TRAVERS SMITH

What's happening in Pensions

Issue 4 ***August 2008***

Scheme funding: Pensions Regulator's mortality assumptions trigger

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn08-15.aspx

In its February 2008 consultation, the Pensions Regulator proposed a new funding intervention trigger based on mortality assumptions (see WHiP Issue 1). The Regulator has announced that this change will now apply only to valuations with an effective date on or after 22 September 2008. A full consultation response is expected "later in the summer".

Transfer values – Pensions Regulator draft guidance

Consultation paper:

http://www.thepensionsregulator.gov.uk/pdf/CETVGuidanceConsultationDocAug08.pdf

The Pensions Regulator is consulting on draft guidance on the calculation of cash equivalent transfer values. The guidance is designed to help trustees with their new obligations to determine assumptions and calculate transfer values under amendments to the Transfer Value Regulations coming into force on 1 October 2008 (see WHiP Issue 2).

As well as describing the requirements of the amended legislation and providing guidance to replace certain aspects of actuarial guidance note GN11 (which will be withdrawn) the draft sets out the Regulator's interpretation of some requirements where the law is unclear and describes what the Regulator will consider to be best practice. For example:

- Members may have benefit options (for example commutation) that, depending on whether or not they are exercised, would increase or reduce the value of their benefits. The draft guidance states that only such options that would increase the cash equivalent should be taken into account.
- Trustees may not offset any options that could reduce the cash equivalent against options that would increase it.
- It would be good practice for trustees to tell members what options and discretionary benefits are included in the cash equivalent and to disclose, but only on request, reasonable details of the transfer basis and underlying assumptions used.
- Schemes in a Pension Protection Fund assessment period are not permitted to pay transfers but are still under a statutory obligation to issue statements of entitlement. The Regulator confirms that it will not take any action in respect of a breach of the requirement to issue statements of entitlement if members have been informed that transfers cannot be paid.

We will report on the final guidance in due course.

Record-keeping

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn08-16.aspx

The Pensions Regulator has launched a consultation on record-keeping. The consultation closes on 15 October 2008. The Regulator recommends the following as good practice:

- testing for the presence of core information about every member;
- identifying additional information required to administer the scheme; and
- if necessary, developing a plan to obtain missing information.

It is also proposed that administration is included in its own right in the "Scope" for trustee knowledge and understanding.

Governance survey

The Pensions Regulator published the results of its third governance survey on 17 July 2008. It notes that improvements must still be made as regards the documentation of internal controls and the maintenance of registers of trustees' interests.

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn08-14.aspx

Dispute resolution Code of Practice

The Pensions Regulator's Code of Practice No.11: Dispute resolution – reasonable periods" (see WHiP Issue 1) came into effect on 28 July 2008.

Appointed Day Order:

http://www.opsi.gov.uk/si/si2008/uksi_20081882_en_1

Code of Practice No.11:

http://www.thepensionsregulator.gov.uk/pdf/CoP11DisputeResolution.pdf

Winding-up guidance

Three documents were published on 30 June 2008, following a recent consultation:

- Pensions Regulator Guidance: "Winding-up: avoiding delays"
- A joint statement by the Pensions Regulator, the Pension Protection Fund and the Financial Assistance Scheme
- A joint consultation report by the same bodies

The guidance is to help trustees to meet Government expectations that key winding-up activities are completed within two years. The DWP has confirmed that it has no intention of setting out in legislation how benefits including GMPs should be equalised for men and women.

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn08-12.aspx

Guidance:

http://www.thepensionsregulator.gov.uk/guidance/windingUp/index.aspx

Pensions Regulator Annual Report

The Pensions Regulator published its annual report and accounts for the financial year 2007/8 on 17 July 2008. Figures in brackets are for 2006/7.

- 143 (149) clearance applications were granted; 0 (1) applications were refused; 494 (874) clearance enquiries were received. The number of withdrawn applications is not given this year (26 in 2006/7).
- 52 independent trustees and 456 member and third party trustees were appointed (552 in total for 2006/7).
- 554 (640) notifiable events were reported.
- 513 (1,233) whistle-blowing reports were submitted.

Press release:

http://www.thepensionsregulator.gov.uk/whatsNew/pn08-13.aspx

Pensions Ombudsman Annual Report

The Pensions Ombudsman and PPF Ombudsman annual report and accounts for 2007/2008 were published on 17 July 2008. The backlog of cases is being slowly reduced. The report contains some illustrations of typical determinations. As for 2006/7, the most common causes of complaint are benefit calculations, ill health pensions and transfers.

