TRAVERS SMITH

What's happening in Pensions

Issue 41 *September 2013*

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Tax legislation

Finance Act 2013

The Finance Bill has received Royal Assent. The Act includes provisions on the following pensions-related matters. Except where otherwise stated, the changes take effect from 6 April 2014.

Finance Act 2013:
http://www.legislation.gov.uk/ukpga/2013/29/contents/enacted

- The reduction of the annual allowance from £50,000 to £40,000.
- The reduction of the lifetime allowance from £1.5 million to £1.25 million. (If a member dies before 6 April 2014 but death benefits are not paid until on or after that date, the lifetime allowance at the time of the member's death (ie, £1.5 million) will apply.)
- The introduction of "fixed protection 2014" in relation to the reduced lifetime allowance. (The proposed new individual protection regime is not covered: this will be included in the 2014 Finance Bill.)
- Amendments to correct defects in the existing fixed protection legislation (some with retrospective effect).
- Amendments to the Finance Act 2004, effective from 6 April 2013, to allow the ending of bridging pensions at any time between age 60 and the member's state pension age without making an unauthorised payment. (Currently, there is an unauthorised payment if a bridging pension ends after age 65.) We will shortly be issuing a briefing note on bridging pensions and rising state pension ages.
- Increasing the income drawdown limit for registered pension schemes to 120% of the value of an equivalent annuity for members of any age, in relation to drawdown years beginning on or after 26 March 2013.
- Removing unintended tax advantages from employer contributions to the pension arrangements of an employee's spouse or family member.
- Tightening of restrictions on overseas transfers (in force since 17 July 2013).

Fixed protection 2014
Regulations came into force on 12 August 2013 containing the registration formalities for fixed protection 2014. Applications must be received by 5 April 2014.

Online and paper registration forms are now available. Member guidance and an online tool for members are also available.

Regulations:
http://www.legislation.gov.uk/uksi/2013/1741/contents/made

Forms:
http://www.hmrc.gov.uk/pensionSchemes/fp14online.htm

Fixed protection (2012)
Amending regulations make corrections and clarifications to the fixed protection (2012) legislation. For example, they clarify that GMP revaluation does not result in a loss of fixed protection. They also allow members of relieved non-UK pension schemes to register retrospectively for fixed protection (2012) by 5 April 2014.

Regulations:
http://www.legislation.gov.uk/uksi/2013/1740/contents/made

Reporting to HMRC
Regulations impose additional reporting and information requirements from 12 August 2013:

Regulations:
http://www.legislation.gov.uk/uksi/2013/1742/contents/made

- on schemes and individuals – to provide information to HMRC in respect of members who have registered for fixed protection 2014;
- on schemes – to make an event report when issuing a statement to a member because their pension input to the scheme has exceeded the annual allowance; and
- on individuals who are not UK resident and who make a request to transfer to a QROPS – to notify the scheme when they ceased to be resident; and on schemes – to make an event report to HMRC about this.

Contribution refunds: former protected rights
Amending regulations provide that sums representing age-related rebates paid by HMRC and employers' minimum payments recovered from employees, in both cases paid to formerly contracted-out DC schemes, are "member's contributions" for the purpose of the limit on short service contribution refunds from registered pension schemes.

Regulations:
http://www.legislation.gov.uk/uksi/2013/1818/contents/made

These amounts are therefore included in the maximum authorised lump sum that may be paid as a short service refund. HMRC had previously expressed the view that such sums were already included (see **WHiP Issue 35**) but the law was not clear.

Scheme rules and the Pension Schemes Act 1993 will still determine how much a scheme must pay by way of refund, which might not include all these sums. Under that Act, when it applies, a refund must include *"contributions made to the scheme by or on behalf of the member on his own account"*. It is not clear that this has the same meaning as HMRC ascribed to the similar provision in the tax legislation. The DWP has not commented.

Asset-backed contribution guidance
HMRC has published a draft guidance note on asset-backed contributions designed to reflect the law on up-front tax relief as amended by the Finance Act 2012 (see **WHiP Issue 35**). The draft note considers arrangements involving contributions paid by an employer to its pension scheme so that the scheme may require an interest in a special purpose vehicle that will hold assets acquired from the employer. It is based on a previous draft note, covering the draft legislation, that was issued in June 2012 (see **WHiP Issue 34**). Feedback is welcomed.

