

# Leaders in Pensions

## Trustee Knowledge Update

Welcome to the February 2017 edition of our Trustee Knowledge Update which summarises recent changes in the law. It is aimed at helping trustees (including trustee directors) comply with the legal requirement to have knowledge and understanding of the law relating to pensions and trusts. This edition focuses on the key legal developments over the last three months.

### Government ([www.gov.uk](http://www.gov.uk))

#### Proposed changes to contracting-out legislation and methodology for equalising for the effect of GMPs

It is generally accepted (and certainly the government's view) that because GMPs are calculated by reference to and paid at age 65 for males and 60 for females, they are discriminatory and trustees must take action to equalise any discriminatory effect. However, which members are better off and by how much, changes over time.

Following discussions with the industry, DWP has proposed a method of equalisation which "involves a one-off calculation and actuarial comparison of the benefits a man and woman would have, with the greater of the two converted into an ordinary scheme benefit". Conversion would be under the provisions of the Pension Schemes Act 1993 and is necessary to prevent further inequalities arising over time through revaluation and increases.

Some changes are proposed to the conversion provisions and consideration is also being given to ensure that there are no adverse tax consequences for members as a result of equalisation and conversion.

In addition, some amendments are being made to existing contracting-out legislation. In particular, from 6 April 2017, fixed rate revaluation will fall from 4.75% to 4%.

**Action points:** Trustees of schemes with GMPs will need to consider this issue in due course but should do nothing until GMP reconciliation exercises are complete and there is a clear timetable for amendments to the conversion and tax legislation.

#### Pension scams consultation

This consultation sets out a package of measures aimed at tackling pensions liberation. In particular, there are proposals to limit the statutory right to a transfer payment so that a member would only have such a right where the receiving scheme was a registered personal or occupational pension scheme (to which a genuine employment link could be demonstrated) or an authorised master trust. Where these conditions are not satisfied, the government expects trustees to make all reasonable efforts to agree to a non-statutory transfer where the receiving arrangement did not appear to be a liberation vehicle.

As an alternative, the government is also considering the possibility of requiring "insistent members" to sign a discharge confirming that they have understood warnings given to them and the risks. This would be accompanied by a 14 day cooling off period, delaying the transfer to allow the member a final chance to consider their position.

**Action points:** This is something to keep a watching brief on at the moment but any changes to the transfer regime will require changes to scheme administration processes which trustees will need to be aware of.

#### Bulk transfers of DC members without consent: call for evidence

The government is seeking views on how the legislation on bulk transfers of DC benefits without consent can be improved. The intention is that any resulting changes to legislation would be made in April 2018.

The call considers the requirement for actuarial certification that benefits are "broadly no less favourable" in the receiving scheme. It acknowledges that the test might not be suitable in a DC context. However, the government is reluctant to rely only on trustees' fiduciary duties and is looking for ways of simplifying or standardising the current requirements for DC transfers or whether an alternative quality requirement might be appropriate.

The current test also requires that either: the transferring and receiving scheme relate to employment with the same employer; or for the transfer to be a consequence of a financial transaction between the transferring and receiving schemes' employers. There are concerns that these requirements might act as a barrier to consolidating small pots or dealing with schemes where the employer has been dissolved. Views are sought as to whether these requirements are necessary.

**Action points:** This is of particular relevance to trustees who may be considering transferring DC liabilities to master trust arrangements. Currently the need for actuarial certification can cause some issues (particularly in relation to investment options and charging structures). Trustees considering such a transfer, should keep an eye on these proposals.

## Legislation

#### Provision of Information Regulations 2017

When a taxable lump sum death benefit is paid to a trust, scheme trustees must provide information to the death benefit trustee on the amount of lump sum death benefit and the tax paid by them. Death benefit trustees must then pass on this information to any beneficiary.

**Action points:** This is relevant for members over the age of 75. It is intended to allow a beneficiary enough information to make a claim for a refund of any tax that the scheme has deducted in relation to the lump sum, above the beneficiary's marginal rate of tax.

#### Occupational Pensions (Revaluation) Order 2016

This order sets out the rate for revaluation of deferred pensions for members reaching normal pension age in 2017. The revaluation percentage for 2016 was 1%.

**Action points:** Where schemes revalue using CPI this sets out how much deferred pension will need to increase by for 2016. This rate will apply whether pensionable service was completed before or after April 2009.

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## Regulator ([www.pensionsregulator.gov.uk](http://www.pensionsregulator.gov.uk))

### Reporting record keeping measures

A survey undertaken by the Regulator has revealed that there has been *"little recent improvement in record-keeping, essential to deliver value for money and protect member outcomes"*. As a result, the Regulator has issued a short four page guide to record keeping. It sets out what information should be kept, the need for annual data reviews and what should be done to keep data secure.

