TRAVERS SMITH

What's happening in Pensions

Issue 10 *May 2009*

Budget and Finance Bill

Major changes are being made to the tax treatment of pension provision for individuals with annual income of £150,000 or more.

No higher rate tax relief for those earning £150,000 or more
The Government has announced its intention to restrict or remove higher rate tax relief for pension contributions for individuals with taxable income of £150,000pa or more with effect from 6 April 2011.

For those with taxable income of £180,000pa or more, only basic rate (20%) tax relief will be available. For those with taxable income between £150,000 and £180,000, there will be a tapering of relief down to 20%.

There will be a 50% income tax band from 6 April 2010 for taxable income above £150,000. See below for how tax relief will be restricted for 2010/11.

The Government has not yet announced the details of how it will restrict tax relief after 5 April 2011. There will be a consultation on this proposal and no draft legislation has yet been published. We expect that the legislation will curtail tax relief or impose a claw-back tax charge for employer's contributions and DB accruals, but this has not yet been formally confirmed.

"Anti-forestalling" provisions
Because the above change is not effective until 6 April 2011, high earners might try to make large pension contributions before then so as to get greater tax relief. The Government therefore proposes to include "anti-forestalling" provisions in this year's Finance Act, whereby 20% tax (2009/10; probably 30% in 2010/11) is charged on the individual to take back the benefit of higher rate tax relief in certain circumstances.

Please see the Appendix for details of how these provisions will operate.

Budget Note BN47:

http://www.hmrc.gov.uk/budget2009/bn47.pdf

Draft legislation and explanatory note:

http://www.hmrc.gov.uk/budget2009/pensions-1550-4.pdf

Technical Guide:

http://www.hmrc.gov.uk/budget2009/pensions-technical-1550.pdf

Guidance for Pensions Industry:

http://www.hmrc.gov.uk/budget2009/pensions-industry-1550.pdf

Guidance for Individuals:

http://www.hmrc.gov.uk/budget2009/pensions-individuals-1550.pdf

Adjustments to tax charges

Following the introduction of the new 50% higher rate tax band from 6 April 2010, regulations are expected to adjust charges applying to registered pension schemes that are linked to the highest rate of income tax.

Budget Note BN01:

http://www.hmrc.gov.uk/budget2009/bn01.pdf

Minimum increase to basic state pension

The Government's informal commitment to increase the basic state pension by at least 2.5% each year has been reaffirmed, even if there is still deflation in September. The Government forecasts 3% annual RPI deflation for September 2009 - the month used to calculate state benefit increases and by many occupational pension scheme rules.

Authorised payments regulations

Long-awaited HMRC regulations have been issued, relaxing the Finance Act 2004 regime in relation to trivial commutation, benefits overpaid in error, and benefits paid after a beneficiary's death. There are changes from the originally announced proposals (see WHiP Issue 3). The regulations have retrospective effect from 6 April 2006 except as regards small lump sum payments.

Regulations:

http://www.opsi.gov.uk/si/si2009/uksi_20091171_en_1

Small lump sum payments
The following, in broad terms, will be authorised payments under the Finance Act 2004 from 1 December 2009.

- Lump sum payments to members of up to £2,000 when the scheme has received an unexpected payment (but not a contribution) (an "accretion" in the language of the regulations) following the transfer out of a member or an annuity purchase. The lump sum must not exceed the value of the accretion and must be paid within six months of the accretion occurring (or by 1 June 2010 for accretions occurring before 1 December 2009).
- Lump sums of up to £2,000 to or in respect of members aged 75 or over who had previously been untraceable for at least five years. The lump sum must be paid within 12 months of discovering the member's whereabouts or learning of the member's death (or by 1 June 2010 if later).
- Trivial commutation lump sums of up to £2,000 under occupational pension schemes. However, the total commutation value of the benefits to which the member is entitled under the scheme and any schemes relating to the same employment must not exceed £2,000, the member must be aged between 60 and 74, and there must have been no transfer out within the last three years.
- For occupational pension schemes with at least 50 members, there are other possibilities for trivial commutation lump sums of up to £2,000 to be authorised payments without considering any other schemes. These may apply if:
    - the scheme was in existence on 1 July 2008; or
    - the arrangement is DB and the scheme's DB arrangements account for more than half of the scheme's assets; or
    - the aggregate amount of scheme assets held for the purpose of each of at least 20 members' arrangements exceeds £2,000.

