DWP Department for Work and Pensions

Financial Assistance Scheme
Pension Protection and Stewardship Division

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Our phone number 0207 449 7404
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Website www.dwp.gov.uk

Date: 28 January 2010

Dear Sir or Madam

Consultation on draft Financial Assistance Scheme guidance relating to the transfer of pension scheme assets to government

The draft Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2010 ('the draft Regulations') were laid before Parliament on 3 February 2010. The draft Regulations complete the package of legislative changes required to implement the extension to the Financial Assistance Scheme (FAS) announced by the Government in December 2007. This follows a number of earlier reforms, which included making the Board of the Pension Protection Fund (PPF) FAS scheme manager from July 2009.

The draft Regulations include provision for the assets remaining in relevant FAS qualifying schemes to transfer to government. When assets transfer to government, beneficiaries in such schemes will receive sole payment from FAS, rather than a payment from their scheme and a top-up payment from FAS. The draft Regulations also provide for valuations of assets and liabilities ('the FAS valuation') to be undertaken in respect of relevant schemes and for individual asset shares to be calculated for scheme beneficiaries.

In general, the FAS valuation will be undertaken by the scheme actuary. As part of the valuation the actuary will be asked to divide the assets amongst relevant beneficiaries to provide an 'Asset Share' for each beneficiary. The Asset Share will be used by the FAS to help calculate payments for those beneficiaries.

The draft Regulations provide that the FAS scheme manager may require scheme accounts to support the valuation. The draft Regulations also provide that guidance may be published in relation to certain activity, including:

- how certain assets are valued by the actuary;
- how Asset Shares should be calculated by the actuary; and

- the form and manner in which the results of the FAS valuation are presented.

This consultation document seeks views on draft guidance in these areas.

The Government is also taking this opportunity to consult on draft guidance on how expected pension data might be provided by schemes transferring assets to government to ensure FAS payments are calculated on an equalised basis.

Draft guidance on the calculation of Asset Shares was previously consulted on between 2 April and 15 May 2009. Responses from that consultation and subsequent consultation on relevant draft regulations over late Summer 2009 have been taken into account in drafting this consultation package. There are two particular substantive changes in the Asset Share guidance that may be noted:

- the guidance no longer sets out that actuaries should calculate a rate of pension that could have been secured with the Asset Share (this function will be undertaken by the FAS scheme manager); and
- the guidance includes calculations that must be undertaken to ensure that Asset Shares are equalised between men and women (in particular for the effects of guaranteed minimum pensions (GMP)).

The Government recognises that the legislation relating to the winding-up of pension schemes is, for good reason, not always totally prescriptive. The procedures described in this guidance should be considered as applying only to schemes that are qualifying schemes for FAS and that are transferring their assets to government. The guidance should not be considered as applying more generally to other schemes in wind-up or seeking to equalise benefits, nor as indicating the Government's view of how procedures should be applied in this wider context.

Target audience

The consultation is technical in nature and is primarily aimed at pension industry professionals and others with an interest in defined benefit occupational pension schemes. However, the Government is mindful that the matters covered in this consultation will affect the payments made to FAS beneficiaries. Therefore, the Government would welcome feedback from members who may be affected and their representatives.

The Government has undertaken considerable informal consultation since the extension to the Financial Assistance Scheme was announced in December 2007. Officials have regular contact with trustees who have given them the benefit of their extensive knowledge of occupational pension schemes.

Where can I find the consultation document?

The draft guidance is available on the Department for Work and Pensions (DWP) website at www.dwp.gov.uk/consultations and www.dwp.gov.uk/fas .

Timing

The consultation period begins on 28 January and runs until 10 March 2010.

A consultation period of six weeks is in line with DWP practice in relation to limited technical consultations.

How can I respond to the consultation?

The Government would be grateful for your comments on any of the points covered in this document. Please ensure that your response reaches us by the closing date.

