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New Pensions Bill Announced

The Government plans to include a(nother) Pensions Bill in its legislative programme for the 2016/17 session of Parliament. The Bill, announced in a set of background briefing notes accompanying the Queen's Speech on the State Opening of Parliament[1], will provide more protection for members of master trusts, remove barriers for those wishing to access their pension savings flexibly and establish a new financial guidance body.[2]

Master trusts

The Bill will require master trusts to demonstrate that they meet strict new criteria '*before entering the market and taking money from employers or members*' and imbue the Pensions Regulator with new powers with which to supervise them. Baroness Altmann confirmed to the Financial Times that the new provisions would also apply to current master trusts, and would involve a capital requirement to ensure that member funds are not diminished by wind up expenses if the master trust goes bust.[3]

Exit charges

The Bill will cap early exit fees charged by trust-based occupational pension schemes and create a system that allows consumers to access the pension freedoms without '*unreasonable barriers*'. Similar provisions, making the Financial Conduct Authority responsible for capping contract-based early exit charges, have been introduced by the *Bank of England and Financial Services Act 2016*.[4]

Financial guidance body

A new pensions guidance body will be created by the Bill. It will bring together the Pensions Advisory Service, Pension Wise and the pensions-related services offered by the Money Advice Service. The aim of

[1] <www.gov.uk/government/uploads/system/uploads/attachment_data/file/524040/Queen_s_Speech_2016_background_notes_.pdf>.
[2] <www.gov.uk/government/speeches/queens-speech-2016>.
[3] *Queen's Speech, Pension Savers receive new protections*, ft.com, 18 May 2016 (subscription required).
[4] See our article below, *Cap on Early Exit Charges*.

the new body will be to provide '*access to a straightforward private pensions guidance service for customers*'. The Money Advice Service will be replaced by a new money guidance body charged with '*identifying gaps in the financial guidance market to make sure consumers can access high quality debt and money guidance*'.

The speech also announced a Lifetime Savings Bill that will put in place the framework for Lifetime ISAs.

The Regulator's 2016 DB Funding Statement

The Pensions Regulator has released a Funding Statement setting out its expectations for the round of defined benefit (DB) scheme valuations that are due to have effective dates in the year to 21 September 2016.[5]

Statutory funding valuations with effective dates in this range are expected to take account of the revised Code of Practice.[6] In keeping with one of the main themes of the Code, the 2016 Statement advocates an integrated risk-management (IRM) approach, which takes a holistic view of the interactions amongst funding strategy, investment and sponsor covenant. The Regulator counsels trustees to consider the sensitivity of assets and liabilities to economic developments. In particular, maturing schemes are urged to give some thought as part of their IRM plans to how they might ensure that their cash-flow needs are met, so as to avoid having to make forced sales of assets.

Deficit-recovery plans

The Statement recognizes the volatility in the financial markets of late, making specific mention of the uncertainty surrounding the outcome of the forthcoming EU referendum. It emphasizes the importance of adopting a longer-term view, and advises trustees to consider whether post-valuation-date experience should be taken into account in their recovery plans.

The Regulator anticipates that valuations in this tranche will reveal larger-than-expected deficits. However, its analysis leads it to believe that most sponsors can afford the higher contributions necessary to eliminate those deficits within the time frames already set out in existing recovery plans.[7] Candid conversations are expected to take place if affordability is in question. The Statement stresses that schemes must be treated fairly if business investment is taking precedence over scheme funding.

Assumptions

Trustees are generally expected to assume lower returns from most asset classes than they did for their previous valuations. The Regulator asks that they reconsider the yield-reversion assumptions that they may have made, and whether the time is right to activate contingency plans associated with past assumptions that have not panned out as hoped.

Trustees who set their assumptions about life expectancy using information produced by the Institute and Faculty of Actuaries' Continuous Mortality Investigation (CMI) may take account of the latest version of the CMI Mortality Projection Model, CMI_2015; however, the Regulator cautions that there is very little evidence that the reduction in life expectancy implied by this model is indicative of changes to long-term trends, and trustees considering moving to CMI_2015 are encouraged to consider what would happen if the reduction proves to be transient. In a similar vein, it suggests that there is insufficient evidence, currently, upon which to base changes to trustees' assumptions about the likely incidence of transfers prompted by the 'Freedom and Choice' reforms.