All of these payments must extinguish the member's entitlement to benefits under the scheme or (if paid after the member has died) must represent all the sums held by the scheme in respect of the member.

Pensions paid in error
A payment of pension made in error that was intended to represent an authorised payment under the scheme rules will be authorised if the trustees believed that the recipient was entitled to it. (But see below for pensions mistakenly payable after the recipient's death.)

If the payment is made after the error was discovered, the payment may still be authorised if:

- the trustees took reasonable steps to avoid making the incorrect payment; or
- it was made while the trustees were considering (during a reasonable period) whether to amend the scheme rules to allow the benefit to be paid, or were in the process of doing so.

Lump sums paid in error
There are provisions to allow a pension commencement lump sum to be treated as an authorised payment even though the amount exceeds the maximum permitted under the Finance Act 2004. This applies where the pension commencement lump sum was calculated by reference to a pension which itself was calculated in error, provided that the error in relation to the pension is covered by the relaxation described above.

Pensions paid after the beneficiary's death
There are also relaxations for pensions paid after the beneficiary's death. These apply if:

- the payment was made within six months after the recipient's death;
- the payment would have been an authorised payment if made the day before the recipient died; and
- the trustees did not know, and could not reasonably have been expected to know, that the recipient had died, or the trustees did know and took reasonable steps to prevent the payment being made.

There are additional provisions authorising the payment of accrued arrears of pension after death, so long as (among other things) the payment would not have prejudiced approval under the pre-6 April 2006 tax regime.

Pension commencement lump sums paid after death
DB pension commencement lump sums paid after the member's death may be authorised if the trustees had not established the member's entitlement to payment until after the member's death and could not reasonably have been expected to pay the lump sum before the member's death. The payment must be made within one year of the member's death, or of the trustees' reasonably being expected to have known of it.

Pensions Regulator's anti-avoidance powers

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn09-05.aspx

The Pensions Regulator has amended its draft code of practice on the use of its extended anti-avoidance powers (see WHiP Issues 6 and 7) and laid it before Parliament. This code outlines the circumstances in which the Regulator would expect to use its power to issue contribution notices under the "material detriment" test applicable since 14 April 2008. This applies if the Regulator is of the opinion that an *"act or failure has detrimentally affected in a material way the likelihood of accrued scheme benefits being received"*.

The changes are intended to be clarificatory. The circumstances are now as follows:

- *The transfer of the scheme out of the jurisdiction.*
- *The transfer of the sponsoring employer out of the jurisdiction or the replacement of the sponsoring employer with an entity that does not fall within the jurisdiction.*
- *Sponsor support is removed, substantially reduced or becomes nominal.*
- *The transfer of liabilities of the scheme to another pension scheme or arrangement which leads to a significant reduction of the:*
    - *sponsor support in respect of these liabilities; or*
    - *funding to cover these liabilities.*
- *A business model or the operation of the scheme which creates from the scheme, or which is designed to do so, a financial benefit for:*
    - *the employer; or*
    - *some other person,*

where proper account has not been taken of the interests of the members of the scheme, including where risks to members are increased.

"Sponsor support" is defined as:

- *the scheme obligations of the employer or any other person; and*
- *the likelihood of recovery in full for the scheme under the scheme obligations,*

and "scheme obligation" means a liability or other obligation (including one that is contingent or otherwise might fall due) to make payment, or transfer an asset, to:

- *the scheme; or*
- *any work-based pension scheme, to which accrued scheme benefits have been transferred, in respect of any persons who were members of the scheme before the act or failure to act.*

The Code is expected to come into force in June or July, but effectively applies already.

Equality Bill

Parliament website Bill page:

http://services.parliament.uk/bills/2008-09/equality.html

The Equality Bill, consolidating and replacing existing anti-discrimination legislation, has been published. It is expected to be enacted in 2010. As a result of the consolidation, the following pensions legislation will be replaced (as well as notable statutes such as the Equal Pay Act 1970, Sex Discrimination Act 1975, Race Relations Act 1976, and Disability Discrimination Act 1995):

- the equal treatment provisions of the Pensions Act 1995 and the 1995 equal treatment regulations made under that Act.
- the 2006 age discrimination regulations.

