SPC news

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in this issue ...

The latest new members of SPC

- **Penfida Partners LLP,** London WC2N 6AA
- **Denton Wilde Sapte,** London WC2N 6AA

New SPC Council

SPC has elected its Council for 2007/2008.
The membership is as follows:-

COUNCIL REPRESENTATIVE		NAME OF ORGANISATION
Mark	Ashworth	The Law Debenture Pension Trust Corporation p.l.c.
Jennifer	Batty	Capita Hartshead
John	Betts	Mercer Human Resource Consulting Limited
Robert	Birmingham	Xafinity Consulting
Terry	Blackmore	Legal & General Group
Lindsay	Davies	Hymans Robertson LLP
Stephen	Dry	Scottish Widows Investment Partnership Limited
David	Fairs	KPMG LLP
Kate	Flavell	HBOS Financial Services
Ian	Gault	Herbert Smith
Mark	Greenlees	Sacker & Partners
Sanjay	Gupta	Watson Wyatt Limited
Liz	Hinchliffe	Prudential
Alistair	Hoare	MNPA Ltd
Duncan	Howorth	Jardine Lloyd Thompson Benefit Solutions
Brian	Huggett	Pearl Group Limited
Kevin	LeGrand	Buck Consultants Limited
Roger	Mattingly	HSBC Actuaries and Consultants Limited
Paul	McGlone	Aon Consulting
Karen	Rhodes	Punter Southall Limited
Cathy	Robertson	Standard Life Assurance
Jane	Samsworth	Lovells LLP
Martin	West	Gissings Consultancy Services Limited
Kevin	Willis	Norwich Union Life

SPC London Evening Meetings

The handouts are available for the following meetings:-

Date	Subject	Speakers
April 25 2007	Personal Accounts – Where will the journey end?	Steve Folkard (Axa and ABI)
May 31 2007	Improving the Sponsor Covenant: an alternative to buying-out	Eric Viet (Aleva)

You can obtain a copy of the handout by clicking on the subject.

We are grateful to Lovells and JLT Benefit Solutions for hosting these meetings.

BUDGET 2007: Extension of financial assistance scheme and the impact of tax rate changes

Financial Assistance Scheme (FAS)

The FAS extends partial protection of benefits to members of schemes being wound up due to the employer's insolvency between 1 January 1997 and 5 April 2005. Alongside the announcement, that its coverage is to be extended to all members affected, was a statement that DWP will set up a review to look at making best use of assets within these schemes.

This suggests that consideration will be given to running something along the lines of the PPF, where available scheme assets are put into a special fund and topped up as necessary by the funding body (the government, in this case), rather than using scheme assets to fund buyout policies.

Rate of Corporation Tax Change

The main rate of corporation tax will be reduced from 30% to 28% from April 2008.

This will reduce the balance sheet effect of deferred tax credits due to scheme deficits, thus increasing the impact of a deficit on the balance sheet by 3%. The "tax shield" associated with borrowing to fund a deficit is reduced by the same amount.

Rate of Income Tax Change

With effect from April 2008, the basic rate of income tax will reduce from 22% to 20%. This will in turn affect the grossing up of contributions to personal pension scheme (and others using the relief at source method) i.e. to invest £100 in a scheme will cost £80 from next April instead of the £78 it costs now. The 10% "starting rate" will be removed for earned income and pensions, but there will be no changes to the rates applicable to dividends, or for savings income and capital gains.

Upper Earnings Limit for NICs

The upper earnings limit (UEL) for National Insurance Contributions will increase by £75 a week above indexation in April 2008 and will be the same as the higher rate tax threshold from April 2009. It is possible that this will be accomplished by a break between the UEL for contracting-out purposes and the UEL for paying the higher rate of NICs. This is already anticipated as part of state pension reform.

Long Dated Gilts

There is a slight decrease in the issuance of long dated gilts i.e. no attention has been paid to those seeking still higher issuance in order to increase supply and hence yields on long dated liability matching gilts.

Taxation After A-Day

There were no real surprises here; most of the measures were simply more concrete versions of the proposed changes announced in the Pre-Budget Report last autumn. ■

SPC Administration Committee meets HMRC

The SPC Administration Committee has had a meeting with HMRC, at which the subjects discussed were overseas transfers (and in particular HMRC's Qualifying Recognised Overseas Pension Schemes listing on its website), HMRC's unauthorised payment processes and benefits paid in two tranches on scheme wind up.

We explained that, from an administrative point of view, the key needs were to deal with **transfers to overseas schemes** compliantly, efficiently and cost effectively. From this point of view the Committee considered that a transfer to an overseas scheme ought to be on safe ground if there had been sight of a letter from HMRC confirming that the scheme had QROPS status and/or the scheme was on the list of QROPS on the HMRC website. Subject to these tests, a transfer to an overseas scheme ought to be able to go ahead without any concerns about a possible subsequent scheme sanction charge.

Sight of a letter from HMRC, confirming QROPS status, generally gave less comfort than the presence of the scheme on the QROPS listing because it was possible to falsify a letter and QROPS status might in any case have been lost after the letter had been produced.

HMRC indicated that, if its QROPS list had been consulted, including at the point of transfer, and there was documentary evidence of this, and a scheme was on the list at that point, a transfer would be on safe ground. It was not an absolute requirement that the list be printed off, although HMRC would prefer it. Ideally, there would also have been sight of the HMRC letter giving QROPS status.