Annual report:

http://www.pensions-ombudsman.org.uk/publications/docs/PO-AnnualReport-2007-08.pdf

Money Laundering Regulations – Registration

HMRC has finally published detailed guidance on the need to register under the Money Laundering Regulations 2007. It had been unclear whether or not paid trustees needed to register as "trust or company service providers" (TCSPs). The new guidance, issued on 31 July 2008, makes it clear that trustees (or directors of trustee companies) of occupational pension schemes and employee share schemes will not, by reason of that fact, be regarded as TCPSs even if acting "by way of business".

We understand that trustees who are not required to register but who, in the light of the earlier published guidance, have done so are entitled to a refund of their registration fee from HMRC.

HMRC guidance:

http://www.hmrc.gov.uk/mlr/mlr9-reg-dates-announced.htm

Finance Act 2008

The Finance Bill (see WHiP Issue 1) received Royal Assent on 21 July 2008 and is now the Finance Act 2008. The sections (90 to 92) concerning pensions are as follows.

The Act:

http://www.opsi.gov.uk/acts/acts2008/ukpga_20080009_en_1

- **Tax relief for employers' contributions**

  There are provisions to clarify that before 6 April 2006 (and since 1 April 2004, when legislation was changed) only employer contributions actually paid to exempt approved pension schemes in the relevant accounting year qualify for tax relief.

  Tax relief on large contributions is spread over a period of up to four years where the contribution (a) is more than 210% of the contributions paid in the previous tax period and (b) exceeds 110% of the contributions paid in that previous period by at least £500,000. The Act will stop companies from avoiding the spreading of tax relief on large contributions by routing them through a different company. This applies to payments made on or after 10 October 2007 under binding obligations entered into on or after 9 October 2007.

- **Taxation of deemed authorised payments**

  At present, regulations may deem certain previously unauthorised payments to be authorised, but cannot then provide for their tax treatment. The Act allows regulations to impose income tax on these payments.

- **Lifetime allowance test**

  Changes have been made to how the lifetime allowance operates for pension increases (benefit crystallisation event 3 (BCE3)):

  - Pension increases will now avoid BCE3 if they do not exceed a "normal" rate of increase in a 12 month period (5% or RPI if higher). For this purpose, schemes will use the RPI figure published two months before the pension increase occurs.
  - The circumstances in which an increase is exempt from the BCE3 test altogether are also widened. Previously all pensioners had to receive the same increase in order for the exemption to apply: now only 20 pensioners have to.

  The changes are backdated to 6 April 2006 (apart from the change in calculation of RPI which is backdated to 6 April 2008).

- **Protection of lump sums exceeding 25% of pension rights**

  The Finance Act 2004 gave transitional protection to members with rights to lump sums on 5 April 2006 of more than 25% of the value of their total rights under the scheme at that time. The calculation of the maximum pension commencement lump sum for these members under the new tax regime was different depending on whether or not the member had relevant benefit accrual after 5 April 2006. It will now be the same calculation in each case (which could be more generous for members with no such accrual). This change is backdated to 6 April 2006.

- **Inheritance tax avoidance**

  These changes are particularly relevant to small self-administered schemes and are designed to prevent the use of tax-relieved pension savings as a way of avoiding inheritance tax. There will now be an unauthorised payments charge if:

  - rights to payments under a lifetime annuity or dependant's annuity are surrendered; or
  - someone with a right to a scheme pension, lifetime annuity, dependant's scheme pension or dependant's annuity becomes entitled to an increase in their pension rights following the death of another member who is connected to him or her, as a result of that person's death.

  In the latter case, there will also be an inheritance tax charge where the person dies aged 75 or over and there is an increase in pension rights or an unauthorised lump sum payment.

  The provisions above concerning the increase of pension rights after death will not apply to schemes with more than 20 members, provided that the same increase provisions apply to all members.

  These provisions apply in respect of surrenders made on or after 10 October 2007 and for increases in pension rights attributable to the death of a member when the member dies on or after 6 April 2008. The inheritance tax charges potentially arise following deaths on or after 6 April 2008.

- **Abolition of fixed stamp duty on certain instruments**

  Fixed stamp duty is abolished on "declarations of use or trust" executed on or after 13 March 2008 and not stamped before 19 March 2008. There is therefore no longer any need to pay £5 stamp duty on, or include stamp duty exemption wording in, most pension scheme deeds.