The Bill fully rewrites the existing equality legislation. Most of the new law is designed to replicate existing law but there are some substantive changes and much of the drafting is different. There is therefore scope for equality law to change, perhaps unintentionally.

Occupational pension schemes will have implied non-discrimination rules in respect of gender reassignment and marriage/civil partnership. This is in addition to existing implied non-discrimination rules (e.g. age and sexual orientation) and the overriding equal treatment rule (sex equality) in Pensions Act 1995.

The new Equality Act will apply in respect of service on and after its commencement. The previous discrimination legislation will apply to prior periods.

Pensions Regulator

Corporate Plan 2009-2012
The Pensions Regulator has published its Corporate Plan for 2009 to 2012. Press reports focussed on a statement that there is an "*option to renegotiate recovery plans to repair scheme deficits, making clear that the best support for a pension scheme is a viable employer*". In fact, this was merely a restatement of the Regulator's previously declared position (see WHiP Issues 6 and 9).

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn09-03.aspx

"Alert in the economic downturn"
The Pensions Regulator has issued a statement headed "Alert to risks in the downturn". The statement is intended to alert "the regulated community" to potential risks and to encourage trustees and other parties to contact the Regulator if they are worried about anything.

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn09-04.aspx

The Regulator stresses that "*good governance of pension schemes is more, not less, important during the downturn*" and reminds those subject to whistle-blowing duties about their responsibilities.

Appointment of an independent trustee to prevent avoidance of a section 75 debt
The Pensions Regulator has appointed an independent trustee with exclusive powers to the Graphex Limited Pension and Life Assurance Scheme. It did this under its special procedure, without the issue of a warning notice, to avoid prejudicing members' interests.

Panel determination:

http://www.thepensionsregulator.gov.uk/pdf/DN1360105.pdf

The scheme had approximately £2.5 million assets and a buyout deficit of around £1.4 million. It had become apparent that certain directors, who were also trustees, were intending to strip assets from the sponsoring employer and then buy them back, using a new company, following a pre-packaged administration. There was a clear, documented intention to offload the pension liability and action to do so was expected imminently. The scheme would then have entered a Pension Protection Fund assessment period.

The Regulator's determinations panel found that two trustees had a conflict of interests that they had not managed appropriately and that action was necessary, in accordance with the relevant provisions of the Pensions Act 1995, to appoint a trustee in order to:

- *secure that the trustees as a whole have, or exercise, the necessary knowledge and skill for the proper administration of the scheme;*
- *secure the proper use or application of the assets of the scheme; or*
- *otherwise protect the interests of the generality of the members of the scheme.*

This is clearly territory where the Pensions Regulator's anti-avoidance powers would be directly relevant but they can be exercised only after the event. Here, the Regulator used an alternative power to take action to try to protect the interests of the scheme members and the Pension Protection Fund before the directors had taken steps to avoid the company's liabilities.

Deflation

The RPI figure for March 2009, published on 21 April 2009, shows year-on-year deflation of 0.4%. We circulated a briefing note on deflation issues for DB pension schemes on 24 March 2009. Please let us know if you did not receive a copy and would like one.

Office for National Statistics website:

http://www.statistics.gov.uk/cci/nugget.asp?id=21

Personal Accounts – consultation

The Government and Personal Accounts Delivery Authority are consulting on a draft order and rules (similar to a trust deed and rules) for the Personal Accounts scheme. The consultation also covers draft regulations to disapply the transfer value regulations. The consultation closes on 20 July 2009.

Consultation paper:

http://www.dwp.gov.uk/consultations/2009/draft-scheme-order-and-rules28april2009.pdf

Employer-related investment

The DWP has published its consultation response for the recent miscellaneous amendments regulations (see WHiP Issue 9).

This casts some light on the reasons for the amendments to the employer-related investment legislation that will take effect from 23 September 2010 (the deadline for complying with the transitional provisions of the relevant EU directive). It transpires that the amendments made by these regulations are not necessarily the final amendments and there may well be further amending regulations before 23 September 2010. These would deal in particular with the issues relating to collective investment schemes.

