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What's Happening in Pensions

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- **Finance (No. 2) Act 2017:** The latest Finance Act confirms the reduction of the money purchase annual allowance to £4,000 and the improved income tax exemption for employer-financed pensions advice, both from 6 April 2017.
- **VAT:** HMRC will allow employers' currently permitted VAT recovery practices in relation to fees for services to DB pension schemes to continue indefinitely. It will, however, remove the VAT exemption for investment management services provided by insurers from 1 April 2019; and the High Court has ruled that EU law does not require HMRC to apply that exemption to the same services provided by non-insurers.
- **Money laundering regulations 2017:** HMRC's position on the record-keeping and registration requirements of these regulations is becoming clearer. The first potentially applicable registration deadline is 5 January 2018.
- **Automatic enrolment review:** The government has published proposals for changes in the mid-2020s to the automatic enrolment regime, including the automatic enrolment of workers from age 18 and a requirement for all pay up to the upper threshold to be pensionable.
- **PPF compensation:** The High Court has held that a member who transferred benefits to a DB scheme and was given a fixed pension transfer credit was entitled to have the PPF compensation cap applied separately to his two pension entitlements. The government has revised its proposals for how PPF compensation will be calculated for members with bridging pensions.
- **Contracting-out:** HMRC has announced that it no longer intends to write to individuals with details of their contracted-out history.
- **DC charges:** The government has consulted on proposals for the detailed disclosure of costs and charges information to DC occupational pension scheme members. The government will be making no changes for the time being to the 0.75% cap on member-borne charges in DC scheme default funds.
- **DC bulk transfers:** The government has consulted on draft regulations to relax restrictions on DC bulk transfers made without member consent between occupational pension schemes (including transfers to master trusts).
- **Inflation:** The CPI increase figure for the year to September 2017 was 3.0% (RPI: 3.9%). The September figure is used for increases to state pensions and for revaluation and indexation under many occupational pension schemes.

- **21st century trusteeship:** The Pensions Regulator has added a new page to the "21st century trusteeship" section of its website, on "Clear purpose and strategy". It encourages schemes to have a formal business plan.
- **Pensions Ombudsman – non-financial loss:** The High Court overturned a Deputy Pensions Ombudsman "distress and inconvenience" award of £500 and substituted an award of £2,750. The distress was caused by repeatedly inaccurate benefit statements and communications over a long period, which the judge said served to increase the level of distress when the errors were discovered.
- **GARs – personalised risk warnings:** The government has published guidance on new obligations that will require personalised risk warnings to be given to members who are considering giving up the benefit of guaranteed annuity rates or other similar guarantees.
- **Master trust regulations:** The government is consulting on draft regulations setting out more detail of the regime for authorising and regulating master trusts and its scope.
- **NEST:** The Government and NEST have been consulting in relation to changes to the NEST rules.
- **Accounting:** The FRC has issued a revised version of Practice Note 15: The audit of occupational pension schemes in the United Kingdom. The FRC has published a report with expectations for improvements in companies' pension disclosures.

Finance (No.2) Act 2017

The Finance Bill has received Royal Assent and is the Finance (No.2) Act 2017. It includes the following pensions provisions, both of which have effect for the current (2017/18) and future tax years:

- reduction of the money purchase annual allowance from £10,000 to £4,000 (see our **briefing note** for details); and
- improvement of the income tax exemption for employer-financed pensions advice, including an increase from £150 to £500 and no requirement for the cost of the advice to be within that limit.

VAT

Services to DB pension schemes

HMRC has issued revised **VAT Input Tax Manual pages** which reverse its previously announced decision to tighten VAT recovery rules that are used by many employers in respect of fees for services provided to their DB pension scheme.

HMRC had previously announced that it would be changing its rules but had allowed employers to continue their existing practices for a transitional period which was most recently due to expire on 31 December 2017.

Employers' currently permitted VAT recovery practices can now continue indefinitely. This includes:

- the practice of addressing invoices to employers so that they can deduct VAT in respect of scheme administration services (but not investment management services); and
- the deemed 30%/70% split where a supplier provides the scheme with both administration and investment management services.

The new manual pages also confirm HMRC's views on the tax consequences of three other ways by which employers might claim VAT deductions. There are, however, difficulties with all of these and specific advice will always be required.

Fund management by insurers

HMRC also recently announced in an update to its **Brief 3 (2017)** that it will be discontinuing its policy of allowing insurers to treat their supplies of non-SIF (special investment fund) pension fund management services as VAT exempt insurance. It originally announced that this change would take effect on 1 January 2018 but then put it back to 1 April 2019.