The Committee explained that printing off the list was particularly burdensome. It generates paper, when the overall aim of administrators is to eliminate it, and the list was formatted in such a way that it had to be printed off in its entirety, rather than as single pages.

HMRC commented that, if a scheme was not on the QROPS list, and indicated that this was because it had only recently obtained QROPS status, it would regard a phone call to HMRC to check the position as entirely reasonable.

If it had evidence that it would be appropriate, HMRC would update the list more frequently than monthly, although it did not wish to update it more frequently than at present. However, if a scheme lost QROPS status, HMRC would not wait a month before removing it from the list.

The Committee suggested that it would be helpful to update the list twice a month. It would also be helpful to reformat it with headers and footers, with each page dated, so that individual pages could be printed off as proof that the list had been consulted.

The Committee expressed concern that the list could not be relied upon as a complete record of all schemes with QROPS status. HMRC had already indicated why it could not insist that every scheme given QROPS status be listed. Nevertheless most were on the list. In general, there was every reason why a scheme would want to be listed, although that was not the case so far as schemes for closed groups of individuals ("family schemes") were concerned.

Some schemes which had been accepted as QROPS in the early days were missing from the list, as they had to notify HMRC if they wanted to go on it. However, HMRC had now changed its procedure so that, when a scheme was given QROPS status, it was informed that it would be added to the QROPS list unless it indicated to the contrary.

The Committee indicated that it would be helpful if HMRC would accept from administrators a form of authority from a scheme for HMRC to disclose its QROPS status, even if the scheme had not agreed to be on the QROPS list.

HMRC commented that if a scheme had been on the QROPS list, but was no longer, it would be happy to deal with telephone enquiries. It would either indicate that it had removed the scheme (i.e. it had in effect lost QROPS status) or it would look into the matter. There might be occasions where schemes unintentionally were deleted from the list even though they retained QROPS status.

It was agreed that HMRC would confirm the key points to arise from this discussion in a Pension Taxation Simplification Newsletter.

SPC confirmed that it had encountered no difficulties with the broader overseas transfer regime.

Unauthorised Payment Processes

HMRC indicated that it was still actively considering this area, both from an operational and a policy point of view.

An issue that HMRC said complicated that consideration was the lack, as yet, of any real examples, of which it was aware, where processing of unauthorised payments had had to be dealt with.

SPC commented that emerging problem areas included the following:-

- Triviality lump sums paid in good faith, but the member subsequently notified that he or she had more benefit than at the time the payment had been made, which now rendered it unauthorised.
- Scheme wind-ups, where benefits would have to be reduced, but they could not be reduced for all members due to scheme rules, and unauthorised payments were therefore triggered.
- A child paid benefits, on the basis that he or she was in full-time education, but subsequently discovered not to have been.
- Small money purchase benefits.
- Cash only schemes, where accrual had ceased at April 5th 2006, and now winding up with surplus.
- Small defined benefits, where the member did not complete the paperwork needed to trigger the start of the payments. Eventually these would become unauthorised forfeitures.
- Schemes entering wind-up before HMRC had been able to issue an assessment for the scheme sanction charge in respect of an unauthorised payment.

The Committee suggested that HMRC would probably start to encounter cases in significant numbers in October or November 2007, in relation to cases going back to April 2006.

In many ways the crux of the problem was that under current processes the member had to deal with their own inspector, while the scheme had to deal with HMRC centrally. It would be preferable to have a system under which all dealings were either by the scheme with HMRC centrally or by the member with his or her inspector, with scheme sanction charges not being levied.

The Committee considered it entirely unreasonable that a tax charge of 40% was levied if the member alone dealt with the unauthorised payment, but an additional 15% charge arose if the scheme became involved.

HMRC was sympathetic, but indicated that, for reasons which it had already explained exhaustively, it was not permitted to inform the scheme if the member had already paid tax.

In essence, the Committee said that schemes did not have certainty as to the tax charge on unauthorised payments when they are made and preferred a means of deducting a single tax charge at source and paying it through the accounting for tax return.

The Committee commented that, not withstanding this, the £250 limit for writing off overpayments was far too low and complicated the position on dealing with unauthorised payments. A higher monetary limit or, better, a provision to write off a permitted number of instalments of payment, rather than a monetary amount, would be helpful. The current system left schemes too exposed to the risk that they would have paid benefits in good faith, and remitted the appropriate tax to HMRC, and would subsequently have to bear a scheme sanction charge in respect of the payment.

Benefits Paid in Two Tranches on Scheme Wind-up

We are concerned with the position on the payment of benefits in two or more tranches, when a scheme is winding up (i.e. an interim pension payment and an interim tax free cash sum whilst the financial status of the company is being determined, then a second payment).

In the case of a retirement, which began before A-day, when a scheme is in the position to make a final payment, what should be the treatment of members who had previously been advised that another tax free cash payment would be available? Under the new tax rules, depending on the pension amount, the cash sum may not be as much as they were expecting, if the 25% of benefit value formula produces a lower figure.