A list of those to whom this document has been sent is attached. If you have any suggestions of others who may wish to be involved in this process, please contact us.

Please send consultation responses to:

Post Financial Assistance Scheme Consultation
Pensions Protection and Stewardship Division
Department for Work and Pensions
Caxton House
7th Floor
6-12 Tothill Street
London SW1H 9NA

Email caxton.fas-responses@dwp.gsi.gov.uk

When responding, please state whether you are responding as an individual or representing the views of an organisation. If responding on behalf of a larger organisation please make it clear whom the organisation represents and (where applicable) how the views of members were assembled.

Freedom of Information

All information contained in your response, including personal information, may be subject to publication or disclosure if requested under the Freedom of Information Act 2000. By providing personal information for the purpose of the public consultation exercise, it is understood that you consent to its disclosure and publication. If this is not the case, you should limit any personal information which is provided, or remove it completely. If you want the information in your response to the consultation to be kept confidential, you should explain why as part of your response, although we cannot guarantee to do this. We cannot guarantee confidentiality of electronic responses even if your IT system claims it automatically.

If you want to find out more about the general principles of Freedom of Information and how it is applied within DWP, please contact:

Post Charles Cushing
Adjudication and Constitutional Issues
Department for Work and Pensions
Information Policy Division, Freedom of Information Unit
1-11 John Adam Street
London WC2N 6HT

Phone 0207 962 8581

Email charles.cushing@dwp.gsi.gov.uk or carol.smith14@dwp.gsi.gov.uk

More information about the Freedom of Information Act can be found on the website of the Ministry of Justice.

What will we do after the consultation?

A summary of responses (including the next steps to be taken) will be published online (and linked from the same web page as above). Paper copies will be available on request.

The consultation process

We value your feedback on how well we consult. If you have any comments on the process of this consultation (as opposed to the issues raised) please contact our Consultation Coordinator:

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Yours faithfully

Andy Maggs

Policy and Legislation, Financial Assistance Scheme

Email andrew.maggs@dwp.gsi.gov.uk

Copy list

Age Concern
Association of British Insurers
Association of Consulting Actuaries
Association of Pension Lawyers
Auditing Practices Board
Better Regulation Unit
Board for Actuarial Standards
British Chambers of Commerce
Community the Union
Confederation of British Industry
Department for Business, Innovation and Skills
Engineering Employers' Federation
Federation of Small Businesses
Financial Services Authority
GMB Union
Help the Aged
HM Revenue & Customs
HM Treasury (MOCOP)
Independent Pensions Research Group
Institute of Chartered Accountants in England and Wales
Institute of Chartered Accountants in Scotland
Institute of Directors
Institute of Payroll and Pensions Management
Investment Management Association
National Association of Pension Funds
National Consumer Council
National Pensioners' Convention
Pensions Action Group
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Pension Protection Fund
The Pensions Regulator
Pensions Research Accountants Group
SAGA
Social Security Policy and Legislation Division, DSD, Northern Ireland
Small Business Service
The Association of Corporate Trustees
The Faculty of Actuaries
The Institute of Actuaries
The Law Society
The Law Society of Scotland
The Pensions Advisory Service
The Pensions Management Institute
The Scottish Executive
The Society of Pension Consultants
The Welsh Assembly
Trades Union Congress
UNISON
Unite the Union

Notification of the consultation has also been sent to members of the FAS advisory panel, actuarial consultancy firms that provide advice to FAS schemes, private individuals who have expressed an interest in participating in the consultation exercise, and respondents to related consultations undertaken by DWP.

Strategy, Information and Pensions

Draft guidance relating to the transfer of scheme assets to government

The Financial Assistance Scheme

CONSULTATION 2010

The Financial Assistance Scheme (FAS)

Consultation on draft guidance relating to the transfer of scheme assets to government

Background

1. The Financial Assistance Scheme (FAS) was set up in 2004. At that time it provided limited help to members of certain pension schemes that were winding-up under funded and could not qualify for Pension Protection Fund (PPF) compensation. Assistance was provided in the form of supplementary payments that would top-up annuities purchased by scheme trustees as part of the scheme wind-up process.

