

PREMIER PENSIONS MANAGEMENT

LEGISLATION UPDATE : 8/05

Statement of Funding Objectives (SFO)

The new SFO comes into force with effect from 23 September 2005. All Pension Plan Valuations after this date will have to follow the new funding requirements. Valuations effective prior to this date can be completed on the existing Minimum Funding Requirement (MFR).

This PPM update gives you an overview of the legislation and the issues Companies and Trustees will now have to consider.

- The SFO will be determined for each Plan by the Trustees.
- This requirement is subject to the Trustees having taken actuarial advice and consulted with the employer.
- The assumptions must be “prudent” and the Trustees should be able to demonstrate this. However, “prudence” is not defined by the legislation. There is, however, some detail on the process Trustees should follow to make “prudent” choices.
- The SFO must be set against the cost of buying immediate and deferred annuities, although it is highly likely that Plans will adopt a weaker basis for funding.
- The employers covenant will need to be considered in detail before setting the SFO. This creates a bit of a conundrum. If a Plan is under funded and there is a strong covenant from the Company, the Trustees will be obliged to set the SFO to take advantage of this so that more contributions are paid in to the Plan now, to improve member security. However, if the Company has a weak covenant then the Trustees will also try and obtain more contributions from the Company to try and improve security for members in the short term in case the Company goes into liquidation.
- The Trustees must specify how the SFO will be met through a Statement of Funding Principles. It is suggested this is integrated with the Statement of Investment Principles to form one document.
- If there is a deficit, a Recovery Plan must be prepared and sent to the Regulator.
- An annual Actuarial report must be prepared to update the liabilities unless the Plan has annual valuations.
- The Regulator has the power to intervene if there is a failure of the requirements, although it is only likely to be used to protect member’s benefits and the Pension Protection Fund.
- The results of the SFO and the Trustees recovery plan must be issued to member’s each year, starting from April 2006. SFO valuations not due until post April 2006 must show the MFR position. This needs to be communicated carefully as the MFR position is likely to show the Plan as being better funded than the SFO and may cause concern to members when the funding position “appears” to have worsened.

These brief bullet points are designed to raise awareness of the key points now in order to aid valuation planning. There is much more detail in the legislation which we are happy to discuss with you.

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