Meeting the Funding Standard -- using a Section 50 application

Elma Fox

Independent Trustee Company

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The Basics

- The scheme is underfunded and/or
- The employer cannot or will not increase contributions to the levels required.
- Increased employee contributions would be insufficient.
- The trustees and employer don't want to wind up.
    - Something has to change.

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What does the employer do?

The employer will have their actuary work out some possible solutions:

- Cease to future accrual
- Cap salaries
- Reduce/remove pension increases
- Reduce existing benefits
- Wind up the scheme
  - The financial and HR implications of these changes will be considered.

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What does the employer do next?

- The options are presented to the trustees – usually with one preferred option.
- The employer will often present a wider business or financial case for:
    - the need for change
    - their preferred option
    - the implications if a change isn't made

What does the trustee do now?

The trustees need to consider the proposals taking into account input from:

- Sponsoring Employer
- Actuary – Scheme and Employer
- Legal Advice – Scheme and Employer
- Members – Active, deferred, pensioner, Trade Unions
- Pensions Board

Sponsoring Employer

- Do the trustees need an accountant to assess the employer's financial position?
- Is the financial situation as presented?
- Can future contributions be afforded?
- How can future contributions be structured?
- Contingent asset – is there a free asset available?
- Strength of the employer's commitment to the scheme?

Actuarial Input

- Is a reduction necessary?
- What is the impact on different categories of members?
- Should other changes be considered?
- What level of contributions will be available into the future?
- Do the proposed changes take account of the risk reserve requirement?

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Legal Advice

- Trustees powers under the deed - amendment, contributions, notice periods, wind up
- Section 50 Prescribed Guidance – member consultation, demand full contributions, take advice
- Treatment of different categories of members
- Consider – contractual contribution rights, extended notice periods, non-wind up periods, use of contingent assets

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Member Communications

- Employer update – financial/business update, cost of pension benefits, proposed changes, future benefits
- Trade Union negotiations
- Trustee communication – Consultation for 1 month, plus mixture of presentations, member meetings, individual communications
- Trustee consideration of member observations and feedback

Other Considerations

As part of the S.50 decision making process issues outside the scheme can arise:

- Future Benefits – DC? Level of Contributions? Risk Benefits?
- Employment Contracts or Benefit Promises
- Future Payments – Should the employer position improve can additional funds be made available – how? To the scheme? To the new scheme? Directly to members?

What Next?

Having taken into account all the advice and information the trustees decide to make a section 50 application. What now?

1. The actuary will draft the application.
2. Review by legal advisor, employer & trustee.
3. Submission to Pensions Board with supporting documentation and in most cases a Funding Proposal.
4. If accepting the application for S.50 direction and Funding Proposal – The Board will do together.

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In Conclusion

- Start the process early
- Allow time of taking and considering advice and member feedback
- Communicate with members as soon as possible
- Take account of all available information but focus on what is relevant to scheme