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[5] *Annual funding statement* (May 2016) <www.thepensionsregulator.gov.uk/docs/db-annual-funding-statement-2016.pdf>.
[6] *Code of Practice No. 3: Funding Defined Benefits* (June 2014).
[7] *Annual funding statement analysis: A review of defined benefit pension schemes with valuation dates between September 2015 and September 2016 (Tranche 11)* <www.thepensionsregulator.gov.uk/docs/db-analysis-tranche-eleven-review-2016.pdf>.

Valuation deadlines

The Funding Statement advises that the Regulator is more likely to take enforcement action over a tardy valuation if the delay was predictable or if the trustees did not forewarn the Regulator that they were having problems

Future publications

The Regulator intends to produce an analysis of the first block of valuations performed under the influence of the revised Code of Practice and soon-to-be-published guidance on DB investment strategy. It may also, if required, respond to the outcome of the EU referendum.

The 'deck' (sub-heading) in the Regulator's press release is more direct than the Funding Statement that it heralds: taking its lead from the separately published analysis, it says that, '*Despite market pressures*', most schemes '*should be able to at least maintain existing recovery plans.*'[8] The Regulator's analysis, very broadly, sets recent increases in FTSE350 employers' reported profits and balance sheet improvements against a decline in the ratio of deficit-recovery contributions to shareholder dividends. The implication is clearly that employers should, in the phrase beloved of our Chancellor of the Exchequer, '*fix the roof while the sun is shining*'. What it does not mention is that some of those FTSE employers have disclosed accounting surpluses in connection with their DB schemes.

We are pleased to see the Regulator mention the importance of cash-flow planning. When we surveyed trustees for our *Trustee Barometer 2015*, only four per cent saw cash-flow risk as a strategic risk consideration.[9] We developed our *Road to Resilience* risk-management framework to highlight the need to manage capital risks alongside growth and protection. The relative lack of trustee attention to this issue has to change, so that schemes evolve to be both balance-sheet- and cash-flow-risk-resilient before they scale the looming mountain of maturing cash flows (the required drawdown on DB assets is set to rise from £20bn p.a. to £100bn p.a. in the next decade).

Trustees who have established an at-retirement service to help members understand their options are more likely to have built a credible evidence base upon which to make assumptions about likely DB-to-DC transfer rates. Trustees also need to consider how their assumptions about the level of outgoing transfers will feed into their cash-flow planning and liability-driven investment (LDI) decisions, as well as the effect on their technical provisions.

We are surprised that the Regulator did not take a stronger position on CMI_2015 given the widespread concerns about the model.

Cap on Early Exit Charges

The Department for Work and Pensions (DWP) and the Financial Conduct Authority (FCA) have published their proposals for capping early exit charges. This follows research carried out last year which found that early exit charges were deterring some pension savers from taking advantage of the pension freedoms introduced in 2015.

Although the proposals for charges in occupational schemes are likely to be of more immediate relevance for readers, the contract-based regime will be considered here first as the suggested regime for occupational schemes will largely mirror that for contract-based schemes.

[8] *TPR publishes 2016 annual funding statement* (13 May 2016) <www.thepensionsregulator.gov.uk/press/pn16-24.aspx>.
[9] <www.hymans.co.uk/knowledge-centre/surveys-reports/trustee-barometer-2015.aspx>.

Contract-based schemes

The FCA consultation document sets out how it intends to satisfy the requirement under the *Bank of England and Financial Services Act 2016* to limit early exit charges for members of contract-based schemes.[10]

The FCA has suggested that a cap of 1 per cent of the value of the member's pension pot should apply to exit charges for existing contracts and that exit charges be banned completely for new contracts. The restrictions on exit charges will apply to any charge imposed on a member over normal minimum pension age who takes, converts, or transfers their benefits under the scheme before their expected retirement date.[11] Regulations will specify that market value adjustments (MVAs) will not be treated as early exit charges for the purpose of the cap.

The consultation period ends on 18 August 2016 and it is intended that the new rules will take effect from 31 March 2017.

Occupational pension schemes

The DWP has also put forward its proposals for capping early exit charges for members of occupational pension schemes with a view to including the necessary legislative provisions in the forthcoming Pensions Bill.[12] For occupational schemes, the Government plans to mirror the FCA's proposed cap level (of 1 per cent of the member's fund value) for existing contracts and prohibit exit charges completely for new contracts for occupational schemes. The DWP also plans to use the same definition of exit charges as is used for contract-based schemes (set out above) and apply exclusions for MVAs in occupational schemes in line with those for contract-based schemes.