DC schemes are SIFs and so qualify for the SIF exemption (and will continue to do so) but DB schemes are not. It therefore appears that insurers will charge VAT on pension fund management services they provide to DB pension schemes from 1 April 2019.

United Biscuits case

The High Court has given its **judgment** in the *United Biscuits* case. In this case, HMRC was challenged on its current and historic practice of exempting investment management services supplied to DB schemes by insurers but not the same services supplied by fund managers.

The High Court held that HMRC's current practice is not in breach of the relevant EU directive and declined to refer the question to the European Court. The judge rejected the trustee's arguments, effectively holding that pension fund management services are not insurance and so should not be exempt from VAT even when provided by insurance firms.

As noted above, HMRC had already announced an end to the VAT exemption that it currently applies for insurers' investment services provided to pension schemes. This will mean that, at least from April 2019, there will be "fiscal neutrality" between insurers and non-insurers but in a way that is more favourable to HMRC than to schemes such as the United Biscuits scheme.

The *United Biscuits* decision and HMRC announcement affect only DB investment management fees. Where the benefits are DC then, as noted above, the separate SIF VAT exemption applies and will continue to apply.

The judge commented that if he had decided the case the other way, the scheme's remedy would have been against the investment services providers, not HMRC, and that a four year time limit would apply.

Money laundering regulations 2017

We recently issued a **briefing note** on new requirements under the 2017 money laundering and terrorist financing regulations. These require trustees:

- to keep certain records of scheme beneficiaries and others;
- to disclose information on request to law enforcement authorities and certain other parties; and
- if the scheme pays tax, to register with HMRC and provide certain information.

The record-keeping and disclosure obligations are in force now but HMRC has been gradually developing its views on what records are required to be kept by trustees of occupational pension schemes and what information is to be registered with HMRC.

The first potentially applicable registration deadline is effectively 5 January 2018. The other is 31 January 2018 but since we originally published our briefing note, HMRC has announced that it will not apply penalties for missing that 31 January 2018 deadline if the registration (where required) is completed by 5 March 2018. The briefing note mentioned above has been updated to reflect this development.

Automatic enrolment review

The government's **automatic enrolment review report** has proposed significant changes to the scope of the automatic enrolment regime but not soon and with caveats. The report says that:

"Our ambition is to implement these changes to the automatic enrolment framework in the mid-2020s, subject to discussions with stakeholders on the implementation approach during 2018/19, finding ways to make these changes affordable, and evidence of the impact of the increases in statutory minimum contribution rates in April 2018 and April 2019."

The headline proposals are as follows:

- Automatic enrolment will be extended to 18 to 21 year olds.
- The automatic enrolment earnings trigger will still apply. It will be kept at £10,000 pa for 2018/19.
- All earnings from the first pound up to the upper threshold (currently £45,000 pa) will be pensionable (ie, the exemption for earnings below the lower threshold, currently £5,876 pa, will no longer apply). This is designed in part to help those with more than one part-time job.
- There will no longer be a category of "entitled workers" (ie, those entitled to be offered access to a pension arrangement but with no employer contributions required).
- Automatic enrolment is not to be extended to the self-employed.
- There are no current plans to raise minimum contributions rates any further than as provided for under existing legislation (but with the review mentioned above to follow the April 2019 increase).

PPF compensation

Fixed pension transfer credits

In ***Beaton v Board of the Pension Protection Fund***, the High Court held that a member who transferred benefits to a DB scheme and was given a fixed pension transfer credit was entitled to PPF compensation calculated separately for his two pension entitlements, ie, with the compensation cap applied separately to each entitlement rather than to his aggregate benefits.

The PPF had applied the compensation cap to his aggregate benefits, resulting in a significant benefit reduction. The Pensions Ombudsman had rejected Mr Beaton's complaint that the PPF was wrong to do this but the High Court found in Mr Beaton's favour. The judge referred the case back to the Ombudsman to consider other outstanding issues but we understand that the PPF has sought permission to appeal.

If the decision stands then it would appear to have consequences not just for the PPF but also for the benefits payable from an occupational pension scheme, for example where scheme benefits are calculated by reference to PPF compensation in a winding-up.

The judge noted that the result would have been different if the transfer credit had been in the form of added years of pensionable service, rather than a fixed pension. In such a case, the PPF compensation cap would apply to the aggregate benefits. The compensation cap does not apply to DC transfer credits.