We also have the following specific situations in mind:

- On trivial commutation, the payment must extinguish the member's entitlement under the scheme. Therefore, if the member takes what is on offer at the interim payment stage, a second amount cannot be paid. Trustees could give the member a choice between taking a guaranteed sum immediately, or waiting to see if a larger sum might be available, but with no guarantee of amount or payment date. (The need to make a second payment can also arise on transfer out).
- A scheme in wind-up provides members with benefits based on a "best conservative guess" of the funding position. Thus for a retiring member, a pension is set up and a pension commencement lump sum (PCLS) is paid.

At a later stage, when the funding position has been clarified, and there are additional funds available to provide further benefits, a further payment could be treated either as a step-up (BCE3) or as a whole new tranche of benefits becoming due, with a further PCLS entitlement (BCE 1/2 plus BCE 7).

A member could be entitled to a pre A-Day lump sum entitlement more than 25% of the pre A-Day fund (i.e. has "grandfathered cash") with the first lump sum payment based on this entitlement. Unfortunately, one of the requirements for preserving the right to a grandfathered cash sum is that all the member's benefits must come into payment at the same time. What would have been an authorised PCLS, if no further funds were available, becomes a partially unauthorised payment (with tax penalties applying) simply because more funds have proved to be available for the member.

These are just examples of the problems faced during the wind-up process. In general what is absent is flexibility, perhaps a set of transitional provisions, which would enable schemes in wind-up to complete the process of winding up liabilities, without incurring additional tax penalties on members and employers.

HMRC recognises that, when a wind-up takes place, it may take some time to establish the funds available to provide benefits, and so the scheme may pay an interim tax-free lump sum with a further lump sum payable at a later date.

HMRC observes that it is permissible for a pension scheme or arrangement to pay benefits in two or more tranches. Under the new tax regime, each tranche would be a separate crystallisation, and so a pension would need to come into payment each time (although the crystallisation could constitute an increase in the value of an existing pension that is caught by the BCE3 rules). A pension commencement lump sum could also be paid, but its value could not generally exceed the 25% limit set out in paragraph 3 of schedule 29 to the Finance Act 2004. However, if the member had uncrystallised rights to a higher value lump sum immediately before A-Day, that right would be protected after A-Day by virtue of paragraphs 31 to 34 of schedule 36.

HMRC is interested in the likely relative sizes of the two tranches. It suggests that, if the first tranche generally constitutes the greater part of the benefits paid, with the second merely a top-up, then constraining the size of the lump sum payable in the second tranche may make little overall difference to the member.

Commenting on the two specific situations, to which we refer, HMRC confirms that a member taking a single lump sum payment under the trivial commutation rules would need to extinguish all entitlements under the scheme. This would prevent payment of a second tranche of benefits.

Referring to the condition of transitional lump sum protection, that all the member's benefits come into payment at the same time, on which we commented, HMRC states that this helps to prevent complications arising around the calculation of the lump sum payable - particularly where accrual after A-Day creates entitlement to an additional lump sum.

On our suggestion of transitional provisions to give schemes more flexibility during the winding up process, HMRC sees some dangers, on the basis that allowing schemes in wind-up greater latitude in the payments, which they are authorised to make, could open up opportunities for abuse, and perhaps encourage wind-ups for tax avoidance purposes. Targeting the provisions could therefore be difficult.

HMRC suggests that the tax consequences, which we identified, could be minimised through careful management of the winding-up process - so that, for example, benefits to individuals with lump sum protection are, so far as possible, paid in single tranches.

In our view, HMRC is being over-cautious on the prospect of tax abuse, where the context is a wind-up, and we will be meeting HMRC again on this subject. ■

HMRC confirmation on pension input periods

We asked HMRC to confirm its view on retroactive nomination of a pension input period, in relation to the annual allowance.

Within a defined benefits arrangement, the Scheme Administrator (normally the trustees) can nominate the end date of the pension input period. A nomination is effective only once it is notified to the members and, if no valid nomination is made, the end date for the first pension input period defaults to 6 April 2007. It is not possible to extend a pension input period and there can be only one pension input period in any one tax year, which means that, once the default end date applies, it applies indefinitely.

The legislation is not explicit on whether a nomination can be made for a date already passed. We asked HMRC to confirm whether it would challenge such a retroactive nomination, including one which attempts to reach back to an earlier tax year e.g. one made in 2007/08 for a date in 2006/07.

We also sought confirmation of whether HMRC interprets "by notice", in the context of making a nomination by notice – s238(4)(b), Finance Act 2004 - as including displaying an announcement conspicuously (e.g. on a works notice board, or on an intranet).

We also asked for confirmation that the same principles would apply to money purchase arrangements, notwithstanding that members may also nominate the period.

HMRC has confirmed that the legislation allows nominations to be made, stating a date already passed. Such a nominated date may be for a previous tax year. This will enable scheme administrators to, for example, make use of a scheme year as the common point of ending the pension input period for all members. The scheme year can then be used as the basis for the pension input period for later years.

On the actual procedure for providing nominations, HMRC has indicated that it is not involved. A notice is made between the scheme administrator and the member. It is for the scheme administrator to decide on the means to convey a nomination to members, which may be regarded as meeting the requirements of the legislation. ■

Contact continues with HMRC on trivial commutation

For some time SPC and others have been emphasising to HMRC the need to revisit the requirements on trivial commutation lump sums under the new pension taxation regime.