The Government's current understanding is that the main source of early exit charges is the contractual arrangements that trustees have entered into rather than requirements under the trust deed and rules. The DWP recognises that the proposed cap will affect the contractual arrangements schemes have entered into with third parties and is seeking views on whether there are any concerns that implementing the exit charge cap will result in costs being transferred elsewhere.

The consultation document is also hoping to clarify who, in practice, is likely to impose exit charges in relation to members of occupational schemes. The Government currently believes that 'service providers' are likely to be the source of the majority of exit charges that are applied to the funds of occupational pension scheme members. As such, it is intended that the primary duty to comply with the early exit cap should be placed on service providers and trustees, depending on who actually applies the charge in practice. For future contracts the Government plans to place the new obligation on scheme trustees so that no new arrangements breaching the exit charge provisions are entered into.

The DWP is seeking responses by 16 August 2016 and it expects that the cap will come into force in 2017.

[10] <www.fca.org.uk/news/cp16-15-capping-early-exit-pension-charges>.
[11] As defined in section 33 of the *Bank of England and Financial Services Act 2016*.
[12] <www.gov.uk/government/consultations/capping-early-exit-charges-for-members-of-occupational-pension-schemes>.

The Secondary Annuity Market

Her Majesty's Revenue and Customs (HMRC) has published a consultation document on the proposed tax framework for the new secondary annuity market that the Government proposes to open on 6 April 2017.[13] Consultation ends on 15 June 2016. In conjunction with this, Her Majesty's Treasury (HMT) is, until 2 June 2016, consulting on the draft secondary legislation required under the *Financial Services and Markets Act 2000* (FSMA).[14] Lastly, the Financial Conduct Authority (FCA) has published proposed rules and guidance, for which the consultation period ends on 21 June.[15]

Tax framework

The new tax rules will permit annuitants to assign or surrender annuities—including joint life and deferred annuities—without giving rise to unauthorised payments. Annuities are assigned when all rights under the policies are purchased by third parties; annuities are surrendered to insurers in return for cash sums. This will extend to annuities purchased before 6 April 2006. HMRC is considering whether annuities issued by non-UK insurers should also be capable of being traded in.

In order for the assignment or surrender of an annuity to be authorised, a number of conditions will have to be met which, in turn, depend on whether the proceeds are paid directly to the annuitant as a taxable cash sum, or are used to set up a flexi-access drawdown arrangement or to purchase a flexible annuity. Unauthorised payment and scheme sanction charges will continue to apply in respect of assignments and surrenders that do not meet the new requirements.

The person entitled to an annuity (including a dependant's or other beneficiary's annuity where the original annuitant has died), or the personal representatives of a person whose annuity continues to be paid after death, will be able to assign or surrender it in return for a cash sum. All rights under the annuity policy must be assigned or surrendered and the proceeds must be paid to the person giving up the rights (or their personal representatives). The value of any contingent rights must be paid to the person with the actual rights under the annuity policy. Payment must be in the form of a single cash payment rather than a series of payments and, at the time of assignment or surrender, the person receiving payment must be at least age 55 unless they have a lower protected pension age or became entitled to the annuity on ill-health grounds. To prevent potential abuse, an annuity cannot be assigned to a person connected to the annuitant, to a sponsoring employer or close company connected to the annuitant; or where it is part of a tax avoidance scheme.

Similar conditions apply where the proceeds are paid into a flexi-access drawdown arrangement or used to buy a flexible annuity. In both cases, there is no need to stay with the existing provider. HMRC's intention is that the transition from the existing annuity policy to the new arrangement on assignment or surrender should not generate any annual or lifetime allowance charges; nor will it produce further entitlement to pension commencement lump sum. It will be possible to use assignment or surrender to '*convert*' a single life annuity into a joint life flexible annuity. The proceeds from the assignment or surrender of a deferred annuity will be paid into a deferred flexible annuity or, if the person is under age 55, an uncrystallised money purchase arrangement. It will be possible to divert part of the proceeds to pay for financial advice as long as it was on commercial terms and about the potential annuity transaction. Provided the various conditions have been satisfied, the receipt of a cash sum on assignment or surrender will be treated as pension income subject to the recipient's marginal rate of income tax. Similarly, where the proceeds are paid into a flexi-access drawdown arrangement or used to purchase a flexible annuity, the resulting income

