



Pensions levy - practical issues

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What's the problem?



- Calculate 0.6% of assets and pay it over
- DC: if necessary, deduct from units
- DB: if necessary, reduce members' benefits by 0.6%



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But when you start digging...

...it's complicated!





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Two aspects

1. Calculation and payment



2. Passing the levy on to members





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Calculation and payment

- General valuation date is 30 June 2011
- Trustees may choose between either 30 June 2011 or the accounting date under the following conditions
 - Scheme is a defined benefit scheme (per PB register)
 - where the assets are not held under contracts of assurance
 - the accounts are prepared to an appropriate accounting standard
- To be paid by 25 September in electronic form



Conclusions

- DC schemes – no choice, must use 30 June value
- DB schemes –
 - Where assets are managed by life assurance company, life assurer is obliged to pay levy and use 30 June value
 - Where assets are managed elsewhere, trustees may be able to use the last accounting date (not schemes with less than 100 actives & deferreds where short form TAR is prepared)
 - Trustees would probably have a fiduciary duty to find out which date produces the lowest levy payable for ‘non-insured’ assets
 - Can choose differently each year



Assets

‘Assets’ means all property, including investments, deposits, debts and contracts of assurance, held for the purposes of a scheme, other than excluded assets.

What’s included

- Assets with investment managers
- Cash in trustee bank accounts
- Cash in transit, e.g., money sent to or from investment managers

What’s excluded

- Assets relating to members whose employment while a member is and always was exercised outside the State
- Annuities
- Death benefit monies arising from life assurance contracts
- Contingent assets
- Schemes in wind-up where the employer is insolvent
- Unfunded public sector schemes!



Some issues – DB schemes

- For ‘non-insured’ DB assets, which date to use?
- Audited accounts, or will draft accounts do?
- What about current assets & liabilities, e.g.:
 - June contributions not yet received
 - Payment made in June to bank for July pension payments
 - Monies still owed to a member who left/retired in June
 - Inter-scheme balances, etc?
- How to value certain illiquid or unmarketable assets?
- Levy does not apply to assets held in respect of overseas employees – need actuarial calculation
- If earlier date used, note that same date must be used for non-insured money-purchase funds under main trust, e.g., AVCs, DC funds in hybrid scheme



More issues – DB schemes

- Will employer pay, either by special contribution or adjustment to long-term funding rate? What do scheme rules say?
- If payable from fund, need to decide where to take money from to pay levy
- Validation and sign-off of calculation: audit trail
- Electronic payment through Revenue Online Services (ROS)
- 25th September 2011 is a Sunday, so realistic deadline is Fri 23rd!
- IAS 19 / FRS 17 treatment for DB schemes:
 - Reduction in expected return on assets for the year (affects P&L)
 - May be corresponding negative past-service cost if levy passed on to members



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Some issues - DC schemes

- Unit price movement since 30 June could result in more/less than 0.6% of units being encashed
- Do routine transactions have to be suspended during a window when the levy is being calculated?
- What to do with members who retired before 30 June whose benefits are not yet processed?
- Who pays for administrative costs of applying unit deductions and updating unit records for each active & deferred member?
- Need to amend future Statements of Reasonable Projection to take account of levy? (also applies to AVCs under DB schemes)



2. Passing levy on to members

Before trustees do so:

- Ask sponsoring employer to pay levy?
- Assess administrative cost of so doing – is it worth it?
- PR considerations; complexity of communications
- Withhold levy from benefits until decision is made?
- If surplus exists (even in a DC plan there may be surplus employer units), obtain legal advice?
- Consistency of treatment of DB and DC employees
- Easier to roll it all in to a funding proposal?
- PAOs: can non-member spouse's benefits be reduced?