In March of this year, following on from an announcement in the pre-Budget Report for 2006 and follow-up meetings with HMRC in the light of the report, aimed at addressing concerns raised on the conditions, the Occupational Pensions Schemes Joint Working Group, which SPC currently chairs, and which also comprises (for this purpose) ABI, ACA, APL and NAPF has submitted a paper to HMRC, explaining the need for change, and in particular the need for a "per scheme test", rather than one which requires a test on the aggregate of all entitlements. ■

Pension commencement lump sums and members with a money purchase arrangement

One of the issues raised at the most recent HMRC/Occupational Pension Schemes Joint Working Group liaison meeting was the point at which a scheme may pay a pension commencement lump sum (PCLS) in respect of a member with a money purchase arrangement.

This is inextricably linked to "entitlement" to a pension arising. JWG believes that it is only since last July, when HMRC included a new example in RPSM11102050 – described as a "change in interpretation of entitlement" - that schemes started to recognise this issue and that the scale of the problem will escalate both dramatically and rapidly. Currently, many schemes will have committed an unwitting unauthorised payment, and many schemes may be continuing to do so.

It is also JWG's view that, unless the problem is remedied, it will fundamentally undermine Government's intention to encourage individuals to exercise the open market option.

Historically, members of occupational pension schemes would receive their tax-free lump sums on (or very shortly after) their retirement date and the associated pension would be put into payment as soon as possible thereafter. However, it was normal (indeed unavoidable) for there to have been a delay of between a few weeks and a few months in establishing the pension, particularly where the member's options included an open market option. The open market option is now a legal requirement in relation to money purchase benefits.

Until April 2006, the delay in establishing pension payments did not contravene legislation nor did it cause inconvenience for members, because they received their tax-free lump sum almost immediately and this would tide them over until the pension instalments commenced. However, since April 2006, the legal position has been rather different and, strictly, it has not been possible to pay a PCLS until the scheme is in a position to either commence pension payments or to pass funds to the pension provider chosen by the member. Clearly, this can leave members in the invidious position of having inadequate (or no) funds on which to live in the interim.

We are pleased to report that, as we went to print, the government had tabled amendments to the Finance Bill, designed to meet our concerns. ■

Clarification of HMRC position on Australian QROPS

We raised with HMRC a question regarding the tax status of Australian superannuation plans from July of this year, which might have an impact on their QROPS eligibility.

From 1st July, we understand that in Australia both pensions and lump sums payable from age 60 will be tax free. Our concern was that this might prejudice schemes' ability to meet Primary Condition 2b under The Pension Schemes (Categories of Country and Requirements for Overseas Pension Schemes and Recognised Overseas Pension Schemes) Regulations 2006 – SI 2006/206. Also, we understand that tax relief is available to some degree on member and/or employer contributions. This might prejudice schemes' ability to meet Primary Condition 2a.

HMRC has confirmed that, to ensure that from 1 July Australian pension schemes can continue to meet the criteria to receive tax-free transfers from the UK, it will be amending its legislation, so that an Australian pension scheme which currently qualifies to receive tax-free transfers from the UK will continue to do so.

Those Australian pension schemes which feature on the HMRC Qualifying Recognised Overseas Pension Schemes list before 1 July 2007 will not be removed from the list because of the changes to the Australian pensions taxation system. ■

SPC clarifies HMRC intentions on pension commencement lump sums

We welcomed the announcement in the 2006 pre-Budget Report notes of an intended easement, so that a pension commencement lump sum may be paid within 12 months of the member becoming entitled to the related pension, and, if this 12 month period falls in part after the member reaches age 75, the lump sum may still be paid.

However, our understanding is that this easement will not extend to other lump sums which can be paid in circumstances other than death, such as trivial commutation lump sums and lifetime allowance excess lump sums, although we would have thought that these were logical extensions of the easement.

We asked HMRC, if our understanding was correct, why the easement was not proposed to extend to these two types of lump sum.

HMRC has confirmed that our under-standing of the easement is correct and that it will not apply to the two types of lump, to which we referred.

It explains that the key element to this easement is that the member must have become entitled to the pension in connection with which the lump sum will be drawn before age 75. This means that by age 75 the amount of any lump sum is in effect fixed. It must then still be paid within the time limit (currently three months), so it seems unnecessary to impose a further restriction that it must be paid by the time the member reaches age 75.

The proposed extension of the rule for the payment from three months to 12 months is to avoid the potentially harsh results if they are breached, because if the lump sums are paid just a day after the current three month time limit, or on the member's 75th birthday (even if well within the three month time limit), the full amount of the lump sum will be treated as an unauthorised payment. If it had been paid on time it would have been tax-free.

The general rule that no capital may be paid once the member reaches age 75 remains. ■

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HMRC clarifies aspects of relief at source

We asked HMRC to clarify some aspects of the operation of its rules on tax relief at source. Our questions were:-

1. Is it possible for the Technical and Scheme Administrator pages of the RPSM to include guidance on acceptable administration practices where the method of tax relief is relief at source?

The old Relief at Source regulations, which applied before 6 April 2006, were supplemented by guidance published in IR76. The guidance reflected practices agreed by HMRC after considerable discussion with the industry. The old Relief at Source regulations have now been superseded by the Registered Pension Schemes (Relief at Source) Regulations 2005. However, in some areas of the new RAS regulations, particularly those which mirror the old regulations, there is an absence of guidance in the RPSM. An example is the treatment of members with no NI numbers (previously covered in PN14.37b of IR 76).