**Action points:** *The Regulator is clear that it expects high standards in relation to record keeping and trustees should ensure that they are taking appropriate steps to meet the targets suggested by the Regulator.*

### Integrated risk management guide for smaller schemes

This is aimed at trustees of smaller schemes who may have more limited resources to implement an integrated risk management (IRM) strategy. It is intended to be read alongside the Regulator's main integrated risk management guidance (published in December 2015). The short guide breaks IRM down into 5 stages and gives examples of how IRM might help in smaller schemes.

**Action points:** *The Regulator highlights the potential benefits and even costs savings of IRM and is clearly keen that all trustees should consider IRM strategies.*

### Response to 21st Century Trusteeship consultation

The Regulator says that it remains committed to driving up standards of governance and has three main proposals to achieve this:

- more targeted education and tools to raise the standards of poor trustees;
- setting out clearly the standards expected from professional trustees and the specific qualities and skills chairs are expected to offer; and
- tougher enforcement against trustees who fail to meet the required standards.

The Regulator does not intend to impose new governance requirements (at least in the short term) but expects trustees who are not already meeting existing standards to do so quickly. It will continue to review the position.

"Extensive" new guidance on investment governance in all schemes is promised for early in 2017 and some existing guidance will be consolidated into "overarching" guidance to make it more accessible for trustees.

On the possibility of requiring a chair's statement in DB schemes, the Regulator says: *"We'll consider with DWP how best to encourage DB schemes to deliver good governance and value for money for their sponsoring employer, and explore which framework – eg scheme return reporting or a more formal governance statement – may work best in the context of DB schemes' specific circumstances and existing reporting requirements"*.

**Action points:** *Trustees need to ensure that governance is an issue that appears on the agenda for trustee meetings and that they are aware of the Regulator's requirements in relation to scheme governance. They should also keep an eye out for the new investment guidance due out soon.*

## Tax ([www.hmrc.gov.uk/pensionschemes/index.htm](http://www.hmrc.gov.uk/pensionschemes/index.htm))

### Chancellor's Autumn Statement

The proposals in relation to pensions include the following:

- The Money Purchase Annual Allowance (MPAA) will be reduced from £10,000 to £4,000 from April 2017. The Government is seeking views on whether the proposed reduction would achieve its policy intentions and whether any groups would suffer a disproportionate impact.
- There will be various changes affecting overseas pensions and pension arrangements. These include the alignment of the tax treatment of foreign pensions with the UK's domestic pension tax and updating the eligibility criteria for foreign schemes to qualify as overseas pensions schemes for tax purposes. HMRC has issued draft guidance on these changes.
- The rules on the taxation of dividend distributions to corporate investors will be modernised in a way which allows exempt investors, such as pension funds, to obtain credit for tax paid by authorised investment funds and proposals will be published in draft secondary legislation in early 2017.

**Action points:** *The main change is the proposed reduction to the MPAA. Any members who have flexibly accessed DC benefits will be subject to the MPAA. Further reductions to the MPAA may affect members' desire to take flexible DC benefits and schemes will also have to update administration practice and annual allowance communications.*

### Pension Schemes Newsletter 83

This contains various updates and reminds members that if they lose Lifetime Allowance protection, they need to notify HMRC in writing, including details of the date that they lost protection and the reason why protection was lost.

There is also a reminder in relation to reporting unauthorised borrowing. Under Finance Act rules, a scheme may borrow up to 50% of the net value of the fund. Borrowing in excess of this limit is unauthorised and must be reported to HMRC.

**Action points:** *This letter serves as a timely reminder to trustees that the various protections offered under the Finance Act (in relation to lump sums, retirement ages and the lifetime allowance) can be lost on making transfers, on augmentations or when alternative benefit options are offered.*

### Countdown bulletin 22

This reminds trustees that the GMP reconciliation process should be complete by October 2018. There will be no facility to raise queries through the scheme reconciliation service after that date and only limited support for individual member queries. It also provides some guidance for trustees on how to interpret the data they receive from the Scheme reconciliation service.

**Action points:** *Trustees of schemes that have GMPs should now be well underway with their reconciliation exercises. If trustees have not already considered how to treat differences between HMRC's records and their own, they should be doing so now.*

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**PPF** ([www.pensionprotectionfund.org.uk](http://www.pensionprotectionfund.org.uk))**2017/18 Levy Policy Statement, Levy Determination and supporting documents**

The PPF has published the 2017/18 levy documentation. The documentation is expressed as provisional because the PPF is still considering a proposal to vary the rules for schemes without a substantive employer but it is clear that there will be no other changes to the rules as published and schemes can rely on what has been published so far.

