

Pensions monthly update – keeping you on track

December 2013

Pension briefing

HIGHLIGHTS

Hogan Lovells pension group is delighted to send you our news Alerter for December, setting out developments over the last two months.

Our Pension Planner gives a comprehensive overview of legal developments in the previous 12 months and expected future changes. For the latest issue, please click on the link in the email alerter.

DATES FOR YOUR DIARY

9 January 2014 – Joint seminar with the Law Commission

A morning seminar at our offices, held jointly with the Law Commission, to consider the implications of the Commission's consultation paper on fiduciary duties of investment intermediaries. For an invitation and to book a place, please click on the links in the email alerter.

22 January 2014 – Trustee training

A half-day seminar aimed at trustees with some experience or who have attended our one day introductory course (or similar training). Focusing on the trustee's perspective, we will consider developments in the previous year and will look ahead at what we can expect in 2014. For an invitation and to book a place, please click on the links in the email alerter.

25 February 2014 – Seminar on retirement issues

An afternoon seminar aimed at employers and trustees. Speakers from the Hogan Lovells pension and employment teams will consider a variety of recent and forthcoming issues, including the proposed extension in April 2014 of the right to request flexible working to all employees and the practical implications of the abolition of the default retirement age. To pre-book a place, please click on the links in the email alerter.

7 March 2014 – Recent developments in pensions

Our regular informal breakfast seminar aimed at trustees and sponsors of occupational pension schemes and their advisers. Speakers from the Hogan Lovells pension team will review legal developments over the past few months and will explain the practical implications for pension schemes. To pre-book a place, please click on the links in the email alerter.

Recent publications

We are delighted to attach our most recent briefing notes, on directors' remuneration and notification obligations in respect of employer-funded retirement benefit schemes (EFRBS), plus our revised briefing on pension liberation.



VAT CASE - NEWS FLASH

In an Opinion given on 12 December 2013 in a Danish reference, *ATP PensionService A/S v Skatteministeriet*, the Advocate-General (AG) has recommended that the ECJ should decide that investment management services supplied to defined contribution pension schemes should be exempt for VAT purposes, provided two requirements are satisfied:

- the beneficiaries bear both the cost of the fund and the risk of the investment (which, the AG commented, will generally be the case with defined contribution as opposed to defined benefit schemes)
- the beneficiaries have an unconditional legal right to their investment – whether a fund fulfils this requirement will be a matter for the national courts to decide, although the AG suggests that the fact that payments out of the fund are made only on retirement is irrelevant.

If the ECJ follows this Opinion (which it is not obliged to do, although it often does), the case should open the way for defined contribution plans to make claims for overpaid VAT and interest. It may also result in lower fees for such plans in the future.

DEFINED AMBITION

The DWP is consulting on proposals for reforming future workplace pension provision.

Flexible defined benefit

- Indexation requirements would be removed for pensions in payment.
- With the cessation of DB contracting-out, statutory requirements for survivors' benefits would be removed.
- Changing pension age to reflect improved longevity would be made easier. Employers would not be permitted to adjust members' pension age within 10 years of reaching their scheme's existing normal pension age.
- Compulsory transfers out to a nominated DC fund would be allowed for active members who cease service before retirement.
- In existing DB schemes, the proposed additional flexibilities would apply only to future accruals.
- A statutory override would enable employers to make changes to future accrual. Employers would not have power to transfer or modify benefits already accrued, beyond the extent allowed under current legislation

DC plus

Four models are considered:

- Model 1 - Money-back guarantee
- Model 2 - Capital and investment return guarantee: the guarantee would be purchased by a fiduciary on behalf of the member to secure a guarantee (using standardised insurance terms and conditions) against part of the capital and possibly an investment return, for a fixed period.
- Model 3 - Retirement income insurance: each year from, for example age 50, a fiduciary would use part of a member's fund to buy (on the member's behalf) an income insurance product insuring a minimum level of income. At retirement, the member draws their pension directly from their remaining fund and only if the fund is reduced to zero would the income guarantee insurance be drawn. The full guarantee would remain, provided that the individual does not draw more than the guaranteed income from the fund. The DWP considers that introduction of this option is unlikely in the short or medium term.
- Model 4 - Collective risk sharing that could provide a guaranteed pension income ("pension income builder"): a proportion of the member's fund would be used each year to buy a deferred annuity, payable from current pension age. The residual contributions would be invested in a collective pool of risk-seeking assets, used to provide future indexation on a conditional basis.

FROM THE PENSIONS REGULATOR

Regulating defined benefit pension schemes

The Regulator has issued a consultation paper on regulating DB pension schemes, plus a draft funding code of practice, draft regulatory strategy and draft funding policy, to replace the previous documents in force since 2006.