On 29 November 2004 HMRC held a "Regulations Workshop" to consult with the industry on some of the draft regulations under the Finance Act 2004, which had been issued at that time, which included the draft Relief at Source regulations. The notes taken at the workshop were published to those attending by HMRC. One of the questions asked was "Can the current procedures to obtain National Insurance numbers still be used?" The HMRC answer was "Yes, current procedures can still be used." Concern was also raised that regulations were replacing all discretionary powers. HMRC confirmed there would be areas were statute would permit some discretion, but it would be much narrower than the then current wide discretion, for example in Chapter 1.

Where the new regulations reflect the old regulations, in the absence of any RPSM guidance, it would not seem unreasonable to assume that the administrative practices previously agreed by HMRC under their care and management powers are still acceptable. However, it would be helpful if this could be confirmed or clarified in the RPSM.

2. Can we please have guidance in the RPSM on the practical implications of Regulation 8 of the Registered Pension Schemes (Relief at Source) Regulations 2005, which deals with the procedures which must be followed where the particulars and/or the declaration made by a member are not made in writing?

3. Questions relating to overclaimed tax relief

The scheme administrator will rely on the member notifying it if he or she ceases to be eligible to pay net contributions to the scheme and if he or she has already paid any contributions, which should not have received basic rate tax relief. It is not clear how one can verify the information provided by a member, to ensure an accurate adjustment to the tax claim to HMRC. Before the scheme administrator becomes aware that excessive relief has been claimed, a member's fund might have been used to purchase an annuity, transferred to another scheme, paid out on death or the premiums might have been used to pay life cover premiums.

3a. If HMRC has evidence that a scheme is claiming excessive tax relief in respect of a member will it continue to tell the scheme administrator of the excessive amount claimed?

3b. If a scheme has claimed tax relief from HMRC in good faith and it is not possible for the excess tax relief to be recovered from the individual's fund (eg because this has been transferred or used to pay benefits), or the contributions have paid only for life cover, can the scheme administrator ask HMRC to recover the excess relief direct from the member?

3c. If a scheme administrator is advised by an individual that he or she has exceeded his or her annual contribution relief limit, is there a procedure for scheme administrators to verify the amount of overclaimed tax relief, which the member has received?

3d. If HMRC determines that excessive tax relief has been claimed in respect of an individual's contributions, we assume that the member must decide which scheme or schemes have received the contributions in excess of the member's annual contribution relief limit. Is this correct?

3e. In the situation above, if the member does not tell HMRC which of the registered schemes, to which they have contributed, has received the excess contributions, how does HMRC determine which scheme is responsible for the excessive claim?

HMRC's answers were:-

1. The final Relief at Source Reg-ulations are different from the draft ones used in consultation in relation to the provision of National Insurance Numbers ('NINO's'). The final Regulations no longer reflect the old Relief at Source Regulations in respect of NINOs. Changes had to be made as a result of general work on NINOs that has been going on across the whole of HMRC. The new position on the provision of NINOs is:-

Unless a new member is either under 16, or not a resident of the UK and a citizen of another country other than the UK, a NINO must be provided, or a statement must be made that the individual does not have a NINO.

2. We are reviewing this part of the guidance; however our guidance can only cover what the legislation says

3a. No decision has yet been made on this point.

3b. HMRC only has the power to reclaim overpaid relief from the Relief at Source provider who has made the incorrect RAS claim – for whatever reason. HMRC will reclaim the overpaid relief from that RAS provider, which can, if it wishes then pursue the member/scheme receiving the transfer as appropriate.

3c. No.

3d. The member decides which schemes have received contributions over the relief limit. We would expect that any adjustment would not prejudice the member.

3e. Not applicable. As set out in 3d above it is the member who must decide upon which scheme contributions over the tax relief limit arise

We are pursuing points 2 and 3a of HMRC's response. ■

FRS17 is no longer test for clearance

The Pensions Regulator has indicated that clearance should now be considered, regardless of the funding position of the scheme involved, if a proposed transaction involves significant covenant weakening. This has emerged via a press release issued on 3 May 2007. The press release reinforces a message in the current clearance guidance, that the underlying principle for considering clearance is whether the event is financially detrimental to the scheme. However, it moves away from another previously key message of the current guidance, that clearance need be sought only on events involving schemes which have a deficit on an FRS17/IAS19 basis. Clearance may now be relevant even where funding is above FRS17/IAS19, and, regardless of the current position, trustees are expected to consider seeking revised funding targets or equivalent mitigation above FRS17/IAS19 levels.

The choice of FRS17 as a clearance trigger was intended to give clarity about the levels at which a party to a transaction could expect to be vulnerable to a Contribution Notice or Financial Support Direction, at the time when the current guidance was first issued. However, more recent guidance, for example in relation to the Statutory Funding Objective, has increasingly highlighted that higher targets may be relevant to weak covenants. This change can be seen as more closely aligning the guidance on ongoing funding with that on transactions.

Updated clearance guidance is expected to be issued in summer 2007. ■

Final PPF levy details for 2007/08

PPF has announced the final pieces of its levy formula.

The outstanding pieces of information were the scaling factor required to calculate the risk based levy and the multiplier applied to the value of the protected liabilities to calculate the scheme based levy. PPF had decided to defer publishing these factors until it had analysed the section 179 valuation information submitted by schemes by 30 March 2007, to reduce the risk of under collection.

