will receive the bridging element part of their compensation from their actual retirement date until the bridging end date and if they postpone their retirement beyond the bridging end date, they will lose their right to the bridging element. A late retirement factor would still be applied to the basic element of their compensation, which is payable for life.

COMMUTATION

The bridging element can be commuted for tax free cash. The member will be able to commute up to 25% of the annual rate of the bridging element of their compensation for tax free cash. For example, if the bridging element is £100pa, the member will be able to commute up to £25pa for tax free cash. The PPF has published commutation factor tables which set out how much tax free cash the member will receive for each £1pa of bridging element which is commuted.

WILL MEMBERS OF EXISTING PPF SCHEMES BE IMPACTED?

The step-down regulations came into force on 24th February 2018. Any scheme entering PPF assessment on or after the date the regulations came into force will be subject to the new compensation rules. There will be no impact on members of those schemes which entered a PPF assessment period before the regulations came into force.

LIFETIME ALLOWANCE

A member's lifetime allowance will be tested against the value of both the bridging element and the basic element.

DATA INTERFACE LAYOUT (DIL)

The amount of the basic and bridging elements of step-down pensions and bridging end dates are already captured on our Data Interface Layout (DIL) tool. Each element has an indicator for a "bridging pension" and where applicable we ask for the end date that the pension would have ceased under the scheme rules. Please see the DIL guidance for details.

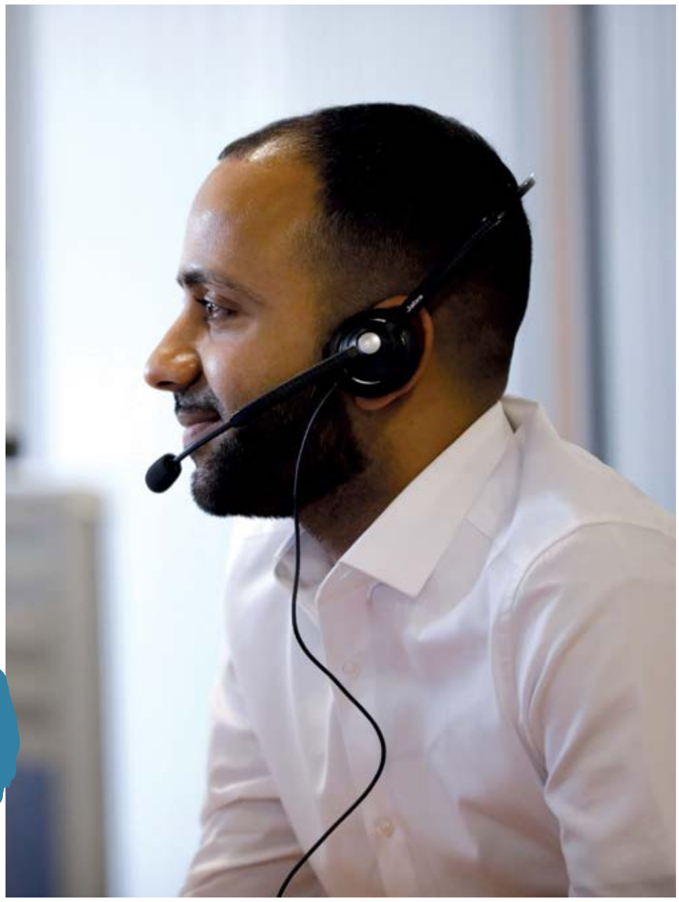
FAS Long Service Cap

Following a DWP led consultation, the Financial Assistance Scheme (Increased Cap for Long Service) Regulations 2018 came into force on 20th February.

The regulations operate in a similar way to the PPF long service cap provisions, which came into effect from 6 April 2017, and the FAS Cap is increased by 3% for each full year of pensionable service over 20 years.

Transitional regulations apply to members who were already entitled to FAS payments when the Long Service Cap came into force, and their cap is recalculated accordingly.

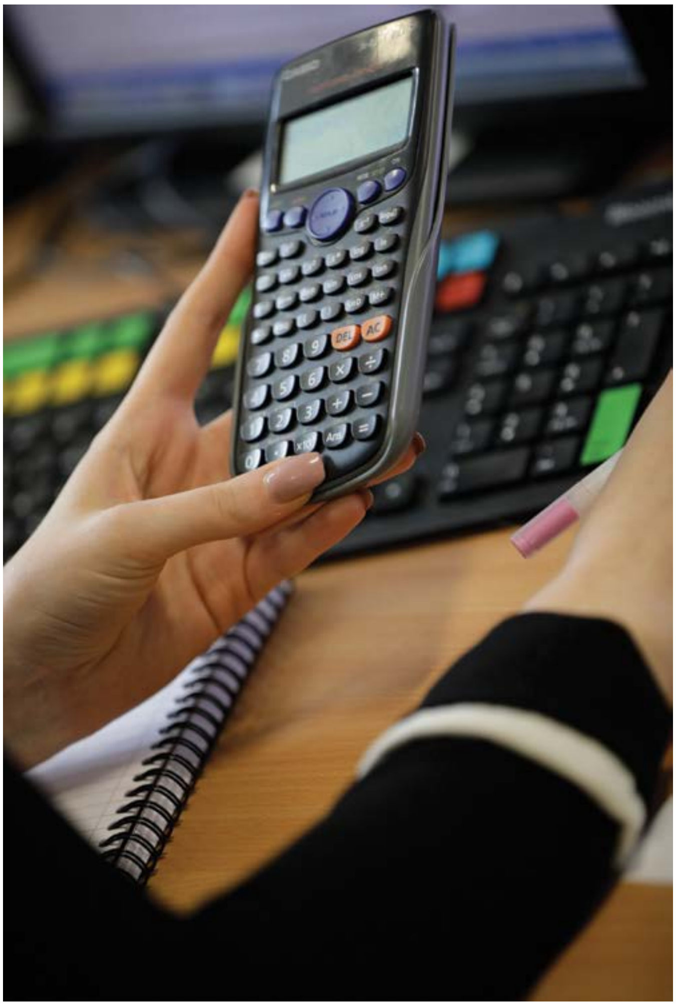
An exercise has been carried out to contact members affected by this change.



The need for audited accounts

Here at the PPF we continue to work closely with TPR to make sure we can support the trustees of schemes in assessment to meet their obligations under the Audited Accounts Regulations. This includes helping trustees take advantage of the flexibility built into the Regs to change accounting periods from between 6 and 18 months (provided this change is "in connection with the ... termination of the scheme") so that accounts can be obtained at the Relevant Date, during and, if necessary, at the end of the assessment period.

In extreme circumstances, the particular demands of PPF assessment may constitute a "reasonable excuse" for missing the 7 month deadline but it is of course crucial to communicate with TPR long before that deadline expires.



TPR has a renewed focus, as part of their 'clearer, quicker and tougher' approach, on ensuring compliance with mandatory requirements. Recently, for the first time ever, TPR has used its powers under the Pensions Act 1995 to fine trustees for their failure to obtain audited accounts.

You can find more about the case and the fines imposed on the trustees of the scheme here. While the wider concerns about governance that the failure to obtain audited accounts were indicative of, are unlikely apply to a scheme in assessment, this highlights the need to meet statutory requirements.

As we work closely with schemes in assessment we can provide advice and guidance on helping ensure audited accounts are obtained. We are also just about to complete the re-procurement of the PPF Scheme Audit Panel.

These activities combine to ensure support for trustees of schemes in assessment to obtain the right accounts, at the right time, at the right cost.

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The information we provide is for guidance only and should not be taken as a definitive interpretation of the law.

PPF Technical Team, June 2018

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