The draft code emphasises that the Regulator will adopt an integrated approach to managing the key risks of a DB scheme: funding, investment and the employer covenant. The Regulator has adopted a suite of risk indicators around these key risks.

The new code is expected in force by July 2014, to apply to schemes undertaking valuations from that time.

Asset-backed contributions

The Pensions Regulator has published guidance for trustees considering using asset-backed contribution arrangements (ABCs) to fund DB pension schemes. The Regulator acknowledges that ABCs may help employers to meet their obligations to schemes and may, in some circumstances, improve a scheme's security. Before entering into an ABC, trustees should consider whether there are any less risky alternatives to support the scheme, such as an appropriate recovery plan and contingent assets.

Double counting in DB schemes

The Pensions Regulator has issued a statement warning schemes against "double counting", that is considering payments under a schedule of contributions to be payments towards s75 debts and vice versa. It advises that double counting may jeopardise eligibility for the Pension Protection Fund where it constitutes a legally enforceable agreement to reduce the amount of a section 75 debt due to the scheme. The statement is intended to apply also to past occurrences of double counting.

FROM THE TAX MAN

Autumn statement

The Chancellor has issued his Autumn Statement 2013. Points of interest relating to pensions include:

- The Basic and Additional State pension will be specifically excluded from the overall cap on welfare spending.
- The guiding principle for future reviews of State pension age will be that people should expect to spend, on average, up to one third of their adult life in receipt of the State pension. The DWP has stated that adult life will be considered to start at age 20. The intention is to give individuals affected by changes to State Pension age at least 10 years' notice.
- Employer National Insurance contributions (NICs) will be abolished for under-21 year olds earning less than £813 per week.
- The Basic State Pension will be increased in April 2014 by the higher of average earnings growth, inflation or 2.5% (the "triple lock").
- Current pensioners, and those who reach State pension age before the introduction of the single tier pension, will be given the option to pay a new class of voluntary NICs to top up their Additional State Pension entitlement.

Individual protection – Finance Bill

Following the Autumn Statement, draft clauses have been issued for the Finance Bill 2014. The Bill will implement the lifetime allowance individual protection 2014 (IP14) regime, to be available as from 6 April 2014. Following consultation, the draft provisions have been amended to make IP14 available to individuals with enhanced protection, provided that they do not have primary protection on 6 April 2014.

Overseas – QROPS guidance

HMRC has set out its policy in relation to imposing unauthorised payment charges in respect of unauthorised transfers to overseas schemes.

- From 24 September 2008 onwards, HMRC's list of QROPSs has stated explicitly that inclusion on the list does not mean that HMRC had verified all the information provided and that a transfer to a scheme which is not a QROPS could give rise to tax charges.
- HMRC will not raise or pursue tax assessments where:
- the transfer from the registered scheme took place before 24 September 2008;
- the receiving scheme was included on HMRC's QROPS list at the time of the transfer; and
- the scheme was not a QROPS.
- For transfers made on or after 24 September 2008, where a transfer is made to a scheme on the QROPS list and HMRC later discovers that the scheme is not a QROPS, HMRC will decide whether or not to exercise its tax collecting powers on the particular facts.

Employer-financed retirement benefits schemes (EFRBS) – "resolution opportunity"

HMRC has written to employers who are the subject of open enquiries about EFRBS entered into before 6 April 2011, offering to settle the enquiries by agreement. Broadly, employers wishing to take advantage of the offer will be expected to agree that either:

- no corporation tax deduction is due for contributions made to the EFRBS until relevant benefits are paid out of the EFRBS; or
- PAYE and National Insurance contributions (NICs) are payable on the contributions to the EFRBS. A corporation tax deduction may be made in respect of contributions to the EFRBS.

FROM THE PENSION PROTECTION FUND (PPF)

Finalised levy determination

The PPF has published its 2014/15 Levy Determination and confirmed that the 2014/15 pension protection levy estimate will be £695 million, as originally proposed. In a change from previous years, a contingent asset may be recertified if it has been certified in at least one of the previous five years, provided certain conditions are met.

Pensions Bill: compensation cap

The Pensions Bill has been amended so that provisions increasing the PPF compensation cap for members with 20 or more years' pensionable service have been extended, to apply the cap to individuals already entitled to PPF compensation.

Pension sharing on divorce

The PPF has included information on the treatment of pension sharing cases in its latest issue of Technical News. Where a cash equivalent transfer value is requested in relation to a divorce and the scheme is in an assessment period, trustees should consider whether it is appropriate to base calculations on PPF levels of benefit.

DEFINED CONTRIBUTION (DC) SCHEMES

Pensions Bill

- a) Charges, governance and administration requirements

The Pensions Bill has been amended to give the DWP power to restrict the charges that may be imposed on members of certain work-based schemes and to impose requirements relating to administration or governance in relation to work-based schemes. Power will also be given to impose duties on the trustees or managers of such schemes. The new powers are wider than those in the Bill as originally drafted as they will enable the requirements to be imposed on schemes closed to new members or to further accrual, rather than only schemes to be used for the new small pot automatic transfer system.