Draft Guidance:
http://www.hmrc.gov.uk/pensionschemes/abc-guidance.pdf

Mergers and other bulk transfers: annual allowance charge
HMRC has issued a statement regarding annual allowance charges on mergers and other bulk transfers where the receiving scheme provides benefits for a member that are equivalent to those under the transferring scheme but which are worth more than the amount transferred in respect of them.

HMRC statement:
http://www.aca.org.uk/files/Annual_Allowance_and_DB_scheme_transfers_-_interim_announcement_from_HMRC-16_July_2013_-20130717160922.pdf

Concerns have been raised that, under the current legislation, there is a pension input if an "underfunded" transfer is made from one scheme to another, and this has been an obstacle for some scheme mergers and bulk transfers.

HMRC intends to legislate, with effect backdated to 6 April 2011, to provide that pension input amounts should not arise in situations where the following criteria are met.

- There is a block transfer of a group of members from one registered pension scheme to another as a result of an employer rearranging its pension schemes or as part of a business transaction.
- The member's retirement benefits in the receiving scheme as a result of the transfer will be the same in principle as would have applied under the transferring scheme if the rearrangement of pension schemes or business transaction had not taken place. This requirement may be expressed using a value test to ensure that some variations in benefit format can be accommodated but this is still being finalised and further detail will be provided by the draft Order.

Marriage (Same Sex Couples) Act 2013

Marriage (Same Sex Couples) Act 2013: http://www.legislation.gov.uk/ukpga/2013/30/contents/enacted

The Marriage (Same Sex Couples) Bill has received Royal Assent. It is expected to come into force to permit same sex marriages from summer 2014.

The Act gives same sex spouses the same status as opposite sex spouses for most purposes. For pensions purposes, however, the Act treats same sex spouses in the same way as civil partners. It therefore allows the restriction of same sex spouses' survivor benefits to benefits based on pensionable service since 5 December 2005. The exceptions to this are pre- and post-1997 contracted-out rights. In particular GMP rights are extended to same sex spouses in the same way as applies to civil partners (ie, they are treated as widowers).

If the Employment Tribunal was right in *Walker v Innospec* (see **WHiP Issue 38**) about the December 2005 restriction being ineffective for civil partners then the restriction in respect of same sex partners would seem to be similarly ineffective. That decision is being appealed. A late amendment to the Bill commits the Government to reviewing and reporting on this aspect of the legislation by 1 July 2014, looking in particular at the costs of full equalisation. The Act includes a power to make regulations to eliminate or reduce this discrimination if the Secretary of State thinks that the law should be changed.

Bridging pensions

Regulations: http://www.legislation.gov.uk/uksi/2013/1754/contents/made

Regulations have been laid, coming into force on 1 October 2013, permitting some amendments of pension schemes' bridging pension (or similar) rules by resolution, in the light of rising state pension ages. We will shortly be issuing a briefing note on this topic.

Disclosure of information

Consultation response: https://www.gov.uk/government/consultations/occupational-and-personal-pension-schemes-disclosure-of-information-regulations-2013

The Government has issued its response to the consultation on consolidating and improving disclosure of information requirements for occupational and personal pension schemes (see **WHiP Issue 38**). The changes will now take effect from 6 April 2014, not 1 October 2013. Regulations will be laid shortly: no new draft of the regulations has been published at this stage.

The response confirms that there will be no principles-based regulation for the time being. Best practice guidance will be explored with the Pensions Regulator, FCA and pensions industry.

The confirmed proposals are as follows.

- Electronic disclosure using a website and email alerts is currently permissible only for matters covered by the disclosure of information regulations. Some other regulations that require disclosure will be brought within the electronic disclosure regime (but will remain separate from the disclosure regulations). They include disclosure in the following areas:
    - early leaver statements
    - transfer values
    - contracting-out elections
    - winding-up notices, reports, etc
    - pensions and divorce (earmarking and pension sharing)
    - appointment of an independent trustee
    - consultation by employers over listed changes
    - notices about payments to employers
- Annual reports for multi-employer schemes will have to list "*the 100 largest investments by value held by the scheme ... stating what percentage of the resources of the scheme each such investment represents*", identifying which are employer-related and (if there is more than 5% employer-related investment) listing the relevant investments and the employer concerned. For these purposes, connected or associated parties do not count.
- There will be a new requirement for DC schemes to tell members about "lifestyling" arrangements for their investments (including "target date funds") both as part of the basic scheme information and again before automatic switching starts to apply (eg, with an annual statement). The information to be given includes a summary of the advantages and disadvantages of lifestyle funds.

