Deloitte.

Issue 2

Employer pensions alert
Pension levy
Key decisions and next steps

What you need to know

The Finance (No.2) Act was signed into law on 22 June 2011 and introduces the controversial four year annual levy of 0.6% on the value of private pension funds.

The final mechanics of the levy are slightly different to those proposed. It is now payable in single instalments (rather than bi-annually), with the first payment due on or by 25 September 2011 and annually thereafter in each of 2012, 2013 and 2014.

It applies to occupational defined benefit (DB) (excluding any contingent assets) and defined contribution (DC) pension funds, Retirement Annuity Contracts and Personal Retirement Savings Accounts (except where a lump sum payment has already been taken and the purchase of a pension annuity is simply deferred).

It does not apply to Approved Retirement Funds (ARFs) or to pensions that have been secured, in individual names, using annuities. Furthermore, assets in an IORP (Institution for Occupational Retirement Provision) relating to overseas employments are not affected. (Assets relating to Irish employments are caught.)

It is applied to the value of assets on 30 June of each year. For non insurance contracts, there is also an option to use the value of assets at the end of the previous accounting year.

The levy is payable by the relevant "chargeable persons". In the case of assets held under insurance contracts, this will be the insurance company and they have the power to reduce members' funds as if the levy was an expense.

Trustees and administrators have joint responsibility for payment in respect of assets that are not held in insurance contracts. However, there is some uncertainty around how duties are split, awaiting clarification from Revenue. In practice, it is expected that Trustees will collect and organise payment of the levy.

The Act gives the Trustees of DB schemes powers to pass the cost to members through an adjustment to members' benefits. Where the decision is made to reduce benefits, actuarial advice will be needed to ensure that the levy cost is allocated fairly across all members. Where the cost is not passed to members, the employer will ultimately bear the cost.

Deloitte commentary

Given current funding challenges with DB schemes, it is not surprising that in our experience, the majority of employers have or intend to refuse a request from the Trustees to meet the upfront cost of the levy and instead request that the cost is passed to members . However, Trustees are not obliged to do so. Employers will therefore need to engage constructively with Trustees to ensure that their concerns are understood.

Apart from cost pressures, the other key reasons for passing the cost to members include:

- To avoid inequities between the treatment of employees in DB schemes and those in DC schemes. Given that the majority of DB schemes are now closed, it is likely that more recently hired employees join a DC or PRSA arrangement in which case the levy will automatically be passed on through a reduction in fund values.

- To ensure the levy cost is allocated fairly across all members now. If the employer's ability to fund the scheme in the future deteriorates, under current rules, pensioners are likely to be proportionately better off, so in effect the bulk of the levy would then be absorbed by the actives and deferreds.

In deciding whether to pass the cost to members, employers will need to be cognisant of any employee/ IR issues, particularly at a time when salaries and increases are under pressure. It may also have unintuitive accounting consequences.

Employers should take into account that an announcement is due soon in relation to a revised DB funding standard. Details of the proposals are provided in our Employer Pensions Alert Issue 1 (available at www.deloitte.ie). It is generally expected that the revisions will be financially more significant than the levy and in many cases trigger a wider restructuring of benefits. It may therefore be preferable to postpone any decision around the levy until the final details and impact of the funding standard are known.

Contacts

What you need to do

1. Assess the cost of the levy over the next four years for each of your schemes.

2. Determine whether it is acceptable and appropriate to have different treatments for those employees in DB schemes and DC schemes.

3. If you have a DB scheme, determine whether you should refuse to meet the cost of the levy and instead request the Trustees to reduce members' benefits. Considerations include:
   - Impact on future costs
   - Possible implications for your funding proposal
   - Potential employee/ IR issues
   - Inequities in treatment between employees in DB and DC schemes
   - Wider pensions regulatory changes. Is it better to adopt a "wait and see" approach?

4. If you choose to request a reduction in benefits, develop a business case to take to the Trustees.

5. Agree a plan for how any change will be implemented. Decide on appropriate interim measures for benefit payments after 30 June up to when the proposed strategy will be implemented.

   If a decision is made not to pass on the cost to DB members, there may be other actions that could mitigate the impact of future levy payments, for example reducing the fund size by securing the pensioner liabilities with an insurance company. This would also lead to a substantial derisking of the scheme's assets and liabilities.

   Deloitte has considerable experience in structuring and executing liability management and derisking strategies, including bulk annuity transactions. For more information on these please refer to one of the contacts opposite.

For more details please contact:

Patrick Cosgrave
Director
T: +353 1 417 2422
E:pcosgrave@deloitte.ie

Paul Johnston
Senior Manager
T: +353 1 417 2482
E:pajohnston@deloitte.ie

Frank Cox
Senior Manager
T: +353 21 420 7805
E:fcox@deloitte.ie

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a private company limited by guarantee, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/ie/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu Limited and its member firms.

Deloitte's 1,100 people in Dublin, Cork and Limerick provide audit, tax, consulting, and corporate finance to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries, Deloitte brings world class capabilities and deep local expertise to help clients succeed wherever they operate. Deloitte's approximately 170,000 professionals are committed to becoming the standard of excellence.

This publication contains general information only, and none of Deloitte Touche Tohmatsu Limited, Deloitte Global Services Limited, Deloitte Global Services Holdings Limited, the Deloitte Touche Tohmatsu Verein, any of their member firms, or any of the foregoing's affiliates (collectively the "Deloitte Network") are, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your finances or your business. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser. No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this publication.

© 2011 Deloitte & Touche. All rights reserved

GREAT PLACE TO WORK® 2011 Best workplaces Ireland
in association with Irish Independent

FSC Mixed Sources
Product group from well-managed forests, controlled sources and recycled wood or fiber
Cert no. SGS-COC-003235
www.fsc.org
© 1996 Forest Stewardship Council