Consultation response:

http://www.dwp.gov.uk/consultations/2008/pensions-misc-regs-response.pdf

Indexation and revaluation amendments

Conservative MPs have called for the recent miscellaneous amendment regulations (see WHiP Issue 9) to be annulled. An early day motion has been initiated by David Cameron and other senior Conservative MPs. They are concerned about the overriding amendment power given to trustees (subject to employer consent) to amend scheme rules to reduce indexation and revaluation caps for future service benefits (see WHiP Issue 9). The Conservatives object to there not having been a Parliamentary debate and want employers to be able to exercise the power unilaterally.

At the time of writing, the regulations remain in place.

Parliament website page:

http://edmi.parliament.uk/EDMi/EDMDetails.aspx?EDMID=38367&SESSION=899

Consultation by employers

The DWP has updated its guidance on the obligation of employers to consult employees before making listed changes to pension schemes affecting benefits or contributions for future service. There are no significant changes of substance, save that the DWP has said that a change of group personal pension provider is not, in its view, a listed change.

DWP guidance:

http://www.dwp.gov.uk/publications/dwp/2005/occ_pen_schemes/occ_personal_pens_schemes_regs06.pdf#search=%22DWP%20guidance%20employee%20consultation%22

HMRC Registered Pension Schemes Manual

HMRC has published various updates to its Registered Pension Schemes Manual. They cover:

- clarifications that only benefits that commence after reaching age 50 before 6 April 2010 can continue as authorised payments after 5 April 2010 where the member is not yet 55;
- procedures for tax relief at source (including annual notices from HMRC requesting details of members' contributions in the previous tax year); and
- reform of the HMRC appeals system.

HMRC RPSM updates:

http://www.hmrc.gov.uk/manuals/rpsmmanual/updates/rpsmupdate020409.htm

HMRC anti-avoidance "spotlights"

HMRC has outlined a pensions anti-avoidance technique in its "Spotlights" internet page. This involves members purporting to surrender scheme benefits to create an artificial surplus, which is then removed from the scheme. HMRC says that it will treat this payment as an unauthorised member payment and levy the appropriate tax charges.

HMRC Spotlights:

http://www.hmrc.gov.uk/avoidance/spotlights.htm

Amendment of PPF compensation provisions

Provisions of the Pensions Act 2008 relating to PPF compensation have been brought into force. These allow the PPF to provide a lump sum before normal pension age to members with a terminal illness and cap revaluation at 2.5% pa on compensation relating to benefit accrual after 5 April 2009.

Commencement order:

http://www.opsi.gov.uk/si/si2009/uksi_20090809_en_1

Short Selling and Bank Accounts Bill

This private member's Bill was introduced on 23 March 2009. It proposes, among other things, "*to require disclosure by pension funds and their trustees of records of loans of their shares for the purpose of short selling, and of the fees received in such cases*". Private members' bills do not usually make it into law.

Parliament website Bill page:

http://services.parliament.uk/bills/2008-09/shortsellingandbankaccounts.html

Equal pay claim time limits

Case report:

http://www.bailii.org/ew/cases/EWCA/Civ/2009/293.html

In *Slack and others v Cumbria County Council*, the Court of Appeal held that if an employee had been employed under consecutive contracts, with no significant changes in terms, the time for bringing an equal pay claim did not necessarily start to run when each contract ended. If there has been an uninterrupted series of employment contracts, the special time limit rules in the Equal Pay Act 1970 for "stable employment relationships" can apply so that time starts to run when the employment ends, not when each contract ends.

In a pensions context, this is particularly relevant to part-time workers' claims. However, different decisions in this area mean that the law is unclear about the circumstances when the "stable employment relationship" rules will apply.

Misguided attempt to dissolve a scheme

Case report:

http://www.bailii.org/ew/cases/EWHC/Ch/2009/611.html

Mr Thorpe was the only member of a small self-administered scheme ("SSAS"). He was also a trustee together with an independent pensioneer trustee. Mr Thorpe invoked the rule in *Saunders v Vautier* purportedly to bring to an end the trusts of the SSAS and to pay the funds to himself. That rule says, broadly, that all of the beneficiaries of a trust (or a single remaining beneficiary), if they are adults, can require the trustees to bring it to an end and distribute the trust funds.