This requirement will now apply between five and 15 years before retirement – earlier than originally proposed (as well as being part of the basic scheme information).

- Only basic information about transfer options will need to be provided as part of the basic scheme information, with more detailed information to be made available on request.
- There will no longer be an obligation to tell members what their normal pension age is but there will be a new obligation to tell them when benefits are payable.
- Information about material alterations to basic scheme information will have to be given as soon as possible after the decision is taken and no later than three months after the decision. Currently, this must be done before the change takes effect, where practicable, and not later than three months after that.
- DB benefit statements will no longer be required to use a specific scheme pension age; instead they can use any date specified by the trustees or agreed with the member. Trustees will also no longer have to use a calculation date within one month of the statement.
- When issuing statutory money purchase illustrations, schemes will no longer have to assume that an index-linked annuity with an attaching dependant's pension will be purchased. If a scheme changes its illustration assumptions, it will have to inform the member and explain the effect on the illustration. Illustrations will be allowed to include expected future voluntary contributions (for both active and, if they are expected to pay any such contributions, for deferred members).
- Members retiring early will have to be given information about their benefits before their pension starts or within one month thereafter (currently two months).
- DC members who are reaching pension age will have to be sent information about retirement options etc at least four (currently six) months in advance.
- There will no longer be a requirement to tell members each time a "real time" online statement is updated. Once every 12 months will suffice.
- Information about the constitution of the scheme, which must be made available on request, need not be given more than once in any 12 month period.
- There will be a new overarching requirement for any information disclosed to be accompanied by a statement giving an address from where further information can be obtained.
- The disclosure obligations for personal pension providers are to be significantly reduced, reflecting the fact that the FCA also imposes similar obligations.

Pension Protection Levy

PPF publications

The PPF has published the following, in connection with the 2013/14 pension protection levy invoices that it will issue to schemes in early September 2013:

PPF website:
http://www.pensionprotectionfund.org.uk/levy/invoicing/Pages/invoicing.aspx

- A Guide to the Pension Protection Levy 2013/14
- Example levy invoices for various scenarios
- Updated FAQs

Experian appointed to replace Dun & Bradstreet

The PPF will use Experian in place of Dun & Bradstreet to provide insolvency risk (failure) scores for pension protection levy purposes for levy years from 2015/16 onwards.

Press release:
http://www.pensionprotectionfund.org.uk/news/pages/details.aspx?itemID=330

The PPF will work with Experian, with input from stakeholders, to create a bespoke model for calculating insolvency risk. It is intended that schemes and employers will have access to the new Experian failure scores from early 2014. There will be no changes to the levy methodology before 2015/16.

Pensions Regulator

Pension liberation: High Court case

The High Court is being asked to decide if *"a number of schemes"* suspected of involvement in pension liberation fraud are occupational pension schemes and so legitimate recipients of transfers from registered pension schemes.

TPR press release:
http://www.thepensionsregulator.gov.uk/press/pn13-24.aspx

The Pensions Regulator appointed Dalriada Trustees Limited as independent trustee of the schemes in question. Dalriada is arguing that the schemes are occupational pension schemes; the Regulator has been appointed by the Court to argue that they are not. The

hearing has been adjourned until the autumn.

Record-keeping
The Pensions Regulator has published its annual record-keeping survey. It will publish results from its detailed review *"towards the end of the year"* and will update its record-keeping guidance to reflect the main findings.

Press release:
http://www.thepensionsregulator.gov.uk/press/pn13-26.aspx

DC governance: management committees
The Pensions Regulator has published *"Monitoring your pension scheme: Management committees for employers"*. This is a guide for employers offering a group personal pension or master trust who want to monitor and review their pension arrangements. It makes it clear that there is no duty to do so but suggests how to set up a management committee and on what it might focus. It also includes example terms of reference for such a committee.

TPR guide:
http://www.thepensionsregulator.gov.uk/docs/employer-management-committees.pdf

Lehman/Nortel: FSD priority

Case report:
http://www.supremecourt.gov.uk/decided-cases/docs/UKSC_2011_0261_Judgment.pdf

The Supreme Court has delivered its judgment in the Nortel/Lehman Brothers case on the interplay of the powers of the Pensions Regulator and insolvency law. The Court ruled that if the Pensions Regulator issues a financial support direction (FSD) against an insolvent company based on circumstances that pre-dated the insolvency, the pension scheme trustees and/or Pension Protection Fund (PPF) may enforce claims for liabilities arising from the FSD as unsecured creditors.