Raising queries with HM Revenue & Customs

HMRC published its 34th Pensions Tax Simplification Newsletter on 24 July 2008. (The word "Simplification" was originally quietly dropped but then reinstated with a note that it will be dropped for the next issue!) The points of interest are as follows:

- The procedure for contacting HMRC with pension queries is outlined, as follows:
  - First consult the online Registered Pension Schemes Manual
  - Call the helpline 0845 600 2622 or email via the website
  - Write to HMRC in the way outlined in Code of Practice 10
- Code of Practice 10 specifies a cut-off point after which HMRC will not deal with queries relating to the interpretation of Finance Acts. As regards Finance Act 2004, this has been further extended to the date on which Finance Act 2010 receives Royal Assent.

Newsletter:

http://www.hmrc.gov.uk/pensionschemes/pen-newsletter34.htm

Code of Practice 10:

http://www.hmrc.gov.uk/pdfs/cop10.htm

Adult dependent children's pensions

HMRC has consulted on draft regulations to extend the transitional provision covering pensions for adult (over age 23) dependent children's pensions in payment on 1 July 2008, or where the entitlement to the dependant's pension arose before then. These are typically pensions payable to adult children who cared for an elderly parent. There was an issue with some such dependants not falling within the existing transitional provisions and pension payments therefore being unauthorised. The effect is intended to be backdated to 6 April 2006.

Announcement:

http://www.hmrc.gov.uk/pensionschemes/adult-dep-child.htm

Draft regulations:

http://www.hmrc.gov.uk/pensionschemes/draft-si-trans-pen-sche.pdf

Winding-up: reduction of scheme pensions already in payment

The Government intends to introduce regulations to prevent inadvertent tax consequences where a member's scheme pension is reduced in the course of a winding-up. They will cover the situation where some, but not all, members' scheme pensions are reduced due to scheme underfunding. The regulations will only apply to schemes with more than a certain number (yet to be specified) of members, and will have backdated effect from 6 April 2006.

HMRC announcement:

www.hmrc.gov.uk/pensionschemes/reductions-scheme.htm

Pensions Bill

The Pensions Bill has completed its House of Lords committee stage and a new version has been published. Parliament is now in recess until October. In addition to amendments previously reported, there are the following developments to note.

- **Extension of the Pensions Regulator's powers**

  The House of Lords accepted the Government's proposed amendment to include an enabling power to extend the Pensions Regulator's anti-avoidance powers (see WHiP Issue 2) by regulations. The Government agreed, however, to propose amendments to meet the strongly-voiced concerns of the opposition, in particular as to the breadth of the proposed regulation-making power.

- **Personal Accounts**

  Following heavy lobbying, workplace alternative DC schemes will be judged by the overall amount of contributions, rather than having to use the same definition of gross earnings used by the Personal Accounts scheme, when assessing whether they qualify as alternative workplace schemes. No further detail has yet been provided.

  Employers will not be allowed to offer inducements to encourage employees to opt out of workplace pensions and Personal Accounts. (This could affect flexible benefit arrangements.)

  The Personal Accounts Delivery Authority has published a report on the charging structure for Personal Accounts. This summarises responses but does not report any conclusions at this stage. Recommendations will be made to the DWP later this year. There was no consensus, but a majority of respondents favoured either an annual management charge only or a contribution charge combined with an annual management charge.

Bill homepage:

http://services.parliament.uk/bills/2007-08/pensions.html

References to "employee" have been changed to "worker" so that agency workers are covered.

- **Contracting-out**

  Protected rights will be completely abolished from 2012. From then, it will no longer be possible for schemes to be contracted-out on a money purchase basis. This means that from 2012 trustees will no longer be required to comply with any of the requirements and restrictions relating to protected rights.

- **Risk-sharing**

  Opposition amendments to allow a new form of risk-sharing benefit structure have been withdrawn. The Government will publish its consultation response (see WHiP Issue 3) in the autumn.

- **Financial Assistance Scheme**

  There will be power to make permanent the temporary ban on purchasing annuities by trustees of schemes that are eligible for the Financial Assistance Scheme. The current prohibition expired on 25 June 2008, but the Pensions Bill will continue it retroactively from 26 June 2008.

  Schemes, such as Northern Ireland's Desmond and Sons, which fall between the PPF and the FAS due to unusual timing of winding-up and insolvency will now be eligible for the Financial Assistance Scheme.

- **Payments to employers**

  The Pensions Act 2004 re-enacted provisions restricting payments from occupational pension schemes to employers but omitted exceptions for certain administrative payments. A Government amendment rectifies the situation and will provide that the restrictions do not apply to authorised employer payments listed in section 175(c) to (f) Finance Act 2004, which include scheme administration employer payments.