The main points are:-

- The scaling factor will be 2.47, nearly five times the 2006/07 factor of 0.53. All other things being equal, the risk based levy could increase by 366%. However, in practice other factors affecting the calculation, such as scheme underfunding, will also have changed. The scaling factor proposed in the PPF's December document was 2.02.
- The scaling factor has been calculated ignoring information on deficit contributions or contingent assets. This means that schemes which have taken action to reduce their exposure to the risk based levy will be less exposed to the increase in the scaling factor than those which have not.
- The scheme based multiplier, which is applied to the total value of the protected liabilities regardless of surplus or deficit, will be 0.016%. This is a smaller increase than was expected. Based on this, PPF appears to have estimated the total s179 liabilities of eligible schemes as at 30 October 2006 was £840 billion.

PPF has confirmed that the ceiling applied to the risk based levy in 2007/08 is fixed at 1.25% of the scheme's protected liabilities.

Once the PPF has set the total levy amount it expects to receive over any particular levy year, which is constrained by legislation, it has wide discretion over the levy formula. Provided it undertakes a consultation process before revising the formula, the way the levy is distributed between different schemes could vary considerably from year to year. ■

Pensions Regulator publishes governance discussion paper and DC risk consultation response report

The Pensions Regulator published in April 2007 a discussion paper on the governance of work-based pension schemes and a report on the responses to its recent consultation document on regulating defined contribution schemes in relation to risks to members.

The discussion paper sets out again the areas which TPR views as key in its governance of work-based pension schemes, but states that it is not intended as a definitive statement on all aspects of governance. It is aimed at trustees and advisers of trust-based schemes but also (in chapter 12) covers governance of contract - based schemes, overlapping to a large extent with the matters covered in the money purchase consultation response report published alongside it. It provides case studies and examples demonstrating what the Regulator views as good and poor practice.

The discussion paper reiterates the importance, which the Regulator places on governance, which underlies fulfilment of all its statutory objectives. In each of the seven areas below, which the Regulator describes as priorities for governance, it explains what it sees as the risk to be addressed, what it is already doing in that regard, and what its new proposals are (although in fact it has stated some of these before).

These priorities, and the new proposals, are as follows:

- Knowledge and understanding - continue to promote targeted education and publicise the trustee toolkit.
- Conflicts of interest - issue guidance specifically on this topic and repeat the key message that conflicts must be identified and managed.
- Monitoring of employer covenant - no new proposals, but continued emphasis on the issue.
- Relations with advisers - issue questions to trustees for them to assess suitability of advisers for purpose (for example as regards the use of contingent assets) and check how advisers will manage conflicts. This will stop short of a code of practice although that will be an option, which the Regulator will keep under review.
- Administration - among other proposals (some of which are covered in the money purchase risk consultation paper), develop closer relationships with administrators.
- Processes for investment choice - give examples of processes to aid selection and review of investment managers, funds and options, and examples of clear member information in money purchase schemes.
- Governance during wind up - among other things, target administrators or providers with significant and outstanding wind up portfolios, and provide example project plans.

The Regulator recognises that good governance in trust-based schemes is highly dependent on good trustees but that increased regulation of trustees might put people off becoming trustees - it will check on whether this is happening, via future governance surveys.

The report of responses to the money purchase risks consultation paper summarises responses received to that consultation, which closed in February 2007. The conclusion is that the responses have not changed the Regulator's fundamental approach, but it will consider the responses during the further development of its proposals. However the Regulator emphasises that its aim is not to increase the burdens on those involved in money purchase schemes, but to improve education and the adoption of good practice. ■

SPC response to DWP deregulatory review consultation paper

In March 2007 Chris Lewin and Ed Sweeney, the external reviewers appointed by DWP to lead its deregulatory review of private pensions published a consultation paper outlining some options for possible changes in the DWP's regulatory framework for occupational pensions.

For a copy of the consultation paper, please click here.

In our response we welcomed the review and suggested that if the possible deregulations referred to in the consultation paper were introduced as a package, they could play a significant part in preserving some final salary provision and ensuring that some existing final salary provision kept a defined benefit element, rather than changing to pure money purchase. We also suggested that the impact of the package would be increased if it contained a "headline" element, perhaps a reduction in PPF levy for risk sharing schemes, or even a tax or national insurance incentive.

The impact of the package would, on the other hand, be diminished by measures which sought to temper deregulation with new safeguarding provisions. The more of these safeguards, the more deregulation would become more or less inconsequential tinkering.

For a copy of our detailed response, please click here. ■

Paul Thornton's review of the responsibilities of institutions regulating work-based pensions

Following his earlier informal gathering of views on the responsibilities of institutions regulating work-based pensions, in March 2007 Paul Thornton published a consultation paper covering issues emerging from that informal gathering of views.

For a copy, please click here.

This was a welcome review, although given its importance, whatever the reasons, it is disappointing that it has been carried out to such a short timetable.

Our conclusion at this stage was that there is no evidence to justify bringing any of the bodies referred to closer together or for changing functions or boundaries. Making changes imposes costs on and occupies the attention of both the bodies concerned and the pensions industry, so there needs to be clear evidence of shortcomings, which a bringing together of organisations or a change of functions or boundaries could remedy. Some of the bodies under examination are very new and are as yet untested in the entirety of their roles. Others are, in our view, operating satisfactorily as they currently exist and with their current functions and boundaries.