The independent pensioneer trustee had refused to co-operate, since it would have breached its undertaking to HMRC not to terminate the scheme except in accordance with its winding-up provisions, so it was (ineffectively, in fact) removed by Mr Thorpe. The case concerned events before 6 April 2006 and so the old HMRC approval regime and the Income and Corporation Taxes Act 1988 applied.

In an appeal from a decision of HMRC's Special Commissioners, the High Court agreed that:

- the rule in *Saunders v Vautier* did not apply because there remained the possibility of other beneficiaries in the future (e.g. a spouse or dependant);
- consequently the scheme's assets remained subject to its trusts and their distribution to Mr Thorpe was a breach of trust; and
- the rule in *Re Hastings-Bass* (which can be used to unravel trustees' discretionary decisions if they were not aware what the consequences would be) did not apply because Mr Thorpe had not exercised a discretion given to the trustees.

It was correct that the scheme had lost HMRC approval as a result of Mr Thorpe's actions and so the 40% tax charge on the value of the scheme's assets was upheld.

However, Mr Thorpe was able to avoid an income tax charge on the amount that he had paid to himself from the scheme. He successfully argued that, as he knew of the breach of trust, he became a constructive trustee of the funds received and, provided that he returned them to the SSAS (with interest), he should not have to pay any tax personally (until he actually receives benefits from the scheme).

Pensions Ombudsman determinations

Trustees personally liable for investment decisions

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/mar/m00358%20and%20others.doc

In the case of *Mr R Adams*, former trustees of the ES Group Pension Scheme were found personally liable for £525,000 (plus interest) of losses caused by unlawful investment activity. The maladministration found by the Pensions Ombudsman included employer-related investment, failure to take investment advice and failure to consider the investment of significant cash assets.

The scheme's rules included exoneration and indemnity clauses but the trustees could not rely on them because of s33 Pensions Act 1995. (This provides that "*liability for breach of an obligation under any rule of law to take care or exercise skill in the performance of any investment functions … cannot be excluded or restricted by any instrument or agreement*".) There is power for the Court (and in practice the Ombudsman) to give a trustee discretionary relief under the Trustee Act 1925 if he or she has acted honestly and reasonably and ought fairly to be excused. Here, all but one of the trustees had acted honestly but not, in the Ombudsman's view, reasonably so no relief was granted.

The Ombudsman said:

"*Those present at the hearing all put it to me that they were not men with ready resources out of which their share of any liability could be paid. However, I have found that they failed in carrying out serious fiduciary responsibilities to others in circumstances in which the law specifically states that they should not be protected from liability. The Applicants' complaints are upheld and it is appropriate that they should be compensated.*"

The main driving force behind the maladministration was Mr Robinson, whom the Ombudsman found to have been dishonest. He emigrated to New Zealand during the course of the Ombudsman's investigation. The other former trustees are jointly and severally liable for the losses caused by their maladministration and may end up paying his share as well as their own.

An augmentation of Mr Robinson's benefits to an accrual rate of 1/17th (from 1/60th) was determined to be valid. The determination does not say whether the trustees will have a right of set off so that Mr Robinson's liability for breach of trust can be deducted from his benefit entitlements.

Failure to provide information – cash compensation

In the case of *Mr W E Hughes*, the Ombudsman found that his employer had failed to inform him of his right to join a (contracted-out) DB section of the employer's pension scheme following his promotion. Instead, he remained in the (contracted-in) DC section.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/feb/27698.doc

It was extremely difficult to calculate Mr Hughes' loss. Unusually, the employer was directed to give him the choice of:

- DB benefits reduced by the State Second Pension/SERPS he would receive by reason of being contracted-in for the relevant period and with his DC section benefits adjusted to relate only to contributions from before his promotion; or
- £5,000 cash compensation for his loss – a figure calculated to compensate him for the distress of not knowing exactly how much damage he has suffered and "*substantially as proxy compensation for a financial loss that cannot be accurately identified but is likely to be significant*".

£100 compensation was also awarded "*for the distress and inconvenience caused by his exclusion from the DB section and the need to make a formal complaint*".