[13] <www.gov.uk/government/consultations/creating-a-secondary-annuities-market-tax-framework>.
[14] <www.gov.uk/government/consultations/creating-a-secondary-market-for-annuities-secondary-legislation/consultation-creating-a-secondary-market-for-annuities-secondary-legislation>.
[15] <www.fca.org.uk/news/cp16-12-secondary-annuity-market>.

will be taxed in the normal way. Payment of tax on receipt of the cash sum will normally operate through PAYE.

Selling an annuity for a cash sum, or receiving income from a flexi-access drawdown arrangement or flexible annuity will generally result in the seller becoming subject to the money purchase annual allowance. As an exception to this, there will be special provision for the surrender or assignment of '*low value annuities*' purchased before 6 April 2016. The Government will work with the FCA to develop an appropriate definition of '*low value annuities*'.

A new benefit crystallisation event (BCE) for lifetime allowance purposes will be introduced where a deferred annuity (other than one purchased prior to 6 April 2006) is assigned or surrendered in return for a cash sum. The amount crystallised by this new BCE will be the cash sum received. On death, any residual cash or flexi-access drawdown funds attributable to the surrender or assignment of an annuity will be subject to the usual (post-pension flexibility) inheritance tax rules.

New information requirements will be introduced which will apply to the insurers who issued the annuities being assigned and surrendered, the various entities buying annuities and those assigning or surrendering their annuities.

Payments under an assigned annuity will no longer be treated as pension income for tax purposes: instead they will be treated as a purchased life annuity (PLA) and taxed depending on the nature and business activities of the buyer. In particular, a person purchasing an annuity as an investment will be subject to income tax at his or her marginal rate on the annuity income, without the tax exemption that normally applies to a part of each payment under a PLA. Subsequent sale of the annuity by that individual would be treated as a chargeable event. The consultation document notes that registered pension schemes do not pay tax on the income and gains from most of their investments, and that the same treatment is '*likely*' to apply to annuities purchased on the secondary market.

Secondary legislation

The Government will introduce secondary legislation to, amongst other things, create new FCA regulated activities covering firms intending to purchase annuities in the secondary market, firms intending to act as intermediaries, and annuity providers intending to buy back annuities that they have issued. The market will not be restricted to UK firms provided at least one firm involved in the transaction is authorised by the FCA to carry out the necessary regulated activity.

The Government has also asked the FCA to consider whether buy back by the annuity provider should always be carried out through an intermediary and, if that is the case, whether there should be a threshold below which providers will be able to buy annuities back directly.

To protect consumers, the existing restrictions on financial promotions under the FSMA 2000 will be extended to the specified activities on the secondary annuity market. In recognition of the complexity of investments in this market, and to prevent retail investment, anyone entering into an annuity assignment agreement as a purchaser will require the appropriate FCA authorisation.

FCA proposed rules and guidance

The FCA believes that there is a '*significant risk of poor outcomes for consumers*' in this market as it will be difficult for them to put a value on their annuities and they are more likely to be older and more vulnerable. The risks to consumers identified by the FCA include running out of money, not receiving value for money, not shopping around, being put under pressure to sell, conflicts of interest between brokers and buyers, fraud and, lastly, insufficient competition amongst buyers.

The FCA's proposals cover the following areas:

- disclosure;
- presentation of offers;
- restriction on charging;
- compensation and prudential arrangements; and
- other regulatory requirements.

Regulated firms '*interacting*' with a potential seller for the first time must provide specified risk warnings and other information before they can proceed. Firms will be required to inform the seller about the compulsory appropriate advice requirement for those with higher-value annuities that was introduced by the *Bank of England and Financial Services Act 2016*. The FCA expects that the annuity provider will carry out this check in practice. Even if not required by legislation, sellers will still be recommended to take advice and all sellers will be encouraged to make use of the extended Pension Wise guidance. Sellers will also be encouraged to shop around for the best value when selling their annuity income. Firms need to inform sellers that consent from any potential contingent beneficiary may be required before they sell their annuity. The FCA wants potential sellers to be aware of the costs of selling their annuity before they proceed. Firms must provide sellers, '*at first contact*', with the types and estimated amounts of any possible charges, and inform them that the annuity provider may cover its costs, directly or indirectly.