We suggested that it would be appropriate to repeat this review in, say, five years time.

For a full copy of our response, please click here.

As we went to print, DWP published Paul Thornton's final report, which the government has accepted. For a copy of the report, please click here. ■

Pensions Regulator guidance on abandonment of defined benefit pension schemes

In **SPC News No. 1 2007** we reported SPC's response to a discussion paper from the Pensions Regulator on abandonment of defined benefit pension schemes.

The Regulator has now published guidance for trustees on the subject. For a copy please click here. ■

SPC response to the white paper "*Personal Accounts: A new way to save*"

Since the preparation of **SPC News No. 1 2007** we have submitted our response to the Government White Paper *"Personal Accounts: A New Way to Save"*.

We highlighted the importance of ensuring the target market for personal accounts is clearly delineanated, so that the personal accounts system does not draw in members who are already well served by existing provision. We therefore strongly suggest that the key delineators, e.g. the annual contribution limit, are contained in primary legislation.

It is also essential that a robust basis is established for exempting contract-based schemes from auto-enrolment into personal accounts, given their already significant, and growing, role in pension provision.

For a full copy of our response, please click here. ■

Interruption of the combined pension forecast service

We have been asked by the Pension Service to alert schemes to an important development concerning Combined Pension Forecasts.

The Pensions Bill currently going through Parliament will change the rules governing State Pensions, including the qualifying conditions attached to them and the age from which State Pensions are payable. Once the Bill receives Royal Assent, which it may do at the end of July (but it could be later than this – after the summer Parliamentary recess), the Pension Service will be unable to provide State Pension forecasts until its IT systems have been reprogrammed to reflect the new legislation. This process could take around twelve months.

It is likely that schemes will be given alternative options for this year's benefit statement exercise until normal service can be resumed. For example, if schemes do not wish to make changes to their software, they could continue to send datafiles to the Pension Service but would receive a "nil coding" for each member. Flyers explaining the absence of State Pension projections could then be provided to enclose with members' benefit statements.

Until the Bill receives Royal Assent, State Pension forecasts based on current legislation will continue to be provided. Schemes may wish to keep this in mind when scheduling their annual benefit statements.

The Pension Service's Combined Pension Forecasting Team will be in contact with participating schemes individually to discuss the options available to them and agree with each how they would like to proceed during the intervening period so as to minimise disruption to them. ■

Leavers with less than two years service from money purchase schemes

In **SPC News No. 1, 2007** we referred to the fact that under section 101AB of the Pension Schemes Act 1993 a cash transfer sum is defined as the cash equivalent at the date on which a member's pensionable service terminates. However, in practice, in a money purchase scheme, it would be difficult to disinvest the member's units at their date of leaving, as there is often an interval between that date and the employer notifying the trustees and the administrators of that date. Fund managers might also set deadlines for disinvestments.

We suggested that, to fit in with the way in which money purchase schemes work, the requirement should instead be to quote a sum based on prices at the date of the quotation.

DWP is considering our suggestion and we have had a meeting with the officials responsible for advising ministers on the subject. At the meeting and subsequently we have briefed DWP on the costs and complications caused by the current requirement. ■

The Occupational and Personal Pension Schemes (Miscellaneous) Amendments Regulations 2007

We have made some observations to DWP on the above regulations. These are summarised below.

- We suggested that exemptions were required in relation to section 253 of the Pensions Act 2004, to ensure that occupational pension schemes with their main administration outside an EU member state, which are not tax registered and have no resident UK members, continue to be outside the jurisdiction of UK pension legislation. These regulations do not address the point, but we have now heard from DWP that ministers have agreed that exemptions from section 253 are justified in respect of unregistered overseas schemes and that it hopes to consult fairly soon

- In relation to the "preservation of benefits" regulations (SI 1991/167):-

  a) Regulation 3(3) of the Miscellaneous Amendments Regulations includes a revision to regulation 8(2)(b) of SI 1991/167, to provide that (except where the ill-health condition is met) benefit cannot be paid before a scheme's normal pension age, unless the member has attained "normal minimum pension age" as defined in section 279 of the Finance Act 2004. That definition refers to an age of 50 before 6th April 2010 and to age 55 thereafter. No mention is made, however, of the transitional provisions within schedule 36 to the Finance Act 2004, which allow members to retain a 5th April 2006 "protected pension age". So, beyond 2010 a member might have, say, a protected pension age of 50 under the Finance Act, yet would not be permitted by DWP legislation to take an early retirement pension until age 55.

  We assume that this is not the intention and have asked DWP to confirm this.

  b) No account has been taken of our comment on the draft of these regulations, pointing out that entitlement to short service benefit only arises on termination of pensionable service, so does not cater for the post A-day situation where flexible retirement is permitted.

- Under the Finance Act 2004 liability for payment of tax is with the Scheme Administrator. The new regulation 14(5A) of the Stakeholder Regulations, introduced by regulation 11 of the Miscellaneous Amendments Regulations, states incorrectly that tax liability is with the trustees or managers of the scheme. ■

Stakeholder pensions: employer designation

DWP has sought SPC's views on proposed changes to the legislation governing the stakeholder pension schemes' employer designation requirement. We had few comments on the specific detailed changes, but we suggested that there is a need to take a much broader look at the need for requirements on employer designation of stakeholder schemes after personal accounts have been introduced.