The High Court and the Court of Appeal had held that FSD liabilities would constitute expenses of a company in administration and would therefore be payable before the claims of other creditors (other than those holding fixed charges). The same priority would also attach to any contribution notice (CN) subsequently imposed on that company for failure to comply with the FSD. Both Courts had commented that this outcome was in some senses anomalous, as the debt imposed on an employer itself under section 75 of the Pensions Act 1995 when the employer becomes insolvent is treated as a provable debt.

The Lehman Brothers and Nortel administrators had argued that because any debt resulting from a FSD/CN would have arisen after the target companies had gone into administration, the debts would be irrecoverable (except in the very unusual circumstances where the insolvent company turns out to have sufficient assets to meet all its liabilities in full).

The Supreme Court, like the High Court and Court of Appeal, rejected this argument and agreed with the lower courts that FSDs should be enforceable, even if issued after a target company has become insolvent. But the Supreme Court held that FSD liabilities are enforceable as provable debts when a UK company is insolvent, rather than being treated as expenses of administration or liquidation.

FSD liabilities therefore have the same priority as unsecured, provable debts when FSDs are issued to insolvent UK companies by reference to circumstances that existed before the insolvencies started. This includes the liability under any CN issued against the insolvent company by the Pensions Regulator following failure to comply with the FSD.

It should be noted that, in both the Nortel and Lehman Brothers cases, FSDs were issued by reference to circumstances existing before the insolvencies began, under the so-called "look-back" provisions of the FSD legislation. The Supreme Court did not therefore need to address the situation in which an FSD might be issued against a company in insolvency proceedings by reference to circumstances or facts that post-date the insolvency.

Travers Smith acted for the trustees of the Lehman Brothers Pension Scheme.

VAT when employer pays scheme expenses

Case report:
http://curia.europa.eu/juris/document/document.jsf?text=&docid=139742&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=3342951

In *PPG Holdings BV*, the European Court has ruled that a Dutch employer which had established a pension scheme as a separate legal entity, as required by law, could treat as its input tax the VAT that it (rather than the scheme) paid on administration and investment management fees. This was on the basis that the liability was not passed on to the scheme. The Court ruled that such deductions can be made if the existence of a direct and immediate link with the employer's economic activities is apparent from all the circumstances of the transactions in question, as was the case here.

In the UK, an employer can treat as its input tax VAT paid on costs incurred establishing a scheme and on fees paid in relation to the day to day management or administration of the scheme (even if paid by trustees), but not (even if it pays them itself) on investment management fees. HMRC may now face VAT repayment claims by employers, with potential for four years' backdating. In practice, it is usually the trustees who pay the administration and investment fees.

In March 2013, the European Court ruled in the *Wheels (Ford) CIF* case (see **WHiP Issue 38**) that DB schemes' common investment funds are not "special investment funds", which are exempt from paying VAT on investment management fees. That decision did not address the position under DC pension schemes. Their VAT treatment under the fund management exemption is currently being litigated before the European Court in another case. That case should also decide whether fund management services could be exempt as payment processing (which is an argument still open to DB schemes too).

HMRC's current position on VAT for funded pension schemes is set out **here**.

Pensions Ombudsman

Application to Court to avoid Pensions Ombudsman

Case report:
http://www.outertemple.com/userfiles/Documents/PellFrischmannJudgment.pdf

The High Court has refused to strike out a claim that was brought to the Court in order to prevent the Pensions Ombudsman from dealing with the dispute (in the case of *Pell Frischmann Consultants Ltd and others v Prabhu and others*).

The dispute concerned an alleged promise of enhanced benefits, worth up to £520,000, which the employer claimed it had never approved. The member, Dr Lamb, engaged the scheme's internal dispute resolution procedure (IDRP) but the employer brought a claim in the High Court for resolution of the matter before that process was concluded. The trustees therefore terminated the IDRP process. Due to the commencement of the High Court proceedings, Dr Lamb was precluded under the Pension Schemes Act 1993 from referring his dispute to the Pensions Ombudsman.