Compensation for distress over misleading information

Mrs M A Wootton was given misleading information that led her to believe she could retire at age 55 on unreduced pension. She had not, however, suffered any financial detriment in reliance on the misleading information. The Pensions Ombudsman therefore determined that no compensation for financial loss was due.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/jan/71204.doc

The Ombudsman did, however, direct that Mrs Wootton be allowed to pay her added years AVCs over the period to age 60, rather than age 55 as originally agreed. This would be a little cheaper for her and she should be refunded the overpayments made on the basis of her expected retirement at age 55.

Mrs Wootton had been offered £250 for distress and inconvenience but she complained that this was not adequate. Unusually, the Pensions Ombudsman directed that she be paid £1,000 as compensation for the "considerable distress" she suffered when learning that she would have to suffer a reduction to her pension or work five years longer for her unreduced pension.

Interest for late payment of benefits following successful claim

In the case of *Mrs G Riddell*, Mrs Riddell was unlawfully excluded from the scheme by reason of working part-time. She was granted 13 years' backdated membership by an employment tribunal. The pension was brought into payment as she had already reached normal pension age. She claimed interest on her lump sum and pension for late payment.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/jan/72726.doc

The Deputy Ombudsman determined that in the absence of any maladministration and of any express provision in the scheme rules, it would not be appropriate to direct the payment of interest. Nor was there any other legal entitlement to the payment of interest. He also took account of the fact that Mrs Riddell was not asked to pay interest on the backdated contributions that she was asked to pay when she was admitted.

Conflicts of interest and independent trustees

The case of *Mrs JE Warwick* concerned the determination of death benefit beneficiaries by a trustee board that included a trustee with a conflict of interest but also an independent trustee.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/jan/71590.doc

Mr Ranger had been a member of a small self-administered scheme until his death in 2004. The trustees were his estranged wife and the independent pensioneer trustee. The scheme provided for a lump sum death benefit and a dependant's pension (for which partial dependency was enough to qualify).

Mr Ranger's subsequent partner, Mrs Warwick, was the complainant. The administrator had written to her asking for evidence of financial dependency, which was only partially provided. She was granted a lump sum of £70,235.20, representing 70% of the sum payable. The remaining 30% was paid to Mrs Ranger. This was a compromise: the pensioneer trustee initially wanted an 80/20 split and Mrs Ranger wanted a 60/40 split. There was no dependency requirement for the lump sum.

As for the dependant's pension, Mrs Ranger was of the view that Mr Ranger had been dependent on Mrs Warwick, not she on him, but Mrs Warwick refused to provide any further information. The trustees seem to have decided to pay 50% of the dependant's pension to Mrs Warwick, though this is not clear from the determination.

Mrs Warwick complained about Mrs Ranger's conflict of interest and said that another trustee should have been appointed.

The Pensions Ombudsman determined that the decisions should stand, as the possibility of bias did not invalidate the decision made by the trustees jointly. Clearly there was a "*potential (sic) conflict of interest*". However, the scheme rules made specific provision for a trustee who was also a beneficiary to be involved in the exercise of a discretionary power. Also, the independent trustee had no power to remove Mrs Ranger.

The request for further information was not unreasonable and Mrs Warwick's refusal to provide it "*supports the suspicion that she may not have been dependent on Mr Ranger*".

The complaint was therefore rejected.

Post-merger discretionary pension increases
In the case of *Algie and Harrop*, a 22 year history of granting discretionary pension increases was brought to an end following a scheme merger in 2002. The principal employer with power to grant the increases was the same under both schemes: Nalco Limited.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/mar/24587%20&%2071249.doc

The Pensions Ombudsman determined that:

- There was no entitlement to ongoing increases under any pension law principle of "custom and practice" (and employment law considerations were outside his jurisdiction). There could not be a contractual obligation that deprives the employer of its express discretion.
- The actuary had given a GN16 (bulk transfer without consent) certificate in which he certified that he had cause to believe that the award of customary discretionary benefits post-merger would be no less favourable. The fact that discretionary increases had stopped immediately after the merger meant one of two things:
  - the actuary was "*deluded or hoodwinked*" or was suffering from poor judgment; or
  - events might have overtaken things (such as "*an unexpected collapse in Nalco's fortunes or the Plan's funds*").
- "*It could not be proper for Nalco, knowing that the Actuary had given a certificate recording a well founded belief which must have been based on knowledge of Nalco and the Plan, to make a decision without good reason which flew in the face of the actuary's belief*".
- "*If Nalco has not had regard to the actuary's 'good cause to believe' then at best there has been maladministration in overlooking it (because a relevant factor has been disregarded) and at worst Nalco has not dealt with the members of the Plan in good faith*".
- The Ombudsman also found that ignoring the existence of an undertaking in the merger deed to consider discretionary increases post-merger, "*believing that it meant nothing of substance (or no more than that the same factors had to be taken into account as would have been taken into account anyway), was maladministration*".
- There was also maladministration in that the 2003 decision not to award increases had been rolled over in subsequent years, and not properly considered annually. There was no evidence that the plan's funding position and Nalco's financial position were meaningfully considered in those later years.

The complaints were therefore upheld. Nalco was ordered to consider its exercise of discretion for each year from 2003 to the present, taking into account the material factors as they stood at the time. If increases are awarded (and they do not necessarily have to be given) back payments are to be made to the complainants with simple interest at base rate added.

Pensions Ombudsman time limits

In the case of *Mr Ralph*, the Pensions Ombudsman exercised his discretion to accept a complaint that fell outside the statutory limitation periods for claims to the Ombudsman (generally three years) and, perhaps, for claims to the Court (generally six years).

The complaint related to advice given to Mr Ralph by his employer, Arjo Wiggins, in 1986 to transfer his benefits to a buyout policy. He became aware that the advice was deficient in 2004 at the latest, when he received a statement dated April 2004, but did not complain to the Ombudsman until July 2007.

The Ombudsman distinguished the recent determination of Mr P Lever's complaint (see WHiP Issue 9) and determined that there was no reason why he could not exercise his discretion to consider the complaint even if it would be time-barred by the Courts. Any inconsistency in this approach was merely a factor for him to consider when deciding whether to exercise his discretion.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2009/mar/27877.doc

Appendix

"Anti-forestalling" provisions of the Finance Bill

These measures will affect individuals:

- who have *relevant income* (see below) of £150,000 or more in the relevant tax year or any of the three previous tax years;
- whose pension provision increases on or after 22 April 2009 (but with some exceptions); and
- whose total *pension input* (see below) in 2009/10 or 2010/11 is greater than £20,000.

There are five key concepts:

- the *pension input*, calculated in the normal way as required by the Finance Act 2004 for the purposes of the annual allowance (but using the tax year as the pension input period). Essentially this means the value of any defined benefit accrual plus the amount of any money purchase contributions paid by or for the benefit of the individual;
- the *special annual allowance*, which is £20,000 less any *protected pension input* (but not less than nil);
- the *protected pension input*, which is the normal, regular, ongoing pension savings of the individual made pursuant to arrangements established before 22 April 2009 (see further below);
- the *total adjusted pension input amount*, which is the individual's total *pension input* less the *protected pension input*;
- the *special annual allowance charge*, which is the tax charge on the individual by reference to the amount by which his or her *total adjusted pension input amount* exceeds the *special annual allowance.* This will be 20% for 2009/10 (and probably 30% for 2010/11 to reflect the new 50% higher rate tax band).

The effect of the *special annual allowance charge* is:

- to claw back higher rate tax relief on the member's own additional DC contributions; and
- to tax the individual on the benefit of additional employer's DC contributions or (subject to exceptions) increased DB accrual.

The formula for calculating the *special annual allowance* ensures that there will be no *special annual allowance charge* for *pension inputs* up to £20,000, even if the *pension input* is more than the *protected pension input*. But there will be a charge if the *pension input* is more than the *protected pension input* and more than £20,000. The figure of £20,000 will be fixed for both 2009/10 and 2010/11.

For DC schemes, *protected pension input* means contributions that are paid at least quarterly, under arrangements made before 22 April 2009, and at a rate that does not increase (unless the increase was agreed before 22 April 2009). This includes employer contributions and (if any) third party contributions, as well as the individual's own contributions. The Treasury is being lobbied for a less rigid restriction of *protected pension input* by organisations representing the self-employed, who often make annual pension contributions, and on behalf of employees who pay AVCs from annual bonuses.

