

## PENSIONS LEVY

The Finance (No.2) Act, 2011 giving legal effect to the pensions levy announced in the Jobs Initiative has been signed by the President and is now law. There has been plenty of media discussion on the levy and calls for the constitutionality of the levy to be tested. However, unless challenged in the courts, the levy will go ahead as set out.

### TECHNICAL DETAILS

- The levy is 0.6% of the market value of assets.
- The levy is payable for four years.
- There is one valuation date each year, June 30. Defined Benefit scheme trustees may instead choose the last day of the preceding scheme year if audited accounts are prepared at a different date. However, if the assets are held under a contract of assurance then June 30 must be used.
- The payment date each year is September 25.
- The levy applies to occupational pension schemes and personal retirement bonds. It also applies to personal pensions and Personal Retirement Savings Accounts (PRSAs) which have not vested (cash has not already been taken from the personal pension or PRSA).
- It also applies to annuities that have been bought in the trustees' name.
- The levy does not apply to Approved Retirement Funds (ARFs, AMRFs), vested PRSAs and vested personal pensions, or annuities bought in the pensioner's name.
- The levy does not apply to occupational pension schemes to the extent that they provide retirement benefits outside the State for members who were never Irish-resident, or where the trustees have passed a resolution to wind up the scheme and the employer is insolvent.
- For all assets under contracts of assurance, the life assurance company is responsible for settling the levy. Where your assets are invested with the investment arm of a life assurance company (e.g. Aviva, Canada Life, Irish Life, New Ireland, Zurich etc.), the levy may be deducted automatically from scheme funds on June 30.
- In most other cases, the trustees are responsible for settling the levy.

## DEFINED CONTRIBUTION SCHEMES

Most defined contribution schemes will stipulate that tax and duties are payable from members' funds. Although trustees should consider requesting that the employer meets the cost, it seems likely that the cost will be borne by the members. Trustees and administrators will need a procedure to ensure that any transfer payment that is made out of the scheme between the valuation date and the payment date is reduced by the levy (assuming the employer is not going to pay the levy) and should ensure that the approach adopted is communicated clearly to members.

## DEFINED BENEFIT SCHEMES

The question of who carries the cost is more complicated in a defined benefit scheme. Most trustees will ask the employer to carry the cost of the levy but the extent to which trustees can insist will depend on the rules of the scheme.

Where it is agreed that the employer will meet some or all of the cost, the employer could simply make a special contribution equal to the amount of the levy. Alternatively, the levy could be deducted from the assets of the scheme and the employer's ongoing contributions adjusted to take account of the levy. Where Funding Proposals are in place or agreed, positive experience since the agreement may mean that the current level of contributions can be maintained.



The Finance (No. 2) Act 2011 allows trustees the option to cut member benefits to fund the levy. Where it is agreed between the trustees and the employer that the members will meet some or all of the cost, there are a number of options available. A special contribution from members or a deduction from DC/AVC assets within the trust is possible. Where Section 50 reductions are already being considered, the cost of the levy could be included in those considerations but it is most likely that some form of reduction in the level of accrued benefit will be used.

## EFFECT OF REDUCING BENEFITS IN DEFINED BENEFIT SCHEMES

If it is decided to reduce benefits for members, whether the scheme is in surplus, just solvent or in deficit will be relevant. Each member's benefits cannot be reduced by more than 0.6% of the assets attributable to that member's liabilities.

### IN SURPLUS

It is more probable that the fund will absorb the levy rather than that benefits will be reduced. However, even if benefits are reduced, the levy on the surplus element of the fund will be deducted from the surplus. Accrued benefits would be cut by 0.6% of the benefit – total just under 2.4% of the benefit over the four years. The levy on the surplus element will not reduce benefits further.

### SOLVENT

If the scheme is just solvent, then the expectation is that accrued benefits would be cut by 0.6% for each year – total just under 2.4% over the four years.

### IN DEFICIT

For schemes in deficit, the levy will be less than 0.6% of the value of the liabilities so, in aggregate, benefit reductions of less than 0.6% each year will be required. The wording of the Finance (No. 2) Act is quite vague around how benefit reductions can be shared – trustees should seek legal advice to ensure they are complying with the law.

It seems that the two main options available will be the 'Share of Fund Approach' and the 'Priority Order Approach'. The Share of Fund Approach allows each member to meet their share of the levy based on their proportionate share of the liability in the scheme. The liabilities could be calculated on any number of different actuarial bases including the long-term funding valuation basis, a best estimate basis or the Funding Standard basis.

The Priority Order Approach allocates the levy to individual members based on the proportion of the assets that would be available to provide benefits for that member on wind-up taking into account the priority order under the Pensions Act. For schemes without guaranteed pension increases, this approach would put more of the burden on pensioners since they have a priority call on the assets in the case of a wind-up. Active and deferred members will receive a cut in their accrued pension.

### PENSIONERS

For pensioners, the cost could either be met by a sizeable reduction (e.g., 15%) in the pension in the year the levy is payable only or a small reduction (e.g., 0.6% for each year the levy is payable) in the pension for life.



## IAS 19 – EMPLOYEE BENEFITS

The International Accounting Standards Board has published amendments to IAS 19 which are particularly relevant to companies with defined benefit schemes who report under IFRS. The amended version of IAS 19 comes into effect for financial years beginning on or after 1 January, 2013. Earlier application is permitted.

The amendments focus on three key areas:

- recognition – the elimination of the option to defer the recognition of gains and losses
- presentation – the elimination of options for the presentation of gains and losses
- disclosures – the improvement of disclosure requirements that will better show the characteristics and risks arising from defined benefit plans.

The amendments will result in an increase in balance sheet volatility for those who opted to use the corridor approach (delayed recognition of actuarial gains and losses) and will result in an increase in the profit and loss element of the total pension expense by effectively reducing the expected return on assets to the discount rate.

If you want further information, please contact your usual Willis consultant.

## OTHER CONSIDERATIONS

When the approach has been agreed between the trustees and the employer, it will need to be carefully documented and communicated. Whilst the levy must be paid by September 25, the approach as to who will ultimately pay for it does not require to be decided upon by that date.

The accounting impact of the levy will depend on the approach adopted.

Knock on effects of the levy could include a delay in capital funding of deficits until after 2014, an increase in the purchase of annuities in the member's name and an increase in wind-ups.

## NEXT STEPS

- Administrators will need to obtain a fund value as at June 30 (or the previous accounting date if accounts have been prepared).
  - The trustees will need to authorise payment of the levy by September 25 so as to ensure that no penalties apply.
  - Any liquidity issues for the fund regarding payment of the levy will need to be addressed.
  - Trustees of DC schemes need to consider whether to request the employer to pay for the levy.
- A communication to members will be required explaining the effect of the levy.
  - Any transfer payments out of the scheme may need to be adjusted to reflect the levy where the transfer occurs before the levy payment has been made in the year.
  - Trustees of defined benefit schemes will need to engage with the employer on how the levy will be paid.
  - If benefits are to be reduced in a defined benefit scheme, the method of doing so will need careful consideration given that different methods can affect one category of member more than another e.g., pensioners could be impacted more than active or deferred members or vice versa.
  - Changes to scheme documentation may be needed to reflect adjustments in benefits.
  - Changes may also need to be made to annual benefit statements and statements on leaving or retiring.



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