The key changes from 2016/17 are as follows:

**Schemes without a substantive employer:** The PPF intends to put in place a rule to ensure that the levy is calculated appropriately for schemes which cease to have a substantive sponsoring employer after a restructuring of the pension arrangements to reflect the increased risks that such schemes pose to the PPF.

**FRS 102:** Where an employer has adopted the new accounting standard FRS 102, there are provisions to allow parties to notify Experian of certain differences which have arisen as a result of the adoption of FRS 102 where this has changed the employer's score for risk of insolvency.

**Revised accounts:** When accounts are revised, the revised data will be used to recalculate monthly insolvency scores from the date of the original filing, rather than the date of filing of the revised accounts. The PPF confirms that as the rule only comes into effect in 2017/18 it cannot be applied to prior years.

**Mortgage exclusions:** A mortgage can now count as a refinance mortgage where the original mortgage was entered into by one group company and the refinance mortgage by another. Charges which are not connected to an amount of borrowing, but relate to an amount of money being recoverable in specified circumstances, can now be considered for exclusion on immateriality grounds. Schemes submitting a credit rating certificate on behalf of more than one employer can now do so on a single certificate.

**Parent companies that file small companies accounts:** The relatively small number of ultimate parents who prepare small companies accounts on a consolidated basis will be assessed on the "independent small" scorecard instead of "large and complex".

**Action points:** *The main levy deadline is midnight on 31 March 2017. This means that trustees should ensure that they have completed the scheme return on exchange by that date. Where action is being taken to reduce the levy (such as putting in place a guarantee), the trustees need to act well in advance of the deadline to ensure everything is in place on time.*

**Cases****Goyal v Goyal (Family Court)**

The Family Court has held that pension sharing is not available in relation to foreign pensions. The judge did however accept that there may be alternative routes to dealing with an overseas pension on divorce.

**Action points:** *The extent to which pension sharing rules apply extra-territorially has been debated for some time. This reasoned judgment clarifies the position.*

**Ombudsman** ([www.pensions-ombudsman.org.uk](http://www.pensions-ombudsman.org.uk))**PO-3633 Mr R (Mayfair Construction scheme) - member had no defence to recovery of overpaid lump sum**

Benefit statements received between 2010 and 2012 stated that the member could take a total pension commencement lump sum (PCLS) from his two schemes of around £25,000. However, a revised quotation produced shortly afterwards gave a combined figure of around £85,000. Perhaps unsurprisingly the member, after taking financial advice, took those PCLSs. A few months later he was informed that there had been an error: the correct total lump sum figure was £30,000. When the administrator sought repayment of the balance, the member responded that the money had been spent, telling TPAS that he had spent £51,000 on credit card debts, £14,000 on a car and various sums on other expenses. However, bank account statements, which he disclosed in 2014, showed £43,000 in his account at the time he was told of the overpayment. The administrator said this cast doubt on the member's claim and that he had not been open and transparent, although as a goodwill gesture it offered to reduce the sum owing by £5,000.

The Ombudsman's Adjudicator found that it was not unreasonable for the member not to have queried the higher quotation: he was not a pension scheme expert and was entitled to rely on the advice of his IFA, who did not query the PCLSs quoted and recommended that he take them. However, it was settled case law that repayment of a debt did not count towards a change of position defence, and the member might have incurred the other items of expenditure even if he had not received such a high PCLS. In addition, the evidence of the bank statement suggested that the member had "not shown equitable grounds for him to avoid making repayment". The member did not accept the Adjudicator's decision and the case was referred to the Ombudsman.

For his part, the Ombudsman noted that the car purchase was not completed until three weeks after the member had claimed that all the money was spent: "He went into the car purchase well aware that he might have to repay a large sum". The Ombudsman also agreed that the other expenditure claimed was either incurred after the member knew about the error, or was expenditure he might have incurred even if the overpayment had not been made. The £5,000 offered to the member by way of offset was ten times the Ombudsman's minimum award for distress and was satisfactory compensation in the circumstances.