Quotations must be in a standard format and include a price comparator using the current open market option price of replacing the annuity. All quotes should be net of any additional costs, such as medical fees, that the firm may charge (estimated if unknown), but they will not need to include those that might be charged by the annuity provider or other third party. There will be a fourteen-day cancellation period in case the seller changes his or her mind.

The FCA proposes to place restrictions on charges for those operating in the secondary annuity market. To avoid any conflicts of interests, brokers in the market must apply a standard charging structure to all sellers based on the services that they offer. Any brokerage fee can be taken from the proceeds of the annuity sale. Annuity providers will be only be allowed to levy charges to cover '*reasonable costs'*, and these must be disclosed to the seller.

The FCA proposes that the sale of annuities falls under the protection of the Financial Ombudsman Service and within the scope of the Financial Services Compensation Scheme. Firms participating in this market will either have to hold minimum capital requirements or minimum levels of professional indemnity insurance. The FCA is also introducing other regulatory guidance to protect consumers, covering record keeping, mental capacity and market fees.

The Government has already pointed out that, for the majority of people, the best course of action is to stick with their existing annuities. The FCA's stated concerns about the potential for poor outcomes is reflected in its proposals, such as the requirement for a price comparator and limits on some charges for brokers and providers. A balance needs to be struck to avoid the situation where the secondary annuity market's growth is restricted because the new regulatory regime makes the new market unattractive to both consumers and other market participants.

It is disappointing that there is no further detail on whether direct buy-back by the original annuity provider will be possible for annuities below some specified threshold. A significant amount of annuity business is written using small pension pots without advice. Direct buy-back would seem an efficient—and likely popular—way of selling a small annuity.

Government Ponders British Steel Pension Cuts

The Department for Work and Pensions (DWP) has published a consultation document setting out some options for separating the British Steel Pension Scheme (BSPS) from its principal employer, Tata Steel UK Limited (TSUK), to improve the chances of finding a buyer for the company.[16]

The scheme and its employer

The BSPS has 130,000 members (14,000 actives, 32,000 deferreds, 84,000 pensioners). It was recently estimated that it has a deficit of £700m on the statutory funding obligation basis, is £1.5bn shy of having the funds necessary to buy out members' benefits up to the level of the compensation that would be paid by the Pension Protection Fund (PPF), and would need £7.5bn to fully secure their benefits.

The parent company of TSUK wants to sell it. The Government is keen to help, so that steel can continue to be made in the UK; however, the costs and risks associated with the BSPS make such a sale unlikely as matters stand presently. The objective of the consultation exercise is to find a way of separating the BSPS from TSUK, whilst keeping it out of the PPF, with a new sponsoring employer, and getting the best result for its members. If a solution is not found, the scheme is likely to fall into the PPF.

The options

The DWP discusses the possibility that its aims could be achieved using an existing legal mechanism, namely a flexible apportionment arrangement, or a regulated apportionment agreement [sic]. However, TSUK's parent company has indicated that it could not afford the costs of securing benefits above the level of PPF compensation if such a route was taken.

The Government is considering making a specific exception, for BSPS members only, to the usual constraints upon the modification of accrued rights.[17] This would allow the trustees, unilaterally, to confine increases to pensions in payment and revaluation of deferred benefits to the statutory minimum levels (the scheme's inflation-proofing rules are currently based upon the Retail Prices Index). The *provisos* for this would be that no further benefits accrue, that a future sponsoring employer is identified, and that the scheme's funding is subject to independent assessment. The trustees would have to agree unanimously that the cuts would be in members' best interests, and the Pensions Regulator's consent might also have to be obtained

Alternatively, the Government could tweak the legislation that allows for transfers without member consent.[18] The idea in this case would be that members could be transferred, in bulk, to a new scheme that would provide them with the same basic pension, but less generous increase and revaluation terms. This option would apply not only to the BSPS, but to other schemes with similar sizes, circumstances and prospects. The trustees would have to agree that the transfer is in members' best interests, and that the scheme is likely to enter a PPF assessment period within twelve months (the transfer would be a precursor to a regulated apportionment arrangement). Members would be able to opt out of transferring, for example, if they would obtain a better outcome from the PPF (as is the case for some BSPS members). The DWP is considering whether the Pensions Regulator's approval should be obtained too. Changes to the law relating to transfers of contracted-out rights would also be necessary.[19]