2. In December 2007 the Government announced an extension to the FAS. This extended the coverage of FAS assistance to 90 per cent of members' accrued pensions and included certain schemes with solvent sponsoring employers. This extension was to be part-funded by the Government taking in assets remaining in FAS qualifying schemes and was possible because of the extra value that the Government could achieve from those assets.

3. Since December 2007, the Government has introduced regulations to extend the assistance paid by the FAS and to transfer the role of the FAS scheme manager from the Secretary of State for Work and Pensions to the Board of the PPF.

4. The Government has recently consulted on the draft Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2010 ('the draft Regulations') that provide for the taking into government of the assets remaining in FAS qualifying schemes. The draft Regulations also provide for certain payments relating to the transferred assets to be made. This consultation ended on 6 October 2009 and draft Regulations have now been laid before Parliament.

5. The draft Regulations take account of the fact that had assets not been transferred to government but instead been used to buy annuities for beneficiaries, some would have received pensions higher than the assistance payments that FAS provides as standard. Typically, such beneficiaries will be those who were in receipt of payments from their scheme before it started to wind-up (as such benefits tend to receive higher priority when schemes allocate assets).

6. To help ensure such beneficiaries do not lose out on the pensions they could have received from an annuity, the assets of transferring schemes will need to be valued and allocated amongst relevant beneficiaries and a 'Notional Pension' calculated; that is, the amount of pension that could have been purchased with the Asset Share. The Notional Pension will be used by the FAS scheme manager to determine whether a person should receive Assistance payments higher than would otherwise be payable by the FAS. The Notional

The valuation

7. The draft Regulations provide for the FAS scheme manager to instruct the trustees (or managers) of relevant schemes to obtain a valuation of scheme assets, liabilities and Asset Shares for FAS purposes. The valuation will be undertaken by a 'Valuation Actuary' approved by the FAS scheme manager who will usually be the scheme actuary. However, there is flexibility in the draft Regulations for the FAS scheme manager to appoint another actuary where, exceptionally, it is considered that they are more suited to the task. The Valuation Actuary will be responsible for producing a valuation that establishes:

   - the value of the assets of the scheme;
   - the value of the liabilities of the scheme for relevant beneficiaries; and
   - relevant beneficiaries Asset Shares.

8. FAS valuations will only be undertaken once the FAS scheme manager is satisfied that necessary preparation work has been completed by the scheme; for example, ensuring data held on scheme members is up-to-date and complete. FAS caseworkers will liaise with schemes to decide when it is appropriate to proceed with the valuation. The preparatory work will include the identification and consideration of assets that may raise particular valuation issues, such as debts owed to the scheme.

9. In certain limited circumstances it is anticipated that full valuations will not be required. For example, it may be apparent that schemes are funded in such a way that all remaining assets will be allocated to high-priority pensioner members only; and that even these members would not stand to receive payments above the level guaranteed by the FAS had the scheme instead purchased annuities. The draft Regulations provide general powers for valuation requirements to be waived at the FAS scheme manager's discretion in respect of the production of relevant accounts, the calculation of liabilities and the calculation of Asset Shares.

10. It is not anticipated that such powers will be used frequently. However, the Government is keen to ensure that opportunities are taken to avoid unnecessary work where possible.

Identifying schemes subject to the valuation and transfer provisions

11. Under the draft Regulations, the valuation and asset transfer processes will not apply to a FAS qualifying scheme in which all defined benefit liabilities have been discharged or where the FAS scheme manager thinks they are likely to all be discharged by:

- annuity purchase (whether because of a binding commitment to purchase annuities or an approval to purchase annuities under section 286A of the Pensions Act 2004);
- payment of transfers or relevant discharge lump sums; or
- buy-back into the State Scheme (permissible in certain limited circumstances).