Bridging pensions

The government **has consulted** on **draft regulations** to change the way that Pension Protection Fund compensation will be calculated for members with bridging pensions or similar arrangements.

At present, individuals receive PPF compensation based on the starting level of the scheme pension for the whole period of payment, even if the scheme pension would have been reduced after a certain period. In an earlier consultation (see **WHiP Issue 66**), the government had proposed that PPF compensation be adjusted and paid on a smoothed basis over the beneficiary's lifetime. In the light of responses, however, the government has changed its proposal so that PPF compensation will start at a higher level and reduce at around the same time the scheme pension would have done.

The regulations are intended to come into force on 24 February 2018 and would apply only to members of schemes that enter a PPF assessment period on or after that date.

Contracting-out

HMRC announced in **Countdown Bulletin 30** that it no longer intends to write to individuals with details of their contracted-out history. These letters had been expected to result in queries to trustees about inconsistencies.

DC charges

Investment charges

The government **has consulted** on draft regulations and guidance on the detailed disclosure of costs and charges information to DC occupational pension scheme members. Trustees of schemes that provide money purchase benefits (other than very small schemes, public service schemes and schemes with only AVC money purchase benefits) would be required to:

- report in the chair's governance statement on the costs and charges for each default arrangement and each alternative fund option which the member is able to select, rather than on the range of costs and charges; and
- make costs and charges information available free of charge on a publicly accessible website, which must be referred to in annual benefit statements and must give an illustration of the cumulative effect of charges and transaction costs on the value of a member's pension pot.

The regulations are expected to come into force on 6 April 2018 but will not necessarily require immediate disclosure (except, it seems, for the website information): the other requirements are based around the end of the scheme year and the chair's governance statement. We will report in more detail on the final regulations.

The FCA will consult on corresponding rules for workplace personal pensions in the new year.

Charges cap

In a **written statement to Parliament**, the pensions minister confirmed that the government will be making no changes for the time being to the 0.75% cap applicable to member-borne charges in default funds in DC schemes used for automatic enrolment. The 0.75% cap has applied since April 2015 (see **WHiP Issue 51**). The minister hinted, however, that a change might be expected in 2020.

DC bulk transfers

The government **has consulted** on draft regulations to relax restrictions on DC bulk transfers made without member consent between occupational pension schemes (including transfers to master trusts).

With effect from 6 April 2018, the following changes would apply in respect of such transfers:

- No actuarial (or other) certification will be required if:
 - the transfer is to an authorised master trust (NB the master trust authorisation regime will not be in place until October 2018); or
 - the trustees have taken independent advice from an investment professional.
- The current condition that the transferring and receiving schemes are related will be removed.
- Where the charges cap applies to a member (broadly, where the scheme is a qualifying scheme used for automatic enrolment), the cap will continue to apply to the member under the receiving scheme (ie, even if the receiving scheme is not used for automatic enrolment).

The following qualifications should be noted:

- Trustees would not be given a statutory discharge. The government says that this is because they should remain at risk of claims regarding the choice of receiving scheme.
- The relaxations would apply only to the transfer of "pure" money purchase benefits (so not, for example, cash balance benefits or money purchase benefits with guaranteed annuity rates).
- The relaxations will not apply to transfers to group personal pension schemes.
- The government has passed on to HMRC comments about Finance Act 2004 restrictions that impede DC bulk transfers. One such restriction is that for the "block transfer" easements to apply, so that certain Finance Act protections can be retained after a transfer, all of a member's benefits have to be transferred. This causes difficulties for hybrid schemes seeking to transfer out only their DC liabilities.

Inflation

The CPI increase figure for the year to September 2017 was 3.0% (RPI: 3.9%). The September figure is used for increases to state pensions and for revaluation and indexation under many occupational pension schemes.

The lifetime allowance will increase by 3.0%, to £1,030,000 for 2018/19.

A 3.0% increase will apply to state pensions under the triple lock, this figure being higher than 2.5% and the national average earnings increase figure (2.2%).

21st century trusteeship

The Pensions Regulator has added a **new page** to the "21st century trusteeship" section of its website, on "Clear purpose and strategy". This encourages schemes to have, and regularly review, a business plan. The page has a link to a sample business plan and (more detailed) sample annual planner spreadsheet.

Pensions Ombudsman – non-financial loss

In *Smith v Sheffield Teaching Hospitals NHS Foundation Trust*, the High Court overturned a Deputy Pensions Ombudsman "distress and inconvenience" award of £500 and substituted an award of £2,750. The distress was caused by repeatedly inaccurate benefit statements and communications, which the judge said served to increase the level of distress when the errors were discovered.