The BSPS deficit on the PPF's 'section 179' basis (which already assumes no increases on pre-6.4.1997 benefits, and only CPI-based increases—capped at 2.5 per cent—on subsequent accrual) is £1.5bn, and

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[16] <www.gov.uk/government/uploads/system/uploads/attachment_data/file/526731/british-steel-pension-scheme-consultation.pdf>.
[17] Under section 67 of the *Pensions Act 1995*.
[18] Under section 73 of the *Pension Schemes Act 1993* and regulation 12 of the *Occupational Pension Schemes (Preservation of Benefit) Regulations 1991* (SI 1991 No. 167).
[19] The *Contracting-out (Transfer and Transfer Payment) Regulations 1996* (SI 1996 No. 1462).

stripping members' inflation protection back to the bare, CPI-based bones will not fill that hole. It will be difficult if not impossible to ensure the continued support of a robust sponsor. The PPF and those that stand to pay its levies in future will view these proposals askance.

The case has noticeable parallels with the BHS situation, and it again raises questions of the legislative framework of 'guaranteed' benefits that are in too many cases unaffordable. It is also ironic that at the time when MPs are questioning trustees, advisers and the Regulator about whether one corporate group has been allowed to shirk its pension responsibilities (be they legal or just 'moral'), the Government is considering going to great lengths to let another shed its.

The 'rules lottery' that has prevented many schemes from moving away—as the government did—from RPI-based increases is a source of ill-feeling that Parliament has so far declined to remove. Although the DWP is at pains to emphasize the exceptional nature of the concessions that it is prepared to make to safeguard UK steel-making and its associated jobs, it seems inevitable that this will set a precedent for others to approach the Government for help to lighten their pensions burden.

New DC Code of Practice

A new Code of Practice, *Governance and administration of occupational trust-based schemes providing money purchase benefits* has been laid before Parliament.[20] The Pensions Regulator has also published its response to the consultation on the draft Code.[21]

In November 2015, the Pensions Regulator published for consultation its draft Code of Practice 13: *Governance and administration of occupational defined-contribution trust-based schemes*.[22] Revisions to the existing version of the Code, which came into effect in November 2013, were made necessary by legislative developments, in particular the 'Freedom and Choice' reforms and new charge-capping and governance requirements introduced in April 2015.

The Regulator comments that the majority of respondents were supportive of the approach taken in the draft Code. However, it notes a number of responses in relation to the proposed three-day timescale for investing contributions. In light of the feedback received, the final Code has been amended to reflect the fact that not all schemes operate daily dealing cycles. Where they do, the three-day deadline will apply; otherwise, the Regulator will expect funds to be invested on the next available dealing date, and within a maximum of five working days.

The Code was laid before Parliament on 9 May 2016 and will come into force in early July, assuming neither House of Parliament resolves that the Code should not be made.

[20] <www.gov.uk/government/publications/occupational-trust-based-schemes-providing-money-purchase-benefits-governance-and-administration>.
[21] <www.thepensionsregulator.gov.uk/docs/dc-code-consultation-response-may-2016.pdf>.
[22] See our article, '*Regulator Publishes Draft Revised DC Code of Practice*', in *Current Issues* January 2016.

Work & Pensions Committee AE Report

In a report on the progress of automatic enrolment, the Work and Pensions Committee has said that '*pension automatic enrolment (AE) has so far been a tremendous success*'.[23] However, the Committee raises some concerns for the future of the AE regime, namely, the regulation of master trusts, the potential effect of Lifetime Individual Savings Accounts (LISAs), and the challenge of getting small and micro-employers to comply.

Master trusts

The Committee is concerned that '*gaps in pensions regulation have allowed potentially unstable master trusts onto the market*' and that if one of these trusts failed that many scheme members could lose their retirement savings. The Committee wants greater regulation for master trusts including more powers for the Pensions Regulator. Further regulation of master trusts as part of a new Pensions Bill has since been announced.[24]

LISAs

Concerns were raised that LISAs could be seen as a competitor product and alternative to auto-enrolment and that some young people may choose to save in a LISA rather than stay auto-enrolled. The Committee recommends that the Government makes the differences between auto-enrolment and LISAs clear to consumers, and that it carries out research on the effect LISAs will have on auto-enrolment before the 2016 Autumn Statement.