- b) Short service refunds

Technical amendments have been made to the provisions in the Bill withdrawing the option of making short service refunds from money purchase occupational schemes. The amendments are intended to ensure parity of treatment with individuals who are contract-joined into a workplace personal pension scheme (who are subject to a 30 day cooling off period) and those joining an occupational scheme who will, in effect, be subject to a 30 day vesting period. Prior to the amendment, members of an occupational scheme would have had a right to short service benefit from the date contributions were paid to the scheme.

Pension Regulator: code of practice

The Pension Regulator's code of practice 13, "Governance and administration of occupational defined contribution (DC) trust-based pension schemes" has come into force. Regulatory guidance for DC schemes and the Regulator's compliance and enforcement policy were published at the same time.

Consultation on charging

The DWP is consulting on restricting charges levied in relation to auto-enrolment schemes or qualifying schemes used to meet the employer enrolment requirement. Changes proposed include the following.

Disclosure of information:

- Including information about charges in the basic scheme information given to members when joining a scheme and in annual benefit statements;
- Standardised disclosure to employers of costs and charges at the point of sale through a code of conduct and on an ongoing basis by mandating information provided to employers;
- Mandatory disclosure of transaction costs to members, employers, trustees and independent governance committees.

Capping charges for default funds in qualifying DC schemes at:

- 1% of funds under management;
- 0.75% of funds under management; or
- A two tier "comply or explain" cap: 0.75% cap with a higher cap of 1% available to employers who explained to the Pensions Regulator the reasons for the higher charges.

Master trust assurance framework

The Institute of Chartered Accountants of England and Wales (ICAEW, in partnership with the Pensions Regulator, has issued a draft assurance framework intended to help trustees of DC "master trusts" demonstrate to potential and existing customers that their scheme is being run to a high standard. Master trusts would be expected to obtain independent assurance annually.

Definition of "money purchase" benefits

The statutory definition of "money purchase benefits" is due to change on 6 April 2014. The new definition will overturn the decision of the Supreme Court on 27 July 2011 in the Bridge case, which held that certain benefits (such as some defined benefit underpins and pensions provided from a DC scheme (internal annuitisation)) were money purchase benefits even though deficits could arise in relation to them.

The DWP is consulting on various consequential amendments and transitional provisions in relation to several areas, including: winding up, section 75 debts, revaluation and indexation, transfers and early leavers, surpluses, administration, the PPF, scheme funding, disclosure and auto-enrolment. In many cases, schemes will not have to revisit decisions made from 1 January 1997 to 28 July 2011 (the date the DWP announced it would legislate to overturn the Bridge decision). Decisions made after 27 July 2011 may have to be reviewed in certain circumstances.

Statutory money purchase illustrations

The Financial Reporting Council has issued a consultation paper on proposed amendments to Technical Memorandum 1 (TM1), which sets out the method and assumptions to be used in producing statutory money purchase illustrations (SMPs). The amendments reflect changes introduced by the new disclosure regulations in force on 6 April 2014.

FROM THE DWP

Disclosure of information

New disclosure regulations come into force on 6 April 2014 and will combine the disclosure requirements for occupational and personal pension schemes. The existing regulations will be revoked. The new regulations also incorporate disclosure requirements in relation to auto-enrolment and qualifying schemes.

Where a scheme contains provision for lifestyling, a statement explaining lifestyling, its advantages and disadvantages, and when it has been or will be adopted must be given to members in various circumstances.

Miscellaneous amendments: draft regulations

The DWP is consulting on draft amendment regulations.

Scheme auditors

- The eligibility conditions for being a scheme auditor in the Scheme Administration Regulations will be amended to

allow, in certain circumstances, someone prohibited from being a statutory auditor of the sponsoring employer under the independence conditions in the Companies Act 2006 to be a scheme auditor. The relaxation will apply in respect of trust-based, multi-employer occupational schemes where at least two-thirds of the employers are not associated or connected and there at least 500 sponsoring employers.

Discharge of liability

- The Discharge of Liability Regulations will be amended to clarify that the statutory discharge will apply to trustees who secure benefits by purchasing an annuity or insurance policy which allows members to take a proportion of their benefits as a lump sum, provided certain conditions are met. A similar provision was inadvertently removed when changes were made to the taxation of pensions in 2006.