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Passing levy on

DC : relatively straightforward

DB :





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The Acme Pension Scheme

Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present value
factor of 15

= €750,000

Anne Droid, active

€60,000 x 25/60^{ths} (= €25,000) x
present value factor of 10

= €250,000

Total: €1,000,000



Assets:

Fund: €1,000,000



The Acme Pension Scheme

Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present
value factor of 15

= €750,000

Anne Droid, active

€60,000 x 25/60^{ths}
(= €25,000) x present
value factor of 10

= €250,000

Total: €1,000,000

Levy:

X 0.6% = €4,500

X 0.6% = €1,500

Total = €6,000



The Acme Pension Scheme

Liabilities:

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= €250,000

Total: €1,000,000

Levy:

X 0.6% = €4,500

X 0.6% = €1,500

Total = €6,000

Options:

1. Deduct €4,500 from pension → €45,500 for next year
2. Deduct €300 p.a. from pension for ever → €49,700 p.a
1. Deduct €1,500 from pension @ NRD in 1st year
2. Deduct €150 p.a. from pension @ NRD for ever



The Acme Pension Scheme

Liabilities:

Ian Clover, pensioner
 €50,000 p.a. x present value factor of 15
 = €750,000

Anne Droid, active
 €60,000 x 25/60^{ths}
 (= €25,000) x present value factor of 10
 = €250,000

Total: €1,000,000

Levy:

X 0.6% = €4,500

More likely

X 0.6% = €1,500

Total = €6,000

Options:

1. Deduct €4,500 from pension → €45,500 for next year

2. Deduct €300 p.a. from pension for ever → €49,700 p.a

1. Deduct €1,500 from pension @ NRD in 1st year

2. Deduct €150 p.a. from pension @ NRD for ever



Years 2-4

Ian Clover

Deduct another €300 p.a. for each year so that by end of year 4, pension has reduced by 2.4% to €48,800 p.a. – stays at this level for life.

Anne Droid

Each year, she will accrue an extra year's pension and may receive a salary increase. The amount to be deducted to pay the levy will increase.



Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present value
factor of 15

= €750,000

Anne Droid, active

€60,000 x 25/60^{ths} (= €25,000) x
present value factor of 10

= €250,000

Total: €1,000,000

Assets:

Fund: €800,000



Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present value
factor of 15

= €750,000

Anne Droid, active

€60,000 x 25/60^{ths} (= €25,000) x
present value factor of 10

= €250,000

Total: €1,000,000

Assets:

Fund: €800,000

Levy:

Levy is now 0.6% of
€800,000

= €4,800

instead of €6,000



Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present
value factor of 15

= €750,000

Anne Droid, active

€60,000 x 25/60^{ths}
(= €25,000) x present
value factor of 10

= €250,000

Total: €1,000,000

Option 1:

X 0.6% x 80%
= €3,600

X 0.6% x 80%
= €1,200

Total = €4,800



The Underfunded Acme Pension Scheme

Liabilities:

Ian Clover, pensioner

€50,000 p.a. x present value factor of 15
= €750,000

Anne Droid, active

€60,000 x 25/60^{ths}
(= €25,000) x present value factor of 10
= €250,000

Total: €1,000,000

Option 1:

X 0.6% x 80%
= €3,600

X 0.6% x 80%
= €1,200

Total = €4,800

Option 2:

X 0.6% x 100%
= €4,500

X 0.6% x 20%
= €300

Total = €4,800

100% coverage for pensioners

20% coverage for actives



Considerations

- If scheme is in wind-up / risk exists that it may wind up / benefits for actives might have to be reduced as part of a funding proposal → probably more equitable to allocate levy in accordance with Pensions Act priorities. If not, actives & deferreds will end up paying for pensioners.
- If solvency level is likely to recover, or strong employer covenant exists, more equitable to allocate evenly.
- Pension increases are not a priority liability, so solvency level coverage for membership categories needs to be adjusted accordingly.



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Other issues to consider

- Use MFS basis or long-term funding basis to determine level of reduction required?
- Reduce pensions in payment now, or wait until next increase due?
 - e.g., if increase of 2.5% due in December, give 1.9% instead
- For actives and deferreds, apply 4 separate reductions, or one reduction at the end of 4 years? What can administrator handle?
- For actives and deferreds, should the reduction be a lower revaluing amount, or a higher fixed amount?
- May need to adjust reduction for varying solvency levels over 4 years
- Legal issues: (1) advice (2) deed of amendment
- Member communications
- Show levy deduction on annual benefit statements, or just put in a note to the effect that benefit will be reduced?