Small employers

The Committee recognises that the process of extending auto-enrolment to the smallest employers will be the '*most challenging phase of AE implementation*'. It recommends that the Department for Work and Pensions (DWP) and the Pensions Regulator focus communications on the financial consequences for small businesses not complying with their auto-enrolment duties.

Security Not Relevant Factor for Transfer Without Consent Certificate

The High Court has ruled that an actuary who is required to give an opinion about a proposed 'bulk' transfer should not take into account the relative security of members' benefits before and after the transaction.[25]

Facts

The case concerned a seriously underfunded defined benefit pension scheme. The principal employer was solvent only because it was being propped up financially by its overseas parent company, which was unwilling to continue to (indirectly) support the scheme.

A plan was devised whereby the scheme (which we will call 'the old scheme', for convenience) would be wound up and its members transferred *en masse* to a new scheme, set up solely for the purposes of the transfer, and sponsored by the same employer. The new, essentially frozen scheme would replicate members' rights under the old scheme, with one important exception: only statutory minimum increases would be made to deferred benefits and pensions in payment (the old scheme provided for more generous escalation). No further benefits would accrue.

All parties accepted that benefit security would be higher after the transfer to the new scheme. If the transaction went ahead, it was believed that all members would receive benefits at least as good as the compensation that they could otherwise expect from the Pension Protection Fund (PPF), and some would

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23 <www.publications.parliament.uk/pa/cm201516/cmselect/cmworpen/579/579.pdf>.
24 See our article above, '*New Pensions Bill Announced*'.
25 *Pollock & Others v Reed & Others* [2015] EWHC 3685 (Ch).

get more. If the transfer did not occur, the principal employer would almost certainly be put under administration, and the scheme would be taken over by the PPF. The trustees considered the new scheme to be sustainable and, having obtained '*a copious amount*' of advice from a broad range of professional advisors, were satisfied that the transaction was in members' best interests.

Transfers without consent

In certain circumstances, legislation permits the transfer of a member's accrued rights without his or her consent. In the case under consideration, the receiving scheme would have been sponsored by the same employer as the transferring scheme, thereby satisfying one of the conditions.[26]

Crucially, however, it is also necessary for the trustees of the transferring scheme to obtain an actuarial certificate saying that the rights acquired as a result of the transfer '*are, broadly, no less favourable*' than the member's rights under the transferring scheme. In the case in question, the transferred members would have acquired rights with less generous increase terms than in their old scheme. The required certificate could therefore only be given if the actuary was able to take account of the increase in benefit security that would come about as a consequence of the transaction.

Judgment

The judge concluded, '*With some reluctance*', having reviewed the wording of the legislation and its evolution, that security of benefits is *not* a factor that the actuary can take into account when deciding whether a transfer without consent will give rise to '*broadly, no less favourable*' rights. It made no difference that the transferring scheme would be wound up.

The judge's feeling of reluctance is probably related to the parties' belief that '*there were no viable alternatives*' to the transaction that would give the members a chance of getting their full benefits. Any other decision would have created a mechanism for the circumvention of the legislation protecting accrued rights.

Latest HMRC Newsletters

Pension Schemes Newsletter #78

Her Majesty's Revenue and Customs (HMRC) has published its 78th newsletter for pension schemes.[27]

This edition clarifies that there will be no (direct) adverse tax consequences for members who apply for lifetime allowance Fixed Protection 2016 or Individual Protection 2016 using the interim application process but who do not follow this up with an online application for a permanent reference number.[28] However, HMRC's look-up service, which will allow scheme administrators to confirm their members' protection status, will only work with permanent numbers. Similarly, a permanent number will be required to allow the protection to be recorded in a person's 'personal tax account' (which will allow people to check their tax records and manage the details held by HMRC).