Treatment of liabilities partially discharged via purchase of annuities, State Scheme Premiums or part transfers

12. During the wind-up process, pension schemes sometimes arrange for liabilities to be partially discharged by the purchase of annuities or by buying back contracted-out State Scheme entitlements. In other cases transfer payments might be made to members on the understanding that further assets could be allocated to those members at the end of wind up.

13. Where additional assets would be allocated to members whose liabilities have been partially discharged by way of a State Scheme Premium (SSP) or a partial-transfer payment, the Government considers it appropriate for those assets to transfer to government. The draft Regulations provide for members who have received partial discharge payments by way of a SSP or a transfer payment to be included in the valuation.

14. Where liabilities have already been partially discharged through the purchase of an annuity, the Government expects trustees, in most cases, to discharge remaining liabilities to these scheme members and not transfer relevant assets to government. However, where even with the income from an additional annuity, members would still receive supplementary top-up payments from the FAS, it is recognised that members would not gain from any further annuity purchase. It is expected that the FAS scheme manager will work with trustees to identify such cases and consider whether it would be more appropriate for relevant assets to transfer to government rather than be used to purchase further annuities.

Defined-benefit additional voluntary contributions

15. Trustees, at their discretion, will be able to separately discharge defined-benefit additional voluntary contributions (DB AVCs) prior to the transfer of assets to government. The FAS scheme manager will expect trustees to identify cases where they plan to discharge such liabilities.

Preliminary valuations

16. In cases where it is necessary to allocate assets in respect of further annuity payments or DB AVCs, the FAS scheme manager will work with the Valuation Actuary in order that a preliminary valuation can be undertaken that includes the liabilities and assets that will be discharged by trustees.

Content of consultation on draft guidance and consultation questions

Introduction

17. This consultation document seeks views on draft guidance relating to FAS valuations. This is in five parts:

- Information on the preparation of relevant accounts, including guidance on valuing particular assets and permitted adjustments;
- Draft guidance on method and assumptions to use when undertaking a valuation under Regulation 22 of the amended Financial Assistance Scheme Regulations 2005;
- Draft guidance to the valuation template;
- Draft guidance on how expected pension data should be provided to ensure FAS payments are calculated on an equalised basis; and
- Draft example calculations for a valuation for relevant FAS qualifying schemes.

Relevant legislative provisions

18. Provisions within the draft Regulations amend the Financial Assistance Scheme Regulations 2005 (SI 2005/1986) ("the Regulations") to provide that guidance may be provided or information requested to support the production of valuations, for example:

- Regulation 2 (as amended) will set out that relevant accounts are in such manner and form as the scheme manger may request; and
- Regulation 22(5) will provide that valuations must be prepared in accordance with guidance published from time to time by the Secretary of State and presented in such manner and form as set out in guidance published from time to time by the scheme manager.

19. It should be noted that in order to aid presentation of the end-to-end valuation process, the draft guidance in the consultation documents does not distinguish between guidance that will be published by the Secretary of State and guidance that will published by the FAS scheme manager. Final guidance will be published in accordance with the relevant legislative provisions.

Draft guidance on the preparation of relevant accounts (including guidance on valuing particular assets and permitted actuarial adjustments)

20. The draft Regulations provide that, except in limited circumstances, the FAS valuation will be based on audited accounts prepared for the purposes of the FAS valuation.

21. The draft Regulations provide for the Valuation Actuary and the FAS scheme manager to make certain adjustments to the value of assets included in the audited accounts. This first section of this consultation document contains draft guidance on the production of relevant accounts and on permitted adjustments.