Maternity leave

New regulations clarify uncertainty about maternity leave. They confirm that the requirement to provide benefits during unpaid additional maternity leave does not, as regards employment-related benefit schemes, go further than the existing requirements of Schedule 5 to the Social Security Act 1989. That Schedule provides that employer pension contributions or accrual need to continue during paid maternity leave (but not during unpaid maternity leave).

Regulations:

http://www.opsi.gov.uk/si/si2008/uksi_20081966_en_1

State Second Pension accrual

The National Insurance Contributions Act 2008 received Royal Assent on 21 July 2008. There are no changes from the Bill as introduced. The Act introduces the Upper Accrual Point (£770pw or £40,040pa) (UAP) for the State Second Pension (S2P) from 6 April 2009. Unlike the Upper Earnings Limit, the UAP will not be increased in line with inflation. This is being done to enable S2P to become flat rate, which is to be achieved by 2030.

The Act:

http://www.opsi.gov.uk/acts/acts2008/ukpga_20080016_en_1

VAT

The NAPF has been joined to the Wheels (Ford) Common Investment Fund's appeal against the HMRC position that investment management of pension funds is subject to VAT (see WHiP Issue 3). HMRC is expected to finalise its consideration of the suitability of this fund as a test case by 30 September 2008. The VAT Tribunal will issue directions in due course as to how the case is to proceed.

Sectionalised and single employer schemes - Hearn v Dobson

In this case, in which Travers Smith acted, the High Court looked at the application of the new statutory funding regime to a scheme's trust deed and rules. The scheme was a multi-employer defined benefit scheme under which all employers but the principal employer had withdrawn from participation and their liability to contribute had terminated. On each withdrawal, a partial winding-up rule had created separate funds within the scheme in respect of the assets and liabilities attributable to each former employer.

Case report:

http://www.bailii.org/ew/cases/EWHC/Ch/2008/1620.html

The High Court held that only the principal employer was an "employer" under the scheme funding legislation. The scheme was therefore a single employer scheme, albeit that it was divided into sections by reference to different employers. It was not a sectionalised scheme within the meaning of Schedule 2 to the Scheme Funding Regulations. The "sections" would therefore not be treated as separate schemes. When calculating the principal employer's contributions, therefore, the assets and liabilities of the whole scheme, including other former employers' sections, had to be taken into account.

Age discrimination claims

The Court of Appeal has ruled in the case of *Johns v Solent SD* that the Employment Appeal Tribunal was right to order the Employment Tribunal to put Mrs Johns's age discrimination claim on hold pending the outcome of the Heyday case on the same question that has been referred to the European Court of Justice (compulsory retirement at age 65). Accordingly, all other Employment Tribunal claims of unlawful compulsory retirement remain on hold.

Case report:

http://www.bailii.org/ew/cases/EWCA/Civ/2008/790.html

No trustee duty to act fairly - Pensions Ombudsman determination

Mr Hobbs complained that a decision by trustees in 2005 to distribute surplus failed to take into account the fact that in 1991 benefit improvements had been granted to pensioners who had been retired for at least a year and not to others. He argued that the trustees should have corrected this unfairness when distributing the surplus.

The Pensions Ombudsman determined that there was no duty on the trustees to act fairly. Rather, they must ask themselves the correct questions, direct themselves correctly in law, and not take into account irrelevant, irrational or improper factors, and the decision must not be one that no reasonable body of trustees properly directing itself could have reached (i.e. the decision is not perverse). Although the Ombudsman had sympathy for Mr Hobbs, he found that it could not be said that no reasonable trustees could have made the decision. He could not, therefore, overturn the trustees' decision.

Determination:

http://www.pensions-ombudsman.org.uk/determinations/docs/2008/may/s00129.doc

SIPPs and protected rights

The DWP has announced that from 1 October 2008 self-invested personal pensions (SIPPs) will be allowed to hold protected rights. It has published its response to the earlier consultation on draft regulations. SIPPs wishing to accept protected rights will need to apply for contracting-out certificates as "appropriate schemes". Applications may be submitted before 1 October.

Press release:

http://www.dwp.gov.uk/mediacentre/pressreleases/2008/jun/pens074-270608.asp

Consultation response:

http://www.dwp.gov.uk/publications/dwp/2007/occ-pen-consult/govt-resp-ppsaspraregs08.pdf

Hyperlinks in this document can be clicked via an up to date version of Adobe Acrobat Reader. We are not responsible for the contents of external websites to which we provide links.

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.

Travers Smith LLP
10 Snow Hill
London EC1A 2AL
T: +44 (0)20 7297 3000
F: +44 (0)20 7295 3500

www.traverssmith.com