The Newsletter also explains that the recently modified provision of information requirements (which provide special transitional rules for 2015/16 pension savings statements because of the alignment of pension input periods with tax years[29]) do not change the circumstances in which pensions savings statements must be provided for 2016/17 or subsequent tax years. HMRC also notes that those who are subject to the tapered annual allowance are not prevented from using the mandatory scheme pays facility if

[26] It is also possible for the receiving scheme to relate to employment with a different employer within the same group of companies, or to an outside company if the transfer is happening as a consequence of a transaction (the sale of a business, for example) between the old and new employers.
[27] <www.gov.uk/government/publications/pension-schemes-newsletter-78-may-2016/pension-schemes-newsletter-78-may-2016>.
[28] The interim process will be used by those planning on taking their benefits between 6 April 2016 and July 2016, when the online service becomes available.
[29] See *Current Issues* April 2016, '*Annual Allowance Information Changes for 2015/16*', for further details.

certain conditions are met. These are that their annual allowance charge for the tax year exceeds £2,000 and the pension input amount for the registered pension scheme for the tax year is greater than the general un-tapered annual allowance, currently £40,000. (This means that scheme pays is not required to be offered for those caught by the taper and whose pension input amount is between £10,000 and £40,000.)

Additionally, as a result of several queries on the subject, HMRC has clarified that the payment date for an uncrystallised funds pension lump sum is the date on which the payment is actually made.

The Newsletter also alerts readers to:

- the publication of statistics on the flexible payments made from pensions;
- a consultation exercise on the details of the tax rules for the secondary annuities market[30]; and
- the process for correctly raising queries with the Pension Schemes Service.

The language used by HMRC in previous newsletters suggested that application for permanent FP16 or IP16 reference numbers would be mandatory for those with temporary references, once the online facility becomes available in July 2016. This raised concerns that protection might be retrospectively invalidated by a failure to convert a temporary reference number into a permanent one. Newsletter 78 makes it clear that it will be a case of inconvenience rather than catastrophe; nevertheless, it appears that there is sufficient advantage to be gained from having LA protection reflected properly in the systems being developed by HMRC that members should be encouraged to apply online when they can.

Contracting-out 'Countdown' Bulletin 17

Her Majesty's Revenue and Customs (HMRC) has published its latest Countdown Bulletin, to provide guidance for pension scheme administrators in relation to abolition of contracting-out, which took effect on 6 April 2016.[31] This edition includes information on the guaranteed minimum pension (GMP) checker service, GMP increments, the Scheme Reconciliation Service (SRS) and the scheme cessation process (for schemes that ceased contracting out before 6 April 2016).

Expressions of interest for registration for the SRS (to help scheme administrators reconcile their records with HMRC's) closed on 5 April 2016; HMRC has said that any expression of interest for registration received after this date will be considered if there are '*exceptional circumstances*' for the late application.

The Bulletin states that administrators who have submitted an expression of interest to use SRS will be contacted and allocated a time slot for submitting their queries. Where possible, query submissions will be prioritised based on when the expression of interest was received. To help reconciliation queries be dealt with as efficiently as possible, the Bulletin sets out some items for scheme administrators consider before submitting queries.

We are reminded of the note on the cover of Douglas Adams' novel *Mostly Harmless*, describing it as '*The fifth book in the increasingly inaccurately named Hitchhikers' trilogy*.' These Bulletins were supposed to be a '*Countdown to the ending of contracting out*'.[32] No doubt it would confuse matters if they were re-named 'Count-up Bulletins'. Or perhaps they are still counting down, but now to the date (in December 2018) when HMRC intends to pull the plug on the GMP reconciliation process.

[30] See our article, '*The Secondary Annuity Market*' in this edition.
[31] <www.gov.uk/government/publications/countdown-bulletin-17-may-2016/countdown-bulletin-17-may-2016>.
[32] *Countdown Bulletin No. 1*.

And Finally…

We have been fairly glued to Parliament TV's coverage of the select committee inquiries into The BHS Affair. It's not what you would call action-packed, or suspenseful; and the jokes are rubbish. However, it has at times featured exchanges punctuated with so many catty remarks that *AF* felt like he was watching a reality television show featuring a bunch of *prime donne* competing to see who could show off most for the cameras. (Oh, wait…)

We were also delighted to note that the art of the loaded question isn't quite dead. They weren't quite up to the standard of the usual text-book example '*Answer yes or no: have you stopped beating your spouse?*', but there were still a few uncomfortable moments for witnesses.

The committees seem to be saving the best for last. The season finale is set to feature a tense show-down with the main protagonists in the sale of the high-street retailer. We do hope that the Parliament TV servers can cope…