22. It should be noted that the Government is mindful that there are various existing requirements on trustees to obtain annual audited accounts within certain timescales and that these can place demands on the resources of schemes at certain points in the year. The FAS scheme manager will seek to work with schemes, accountants and auditors during the preparation period to provide an indication of when a valuation is likely to take place. This will allow them to decide whether to exercise the flexibility allowed within existing accounting requirements to adjust their accounting cycle so that the audited accounts produced at the calculation date meet both FAS valuation and other requirements.

Q1) The Government would welcome responses on the preparation of relevant accounts and the draft guidance on valuing particular assets and permitted actuarial adjustments.

Draft guidance on method and assumptions to use when undertaking a valuation under Regulation 22 of the FAS Regulations 2005

23. This section contains draft guidance on the calculation of Asset Shares. The Government intends that actuaries will allocate assets in broadly the same way as they would were schemes completing wind-up by purchasing annuities, principally by applying section 73 of the Pensions Act 1995 which sets out the order in which assets should be allocated on wind-up. This will help ensure that outcomes for members of schemes transferring assets to government will be broadly consistent with the outcomes of members of schemes that have already wound up.

24. However, there are some elements of discretion in the application of winding-up rules and processes and this draft guidance proposes standardised approaches in such areas by, for example, setting out how Asset Shares should be calculated:

- in respect of liabilities that should be valued on a ‘full buy-out’ basis;
- for beneficiaries who have died during wind-up;
- to equalise for the otherwise unequal effects of allocating assets against guaranteed minimum pensions; and
- the treatment of schemes whose assets exceed the statutory priority order liabilities.

Q2) The Government would welcome responses on the draft guidance on the calculation of Asset Shares. Responses are particularly welcomed on practicability and whether sufficient information will be readily available for the guidance to be applied.

25. In addition to responses on the general application of the guidance. There are three specific issues on which the Government is seeking views:

- the calculation of Asset Shares in respect of beneficiaries who die before the valuation calculation date;
- the treatment of State Scheme Premiums in the calculation of Asset Shares; and
- disregarding interest calculations in the calculation of Asset Shares.

The calculation of asset shares in respect of beneficiaries who die before the calculation date

26. The Government is seeking to ensure that beneficiaries receive the full value of assets allocated to them in the valuation. Where beneficiaries have died the Government considers that any arrears should, where possible, be paid to their estates. To help meet this aim the Government proposes that Asset Shares are calculated for all beneficiaries who were entitled to a pension at the start of wind-up or who became entitled to a pension after that time and who die before the calculation date.

27. Where a beneficiary entitled to a FAS payment dies before the calculation date the FAS scheme manager will be able, under the Regulations, to calculate the amount that deceased member should have been paid up to the date of death, compare that with the interim pension paid and where arrears are due, pay those arrears to their estate.

28. The FAS scheme manager will also have the power to make such payments where a beneficiary dies between calculation and transfer dates and before becoming entitled to a FAS payment.

29. However, the FAS scheme manager will not have the power to make such payments where a beneficiary dies before the calculation date and before they have an entitlement to FAS, i.e. an early retiree. The Government will consider extending legislation in due course so that such payments can be made but, in the meantime, it expects that trustees will be able to make relevant arrears payments to estates on the approval of the FAS scheme manager.

30. The Government does not anticipate that it will be cost-effective to seek to reclaim any overpayments from estates. It therefore proposes that where an overpayment has occurred, Asset Shares will be disregarded where necessary and such members excluded from the FAS valuation. In this instance, assets

Q3) The Government welcomes views on the proposed approaches to beneficiaries who have died during wind-up, particularly if its proposals do not accord with conventional practice in scheme wind-ups.

The treatment of State Scheme Premiums in the calculation of Asset Shares

31. In certain circumstances State Scheme Premiums (SSPs) can be paid by schemes in order to reinstate certain members' State Pension rights. In such cases, FAS payments are calculated by turning the amount paid for the premium into a notional pension and deducting it from the amount of gross assistance due. This deduction is achieved by the FAS applying an annuity factor to the premium in order to estimate the amount of bulk annuity that could have been secured with the cash sum.