FROM THE LAW COMMISSION

Fiduciary duties of investment intermediaries

The Law Commission has issued a detailed consultation paper considering the fiduciary duties of investment intermediaries. In relation to ethical investment, the Commission considers that:

- Wider factors relevant to long-term investment performance, including environmental, social and governance issues, may be taken into account where they would further the purpose of the investment power.
- Macro-economic factors may be taken into account provided that the anticipated benefits of an investment decision based on such factors must outweigh the likely costs.
- Factors relating to beneficiaries' quality of life now and in the future may only be taken into account when choosing between two equally beneficial investments.
- General ethical issues, unrelated to risks, returns or the interests of beneficiaries may only be taken into account in limited circumstances, such as for a DB scheme set up by a religious group, charity or political organisation or where a DC scheme allows members a choice of investment strategies.

PUBLIC SECTOR

Transfers from local government

The Government Actuary's Department (GAD) has announced certain changes in relation to transfers of staff eligible for membership of the Local Government Pension Scheme (LGPS), in the light of the introduction on 1 April 2014 of a new LGPS and of transitional provisions in regulations yet to be laid before Parliament.

FROM THE EU

EIOPA work programme

The European Insurance and Occupational Pensions Authority (EIOPA) has issued its work programme for 2014. Areas of focus include: continuing to develop a new regulatory and supervisory framework for IORPS; solvency issues for IORPS, including continuing to develop the holistic balance sheet approach; personal pensions, with a focus on

consumer protection; charges for occupational schemes; presenting investment choices in a manner that leads to appropriate decisions by consumers; and good practice on transfers between schemes.

Levy to fund EIOPA

The Economic and Monetary Affairs Committee of the European Parliament has recommended granting EIOPA an independent budget, funded by contributions from the pensions industry and taxpayers.

FROM THE COURTS

Moral hazard: time limits for references to Upper Tribunal

The Court of Appeal in Northern Ireland has held that the Upper Tribunal would have power to direct the Pensions Regulator to issue a contribution notice (CN), even though the act which would give rise to the CN had been committed more than six years previously. The Pensions Regulator Determinations Panel had considered whether or not to issue a CN within six years of the act concerned, and it was the date of the Panel's determination which was relevant to the six year time limit.

The case will now revert to the Upper Tribunal (The Pensions Regulator and anor v Annick Desmond).

Suspected pension liberation schemes were occupational pension schemes

The High Court has held that certain schemes suspected of being pension liberation schemes were occupational pension schemes, as defined in section 1 of the Pension Schemes Act 1993. By agreement between the parties, the Court did not consider whether the schemes were fraudulent pension liberation vehicles. On the true construction of the language of the schemes, the schemes were "for the purpose of providing benefits to, or in respect of, people with service in employments of a description or for that purpose and also for the purpose of providing benefits to, or on respect of, other people" (Pi Consulting (Trustee Services) Ltd v The Pensions Regulator and others).

FROM THE PENSIONS OMBUDSMAN

Member had not relied to her detriment on incorrect benefit statements

The Pensions Ombudsman has held that a member subject to an earnings cap whose benefit statements for several years had incorrectly shown her pensionable salary as

uncapped had not suffered financial loss as her overpaid contributions were being returned to her, with interest. However, she had suffered non-financial loss at the "higher end of the scale" and was awarded £800 compensation for distress and inconvenience (Fairfield).

Member had relied on incorrect information but had not suffered financial loss

The Deputy Pensions Ombudsman has held that, although the member had relied on misleading information about the date her bridging pension would reduce when deciding to take early retirement, it had not been shown that she had suffered financial loss as a consequence. Even if there had been financial loss, the member had a duty to mitigate the loss but had not done so (Thew).

This note is written as a general guide only. It should not be relied upon as a substitute for specific legal advice.

KEY HOGAN LOVELLS CONTACTS

Jane Samsworth	(Partner)	+44 20 7296 2974	jane.samsworth@hoganlovells.com
Katie Banks	(Partner)	+44 20 7296 2545	katie.banks@hoganlovells.com
Duncan Buchanan	(Partner)	+44 20 7296 2323	duncan.buchanan@hoganlovells.com
Claire Southern	(Partner)	+44 20 7296 5316	claire.southern@hoganlovells.com
Edward Brown	(Partner)	+44 20 7296 5995	edward.brown@hoganlovells.com

"Hogan Lovells" or the "firm" is an international legal practice that includes Hogan Lovells International LLP, Hogan Lovells US LLP and their affiliated businesses.

The word "partner" is used to describe a partner or member of Hogan Lovells International LLP, Hogan Lovells US LLP or any of their affiliated entities or any employee or consultant with equivalent standing. Certain individuals, who are designated as partners, but who are not members of Hogan Lovells International LLP, do not hold qualifications equivalent to members.

For more information about Hogan Lovells, the partners and their qualifications, see www.hoganlovells.com.

Where case studies are included, results achieved do not guarantee similar outcomes for other clients. Attorney Advertising.

© Hogan Lovells 2013. All rights reserved. #4478536