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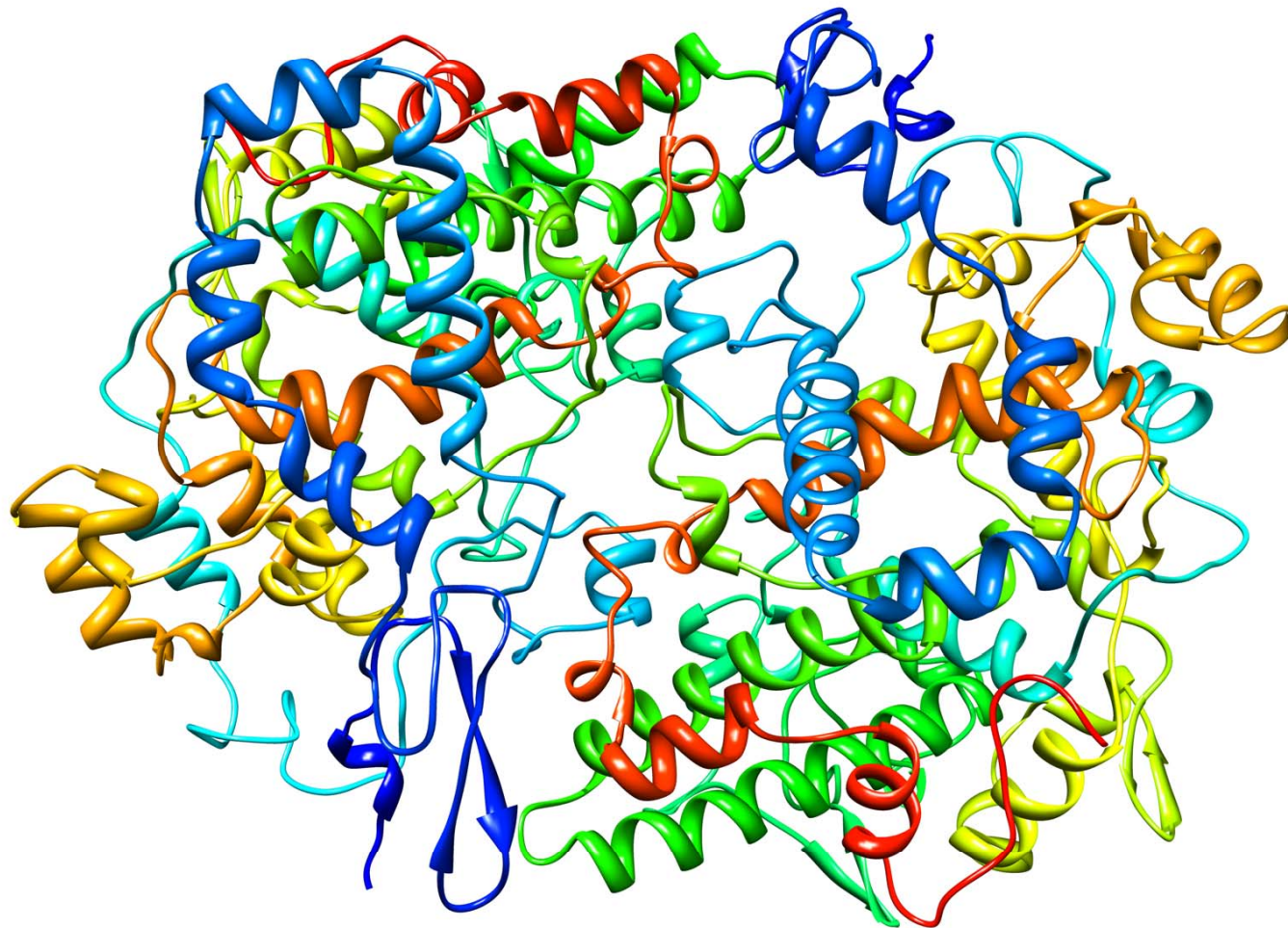
Summary for trustees

- Make sure you agree with your administrator who is making the return and how the levy is being calculated (incl. which date)
- Ask employer to pay, setting out issues
- Agree source of funds for levy payment
- Agree with actuary, legal adviser and administrator how to pass on levy to members
- Interim deduction until decided?
- Arrange deed of amendment
- Agree member communications



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All clear now?



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