The aim of personal accounts is to encourage saving within the target groups, in order to provide adequate retirement income. Therefore, where a good occupational scheme is available to the individual there will be an exemption from the auto enrolment provisions. Abolishing the requirements for an employer to designate a stakeholder scheme is appropriate where this would otherwise run alongside auto-enrolment into personal accounts.

It would add unnecessary complexity to retain a requirement to facilitate the continuing collection and payment of contributions where individuals and employers would also be caught by the auto-enrolment requirements of personal accounts. In reality the number of active members of the designated stakeholder would quickly fall and retention of the payment requirements does allow members further choice and diversity. However, it would be better if the potential of duplication could be removed.

There are two different situations, i.e. depending on whether the employer contributes to the stakeholder.

A) The employer is not contributing

It is unlikely an individual will opt out if the personal account would force the employer to make a contribution not otherwise being made. Therefore, for example, both employees who have access to an unused designated stakeholder scheme and employees who pay to designated stakeholder schemes, to which no employer contributions are made, may be better served by enrolment into the personal account. A short transitional period before employers are no longer required to facilitate contributions into the stakeholder might be appropriate. However, ideally an employer should not have to collect contributions for payment to more than one scheme for an individual. Instead, the employer could be required to give notice of their intent to cease collection before the commencement of personal accounts. This would allow the individual time to consider making arrangements to pay contributions directly to the stakeholder or make contributions only to the new scheme.

B) The employer is contributing

Here the requirement to continue facilitating the collection and payment of employee contributions should continue for as long as the employer is making their own contributions to the stakeholder. Where these employer contributions cease there should be a similar notice period as applies in **A)**, warning of the cessation and a further trigger for auto-enrolment into personal accounts.

The requirement in **B)** should ideally be matched by the exemption from auto-enrolment where the employer offers access to a stakeholder, to which contributions are made. Just as personal accounts should not replace good occupational schemes they should also not replace existing access to good contract based schemes. This exemption should include existing group personal pension schemes. The existing exemptions for the designation of stakeholder make a good basis for establishing conditions for exemptions for personal account enrolment for good contract based schemes.

The exemption requirements should supersede the residual retention of stakeholder designation provisions leaving any requirement for transitional provisions to apply only to **A)** above. The requirements for personal accounts should not add to the administrative burden for employers who are already contributing to good contract based schemes. Such employers should be encouraged. ■

SPC response to draft revised statement of recommended practice on pension scheme accounts

In **SPC News No. 1 2007** we reported that the Accounting Standards Board had asked the Pensions Research Accountants Group (PRAG) to consult on the revision of Statement of Recommended Practice 1 on Financial Reports of Pension Schemes.

PRAG issued an exposure draft of a revised SORP, a copy of which you can obtain by clicking here.

We have now submitted a detailed response to the exposure draft, which you can obtain by clicking here.

Our main comments were that:-

- The draft SORP erroneously interprets the legislation as requiring Summary Funding Statements to be included within the Annual Report for defined benefit schemes, once MFR is no longer applicable.
- The SORP goes into particular detail, and is very prescriptive, on investment reporting. While this may be by design, in order to increase consistency, it will have adverse consequences at times. Notably, it might force inconsistencies between pension scheme reporting and the reporting for authorised funds and International Financial Reporting Standards and further, by referring to exact treatment of specific investments rather than principles, omissions of particular investments will lead to uncertainty in their particular treatment. This will become an increasing problem as investment markets evolve and new investments (particularly derivative instruments) are widely used by pension funds.

Furthermore, in certain paragraphs there are references to bid value but other areas are not specific as to the valuation basis. We recommended that, rather than have inconsistencies and potential omissions, there is an overriding definition of valuation basis which applies throughout the report unless explicitly stated to the contrary. We note that the move to using bid under accounting valuations is causing difficulties on investments where no bid exists. We recommended that the requirement be to use bid where available and that, where no bid value exists, a last traded valuation basis can be used as an alternative.

We also note that the use of bid will:

- Reduce the reported value of pension scheme assets
- Result in inconsistent reporting, which might give rise to need to run mid and bid reporting in parallel
- understate actual investment performance if a mid to bid performance calculation of performance were used. ■

SPC response to NAPF's review of the Myners principles

SPC submitted a detailed response to the NAPF's review of the Myners Principles in its discussion paper "Institutional Investment in the UK – Six Years On"

For a copy please click here.

For a copy of the discussion paper, please click here. ■

About SPC

SPC is the representative body for the providers of advice and services needed to establish and operate occupational and personal pension schemes and related benefit provision. Our Members include accounting firms, solicitors, life offices, investment houses, investment performance measurers, consultants and actuaries, independent trustees and external pension administrators. Slightly more than half the Members are consultants and actuaries. SPC is the only body to focus on the whole range of pension related functions across the whole range of non-State provision, through such a wide spread of providers of advice and services. We have no remit to represent any particular type of provision.

The overwhelming majority of the 500 largest UK pension funds use the services of one or more of SPC's Members. Many thousands of individuals and smaller funds also do so. SPC's growing membership collectively employ some 15,000 people providing pension-related advice and services.

SPC's fundamental aims are:

(a) to draw upon the knowledge and experience of Members, so as to contribute to legislation and other general developments affecting pensions and related benefits, and

(b) to provide Members with services useful to their business.

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