**Action points:** *This case reaffirms the position that repayment of a debt is not a defence to having to repay an overpayment as presumably, the member can take out new debt and will then be in the same position. It also illustrates the importance of getting as much evidence as possible of a change of position.*

**PO-13059 Mr Y (NGF Europe Pension Fund) - occupational physician assessing future ability to work**

This determination related to the employer's rejection of a member's application for total incapacity benefit. The rules defined "Total Incapacity" as "physical or mental deterioration which, in the Principal Employer's opinion, permanently and totally destroys the Member's earnings capacity", which the employer interpreted as meaning that the member must be incapable of carrying out "any paid employment of any kind" for the 20 years to his normal retirement date. However, the Ombudsman said that "Mr

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*Y's earnings capacity depended on what work he could reasonably be expected to be capable of doing, taking into account his qualifications and work experience."* The Ombudsman criticised the failure by the employer and medical advisers to consistently apply, describe and interpret the relevant rules definition; and the failure of the employer to revert to the medical advisers in the case to clarify the wording.

The Ombudsman was also critical of the employer expecting its occupational health advisers to opine on the member's ability to work in the future. He cited a British Medical Association publication which states the BMA's view, in relation to pensions ill-health retirement cases, that: "Occupational physicians should not be asked to assess patients' ability to obtain work in the future." He went on to suggest that the employer had thus been wrong to attach the weight it had to "a prediction... that was outside the adviser's remit". He directed the employer to take its decision afresh and, after obtaining any further medical evidence or professional advice it required, to convey that decision to Mr Y, giving him its reasons for the decision.

**Action points:** *This determination illustrates the need to ensure that medical advisers asked to determine whether a member satisfies an ill health test should be suitably qualified to judge the medical condition that the member has. Occupational physicians may well not be able to come to a conclusion about some conditions.*

## Miscellaneous

**Data protection** – The Information Commissioner's Office has issued new 2017 guidance on the General Data Protection Regulation which will come into force in May 2018. There had been some uncertainty following Brexit about whether organisations (including pension schemes) would need to comply with this European Regulation, but it seems clear now that they will.

This means that trustees should review their existing data protection arrangements to ensure compliance with the new law and should ensure that data protection is on the agenda for meetings in the second or third quarters of 2017.

**Progress on IORP Directive** – The new European Pensions Directive (IORP II), came into force on 13 January 2017. Member states have until 13 January 2019 to

**Dates for diaries:** Trustee training remains one of the most important ways of ensuring that trustees have the knowledge and understanding required to perform their duties. We will be holding trustee training courses on 21 February 2017, 13 June 2017 and 17 October 2017. If you have any enquiries about these courses or would like to reserve a place, please contact **Kieron Mitchinson** – E: kieron.mitchinson@cms-cmck.com.

If you are interested in any additional trustee or employer training, please contact **Kieron Mitchinson** who can provide you with a list of our current training topics or discuss any particular training needs you might have.

**General:** For further information on our pension services, please contact **Mark Grant** – E: mark.grant@cms-cmck.com, T: +44 (0)20 7367 2325 or your usual pension partner. Please also visit our website at [www.cms-cmck.com](http://www.cms-cmck.com).

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The information in this publication is for general purposes and guidance only and does not purport to constitute legal or professional advice. It is not an exhaustive review of recent developments and must not be relied upon as giving definitive advice. The Update is intended to simplify and summarise the issues which it covers. It represents the law as at 7 February 2017.

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transpose it into national law. The Directive would require trustees to make a number of changes in relation to scheme governance but currently, it is not clear whether Brexit means that the changes to UK law required by the Directive will not be made. The Government has so far said nothing directly on this point so we can only wait and see what happens over the next 12 months or so.

**Extension of pension scheme temporary clearing exemption under EMIR** - The European Commission has decided to extend the transitional relief for pension schemes from central clearing for their OTC derivative transactions until 16 August 2018. It says that without the extension, schemes "would have to source cash for central clearing. As [pension schemes] do not hold significant amounts of cash or highly liquid assets, imposing central clearing requirements would require very far-reaching and costly charges to their business model. This could ultimately affect pensioners' income".

**Office for National Statistics Statement on future of consumer price inflation statistics** – The ONS has announced that CPIH (a variant of CPI which includes a measure of owner-occupiers' housing costs, and has tended to be higher than CPI) is to become its preferred measure of British consumer prices inflation, with effect from March 2017. However, there is as yet no suggestion that the government or Bank of England intend to switch from CPI to CPIH for any wider purposes. The ONS has stressed that RPI will continue to be published, noting that it is used in a large number of commercial contracts, including index-linked gilts. In contrast, RPIJ (a variant of RPI regarded as more in line with accepted statistical standards) will no longer be published.

The statement refers to a letter from the National Statistician in March 2016 which said: "RPI is not a good measure of inflation and does not realistically have the potential to become one. I strongly discourage the use of RPI as a measure of inflation as there are far superior alternatives."

None of this has any direct impact on measures of inflation used for revaluation and increases in pension schemes, but if the government does adopt a new measure in the future, it could lead to even greater uncertainty for trustees trying to work out which measure to use.