For DB schemes, *protected pension input* includes any increases in benefits that arise under the rules as they stood at 22 April 2009, including the effects of normal pay rises and career progression. If benefits are improved and at least 50 members are affected in the same way, the improvement will be categorised as *protected pension input*.

For cash balance schemes, *protected pension input* includes increases to benefits to the extent that there is no material change to the way that benefits are calculated on or after 22 April 2009. If there is a material change, there is protection if it applies to at least 50 active members of the same scheme.

Any additional pension provision made between 6 and 21 April 2009 will be protected. It will not be subject to the *special annual allowance charge*, but will reduce the *special annual allowance* (for 2009/10 only).

It is the individual who is responsible, via self-assessment, for paying any special annual allowance charge. Schemes do not have to make any notification to HMRC about this. They may, however, be asked by members – particularly DB members - for information to help them arrange their tax affairs and complete their tax returns. And members may ask for a refund of contributions.

If an individual's total *adjusted pension input amount* exceeds the *special annual allowance*, he/she may be able to ask the scheme for a refund of contributions paid after 5 April 2009. Schemes may agree to this if the rules allow. (In many cases a rule amendment will be required.) The Finance Act 2004 rules will be extended to allow refunds ("contributions refund lump sums") as authorised payments but only if the contributions (a) were paid by someone potentially liable to the *special annual allowance charge* (i.e. income over £150,000pa) and (b) were AVCs or non-regular contributions paid to a personal pension scheme (or retirement annuity contract).

If there is to be a refund of the individual's contributions, it must be paid in the following tax year to avoid it being an unauthorised payment. The refund will cancel the relevant part of the *special annual allowance charge.* It will be chargeable to tax at 40% (or probably 50% for contributions paid in 2010/11) so as to reverse the tax relief originally given on the contribution. The scheme administrator will be responsible for paying this tax charge and notifying HMRC on the scheme's tax return. It is not clear what timing adjustments would be permitted by reference to interest or investment returns (positive or negative).

Refunded employer contributions (including any made pursuant to a salary or bonus sacrifice arrangement) would, in these circumstances, be unauthorised payments.

If an individual is liable to tax for exceeding both the *special annual allowance* and the annual allowance (£245,000 for 2009/10), there is an adjustment made to the *special annual allowance charge* to avoid double taxation.

For the purpose of testing whether the £150,000 threshold has been reached, an individual's *relevant income* includes:

- all income (including investment income) after deducting certain tax reliefs (but not the personal allowance), gift aid donations and up to £20,000 pension contributions;
- any employment income foregone by salary or bonus sacrifice in return for employer pension provision, but only if the arrangement was entered into on or after 22 April 2009; and
- redundancy payments (about which there has been some lobbying).

The individual is caught if *relevant income* reaches this threshold in the relevant tax year, or in either of the preceding two tax years.

If the employer changes its pension arrangements, by setting up a new scheme or transferring members between its schemes, the contributions/accrual under the new scheme may continue to be treated as *protected pension input* so long as the new scheme is an occupational pension scheme or a group personal pension scheme (in either case) for the benefit of at least 20 employees and there is no material change in the way that benefits are calculated (or any material change affects at least 50 active members).

If the individual changes jobs and joins a new scheme, the pension provision will be *protected pension input* if the basis of contributions or accrual is the same for 20 scheme members. If an individual leaves his/her current employer and starts contributing to a personal pension, for example because he/she has become self-employed or the new employer offers little or no pension provision, the personal pension contributions will not be protected.

The *special annual allowance charge* does not generally apply to pension provision made in the tax year in which the individual dies or takes ill-health retirement. For DB schemes with at least 20 members, it does not apply in the tax year in which all benefits are taken.

The Government will consider changing pensions tax charges under the Finance Act 2004 regime to reflect the fact that the highest earners may have paid a *special annual allowance charge*. There are no immediate changes.

Anti-avoidance rules are included. HMRC will look very closely at any arrangements designed to avoid the *special annual allowance charge*, for example by reducing income to below the £150,000 threshold or artificially reducing the value of DB accrual.

There are a number of worked examples in HMRC's "Guidance for Individuals" and "Technical Guide" (see links on page 1).

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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 and Philip Stear.

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