The employer readily admitted that it had brought the claim in order to have the matter dealt with by the Court rather than by the Pensions Ombudsman. It wanted to test Dr Lamb's evidence under cross-examination and to claim costs from him if he lost. Dr Lamb claimed that this was an abuse of process, contrary to the Court's Civil Procedure Rules, and that the employer had failed to comply with a Court protocol on sending letters before claim and attempting to resolve matters out of court. On these grounds, he asked the Court to strike out the employers' claim.

The Court dismissed Dr Lamb's strike-out application, saying that:

- "*... the Court should not strike out save in the most clear and obvious cases and the fact that the issue of proceedings might have been motivated by an improper motive* [which the judge did not say it was] *is beside the point if the claimant has a genuine claim*".
- It was not an abuse of process for the employer to issue proceedings before the IDRP process had been completed. It might have been sensible for them to wait but, in any event, the employer would not have been bound by the outcome.
- The fact that the Civil Procedure Rules apply an overriding objective *"of enabling the court to deal with cases justly and at proportionate cost"* did not mean that cases should be struck out where an alternative procedure existed that was more in line with that objective.
- Striking out was not a sanction available to the Court for breach of the protocol. In any event, such a draconian course of action would not be justified.

Dr Lamb had sought, in the alternative, a prospective (or pre-emptive) costs order against the trustees or employer, under which his legal costs would have been paid by them. This was refused by the judge, because Dr Lamb was acting purely for his own benefit and there were no other grounds for granting such an order.

Annual report

Annual report:
http://www.pensions-ombudsman.org.uk/publications/docs/AnnualReport2012-13.pdf

The Pensions Ombudsman has published his 2012/13 annual report. Two points of interest are as follows.

- The Ombudsman has been piloting a new approach allowing investigators to issue pre-determination opinions in a formal document rather than a letter. These may be published in the future. The changes are now likely to be implemented permanently.
- There have so far been no complaints to do with pension liberation.

Determination: Ill health pension decision deferred

Determination:
http://www.pensions-ombudsman.org.uk/determinations/docs/2013/jun/po-667.doc

The Deputy Pensions Ombudsman found NHS Pensions responsible to Mr P E Hayes for maladministration in that it had:

- wrongly declined an ill health pension application on the grounds that it was too early to conclude that the member's incapacity was permanent; and
- failed to give adequate reasons for its decision.

The NHS pension scheme rules provide (broadly) for an incapacity pension to be paid to a member permanently incapable of working due to ill health. NHS Pensions is required to take into account (among other things) whether the member has received "*appropriate medical treatment*" and the rehabilitation it would be reasonable for him or her to undergo. "*Appropriate medical treatment*" is defined as medical treatment it would be normal to receive in respect of the incapacity but not any treatment that NHS Pensions considers it would be reasonable for the member to refuse.

NHS Pensions decided that while therapeutic treatments were ongoing, it was too early to say that incapacity was permanent. The Deputy Ombudsman, however, determined that it should have made a decision, on the balance of probabilities and based on their medical adviser's opinion on the likely efficacy of ongoing and potential treatment.

Mr Hayes had referred his claim back to NHS Pensions under the scheme's internal dispute resolution procedure. At the two stages of this process, NHS Pensions did consider the treatments he was undergoing and options for further medical intervention. Mr Hayes was suffering from a range of conditions and had rejected some surgical options because he did not want to take the risks involved. NHS pensions received medical evidence that the risks were small and so decided that it was not reasonable to refuse treatment. It did not, however, consider Mr Hayes' personal objections. The Deputy Ombudsman determined that NHS Pensions had failed to take account of the risks of proposed treatments from the particular member's perspective and this is what the scheme rule required.

The Deputy Ombudsman also determined that NHS Pensions had fallen short of the standards required for proper administration in failing to give adequate reasons. Ill health pension decisions require a level of reasoning "*towards the upper end of the spectrum*" to be given. The reasons given failed to address Mr Hayes' reasons for refusing treatment.

The Deputy Ombudsman therefore referred the decision back to NHS Pensions for reconsideration, based on the medical evidence available at the time of the original decision. In considering the matter, it simply needed to take a view on whether it was reasonable for Mr Hayes to refuse further surgery and then whether this would have made any difference to its view as to the permanency of his incapacity. She added: "*I would hope that they will provide full reasons in plain and simple language*". She also ordered £250 to be paid in recompense of the additional stress caused to the member.

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If you wish to discuss any points arising from this note, please speak to your usual contact in the Travers Smith Pensions team or to one of the Pensions partners: Paul Stannard, Peter Esam, Philip Stear, Susie Daykin and Daniel Gerring.

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