

PREMIER PENSIONS MANAGEMENT

LEGISLATION UPDATE : 03/07

Trust or Contract Based Defined Contribution Scheme?

Following the introduction of A-Day legislation last April which removed many of the advantageous rules for a trust based scheme, many companies have been reviewing their Defined Contribution (DC) arrangements to ensure they are operating as cost effectively and efficiently as possible and meet the current and future needs of their type of business/employees.

In summary, there are two choices for DC provision, available to companies as follows:

- (1) A trust based scheme, which requires a trustee board to manage the operation of the scheme, or,
- (2) A contract based scheme with an insurance company, which is an individual contract between the insurer and the employee that the Company contributes to.

These contracts have now become more commonplace. Also, the quality of the IT systems and support provided has seen substantial improvements over the last few years and is often superior to that used by Third Party Administrators operating trust based dc plans.

If the Company is setting up a brand new arrangement and has no legacy schemes to consider, it is difficult to justify a trust based scheme. This is because of the associated costs of setting up and running the trust, finding trustees, preparing accounts etc. In contrast, the relatively simple solution of setting up a contract based scheme where the only real obligation of the Company is to deduct and pay contributions monthly is becoming more popular with a number of employers.

However, where a Company already has a trust based scheme, either a Defined Benefit or Defined Contribution (or both) the decision making process is much more complex.

To try and set out all the pro's and con's for Trust Based or Contract Based DC arrangements would require a comprehensive paper. Premier Pensions Management updates are designed to be short and concise and therefore, the objective of this update is set out the high level issues which Companies should be considering when reviewing their current arrangements:

- Current status of Trust Based Scheme and Trustee Board
- Current funding implications of Trust Based Scheme
- Company's overall pension strategy
- Financial strength of Company
- Size of Company
- Type of Company
- Employee expectations
- Employee financial awareness
- Employee turnover
- Administration and investment costs
- IT literacy of staff and employee on line access
- Governance
- Communication

- Projections at retirement
- Legislative requirements
- Provision of Financial Advice
- Payroll capability

Each one of these topics needs to be considered (some will only be second order considerations), and the weighting given to each will depend on the Company priorities. Nevertheless, all will play a part in ensuring that the pension provision is delivered efficiently and cost effectively for your organisation.

It is possible the decision making process will lead to a Trust based scheme being wound up. This would require a further set of considerations in addition to the above.

The Pensions Regulator has recently entered into consultation on contract based schemes. Because of this some Companies have decided to wait for the outcome of the consultation before deciding whether it wishes to pursue a contract based route for the future. For some Companies, reviewing the position now and implementing changes is essential, irrespective of any changes the Regulator may put forward.

The subject is certain to remain topical over the next few months as “de-risking” of pension liabilities and minimising the Company’s long term exposure to fiduciary responsibilities continues to be a key pension objective. At Premier Pensions Management we have significant experience with both trust based and contract based schemes and we have used this to help our clients through the decision making process and, where appropriate, assist in implementing any changes.

If you would like more information on how we can assist your Company in conducting a review of your current arrangements please contact Paul Couchman.

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This update includes general information and cannot be relied upon for individual schemes issues. You should contact your adviser or Paul Couchman at Premier Pensions Management Ltd, Capital Business Centre, Units 14 & 15, 22 Carlton Road, South Croydon, Surrey, CR2 0BS. DL: 020 8916 2129. Email: paul.couchman@premierpensions.co.uk, if you require definitive advice