32. The Asset Share guidance sets out how liabilities should be valued where an SSP has been paid or where the trustees have agreed with relevant authorities to pay such a premium.

33. Where SSPs have been paid before FAS valuations are undertaken or are due to be paid after the valuation, the Government considers that the Guaranteed Minimum Pension (GMP) liability should be treated as being satisfied (including any liability to pay GMPs during wind-up). Where SSPs have not been paid, but where payment is due, it is proposed that the cost of the premium should be considered as an expense of the scheme (and thus accorded high priority) and for the GMP liability to be treated as satisfied by the commitment to pay the premium.

Q4) The Government welcomes views on the proposed treatment of State Scheme Premiums in the valuation particularly whether the proposal aligns with industry practice.

Disregarding interest calculations in the calculation of Asset Shares

34. The FAS does not provide interest when making any lump sum arrears payments back to a member's entitlement date. This position will be maintained when new types of payment are made as a consequence of asset transfer. For consistency with this approach, and to avoid unnecessary complexity in the calculation of Asset Shares, the Government does not propose that interest is applied in the valuation of liabilities (for example, where past payments to members are included in the assets that are divided amongst members).

Q5) Views are welcomed on disregarding interest in relation to past payments in the calculation of Asset Shares.

Draft guide to the valuation template

35. This part of the consultation document contains draft guidance to completing the valuation data template. The draft data template has been published separately as a Microsoft Excel document.

Q6) The Government welcomes responses on the valuation template and the completion guidance. Responses are particularly welcomed on practicability.

Draft guidance on how expected pension data should be provided to ensure FAS payments are calculated on an equalised basis

36. FAS payments are calculated by reference to the amount of pension a member had accrued within their scheme: the member's 'expected pension'. The Government is taking this opportunity to consult on a change to the information required on a member's expected pension that will be required from schemes that transfer assets to help meet the Government's obligation to ensure that FAS payments are equalised between men and women.

Q7) The Government welcomes responses on the draft guidance on how expected pension data should be provided. Responses are particularly welcomed on practicability and whether sufficient information will be readily available for the guidance to be applied.

Consultation on the proposed revision to the synthetic buy-out basis and the actuarial factors used to calculate FAS payments

37. It should be noted that the Government is separately consulting on related proposals to revise the FAS synthetic buy-out basis.

38. Under certain priority orders falling under section 73 of the Pensions Act 1995, certain liabilities have to be valued by reference to 'buy-out'; that is, the cost of

securing benefits with insurers. In order to ensure consistency between schemes transferring assets and in recognition that such schemes will often not have received actual buy-out quotes from insurers, the Government intends that such liabilities will be valued on the synthetic buy-out basis on which it is consulting.

39. The consultation on the synthetic buy-out basis is available on the DWP website at www.dwp.gov.uk/consultations and www.dwp.gov.uk/fas .

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Annex – List of consultation questions

Q1) The Government would welcome responses on the preparation of relevant accounts and the draft guidance on valuing particular assets and permitted actuarial adjustments.

Q2) The Government would welcome responses on the draft guidance on the calculation of Asset Shares. Responses are particularly welcomed on practicability and whether sufficient information will be readily available for the guidance to be applied.

Q3) The Government welcomes views on the proposed approaches to beneficiaries who have died during wind-up, particularly if its proposals do not accord with conventional practice in scheme wind-ups.

Q4) The Government welcomes views on the proposed treatment of State Scheme Premiums in the valuation particularly whether the proposal aligns with industry practice.

Q5) Views are welcomed on disregarding interest in relation to past payments in the calculation of Asset Shares.

Q6) The Government welcomes responses on the valuation template and the completion guidance. Responses are particularly welcomed on practicability.

Q7) The Government welcomes responses on the draft guidance on how expected pension data should be provided. Responses are particularly welcomed on practicability and whether sufficient information will be readily available for the guidance to be applied.