The errors concerned a right to retire early on unreduced pension, which Mrs Smith lost by not being in a particular role in the five years before she retired. She had taken another role on the basis of incorrect information from her employer. The wrong information was given on another two occasions. She said that she retired in reliance on the information and would otherwise have continued working.

The employer offered Mrs Smith £5,000, including in respect of her claim of financial loss, which she rejected. The Deputy Pensions Ombudsman determined that she had not suffered financial loss, due to a redundancy payment and increased pension scheme benefits, but awarded her £500 for distress and inconvenience.

Mrs Smith lost her appeal to the High Court on the financial loss point, on the grounds that the Deputy Pensions Ombudsman's decision could not be described as lacking any evidential foundation or as perverse or irrational. On the question of non-financial loss, however, the judge was satisfied that the Deputy Pensions Ombudsman had made an error in the application of principle, including that:

- the Deputy Pensions Ombudsman appeared to have found only one instance of maladministration but there were several;
- the number of instances of maladministration is material to the likely level of distress;
- distress at learning that the information provided over a six year period has been inaccurate is likely to be of a different order from that occasioned by a single instance; and
- There was a period of about four months in which Mrs Smith's entitlement to a full or reduced pension was the subject of debate which prolonged the period of distress and uncertainty.

The judge then considered that he was required to exercise the compensating power afresh and awarded £2,750. He added that the fact that no financial loss was caused was no reason to reduce this figure.

GARs – personalised risk warnings

The government has published **guidance** for trustees and others on new obligations due to come into force on 6 April 2018 that will require personalised risk warnings to be given to members who are considering a transfer or benefit conversion that would involve giving up the benefit of guaranteed annuity rates or other similar guarantees. See **WHiP Issue 65** for background to this requirement.

Master trust regulations

The government **is consulting** until 12 January 2018 on draft regulations setting out more detail of the regime for authorising and regulating master trusts, which is due to commence on 1 October 2018. See **WHiP Issue 64** for background.

The Pension Schemes Act 2017 defines a master trust scheme as an occupational pension scheme which provides money purchase benefits and is used or intended to be used by two or more employers, but not only by employers who are connected to each other and is not a relevant public service scheme. The new draft

regulations address the question of when employers are connected. They also disapply and apply the authorisation regime to certain categories of scheme, with particular consideration given to mixed benefit schemes that primarily provide DB benefits.

NEST

The Government **has consulted** on **draft regulations** to make changes to the NEST rules. The regulations would amend regulations to:

- allow participating employers to contractually enrol their workers in NEST;
- clarify that individuals may join NEST in the event of a bulk transfer with consent and require that any amount must be applied to a member's account as a result of a bulk transfer;
- give NEST the ability to close members' pension accounts that have no funds if certain conditions are met; and
- require NEST to carry out research with members and participating employers and their representatives, in connection with the operation, development or amendment of the scheme.

NEST **is now consulting** on changes to its rules to reflect the above changes and some other changes, including with regard to the payment of lump sum death benefits.

Accounting

Scheme accounts

The FRC has issued a revised version of **Practice Note 15: The audit of occupational pension schemes in the United Kingdom** and a **Feedback Statement and Impact Assessment**. The revisions reflect:

- revisions to UK auditing standards;
- changes to UK accounting standards and the revision of the pension SORP;
- continuing developments in regulatory codes and guidance issued by the Pensions Regulator;
- legislative changes; and
- the increase in master trusts in the pensions sector.

Company accounts

The FRC has published a **thematic report** to help companies improve the quality of their pension disclosures when preparing their next report and accounts.

Sixty companies were informed, before their year-end, that the FRC would review one of three themes in their next reports and accounts. Many companies responded by improving the quality of their reporting in the selected area. The FRC has now analysed the enhanced information and recognises the most significant improvements, including extracts from the better disclosures which most closely matched the FRC's expectations.

TRAVERS SMITH

With regard to pension disclosures, improvements that were observed included the following:

- Many companies provided more information about the risks and uncertainties arising from their pension schemes.
- Better explanations of why there was a marked increase in companies' pension deficits and the actions to address the issue.

The FRC says that it will continue to challenge and expect change by those who do not:

- disclose the information needed to support an understanding of how pension-related risk may affect the amount, timing or uncertainty of future cash flows; or
- clearly explain the basis on which different plan assets have been valued.

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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: Susie Daykin, Daniel Gerring, David James, Dan Naylor, Paul Stannard and Philip Stear.

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