SPC news

Issue No. 4, 2009
Issued in September, 2009

in this issue ...

SPC News No. 4, 2009

If this issue of SPC News was forwarded to you, and you would like to receive a copy direct from us, please e-mail Carla Smidt at SPC

(carla.smidt@spc.uk.com)

Forthcoming SPC London Evening Meetings

Date	Speakers	Subject	Venue
October 6th 2009	Rick di Mascio (Chief Executive, Inalytics)	Use of Objective Evidence to Improve the Due Diligence Process When Selecting Investment Managers	Jardine Lloyd Thompson Benefit Solutions, 6 Crutched Friars, London EC3N 2PH

We are grateful to Jardine Lloyd Thompson for hosting the meeting. The meeting is preceded by refreshments at 5.00 p.m. It begins at 5.30 p.m and is expected to end at 6.45 p.m. following questions and answers. ■

DMO quarterly consultation

SPC was represented at the Debt Management Office's quarterly consultation in May.

SPC was one of 15-20 organisations represented, including fund managers, hedge funds and representative bodies.

SPC is helping to ensure that the needs of pensions investors are properly considered in forming policy on gilt issues. If these are areas you wish us to pursue, please e-mail john.mortimer@spc.uk.com. ■

SPC meets Pensions Regulator

Following this year's SPC AGM, on May 27th, there was an opportunity for SPC Members to meet senior representatives of the Pensions Regulator, to discuss current issues.

You can read a note of the meeting by clicking here. ■

SPC Contacts

Since the last issue of SPC News, we have hosted or participated in the following:

- Representatives of the SPC Investment and Money Purchase Committees have taken part in PADA roundtables on its investment approach.
- We have participated in an Actuarial Profession seminar on the global financial crisis.
- The SPC Financial Services Regulation Sub-Committee has hosted a meeting with the Financial Ombudsman Service, against the background of the re-negotiation of its Memorandum of Understanding with the Pensions Ombudsman.
- The Sub-Committee has also met representatives of the Serious Organised Crime Agency, to form a better understanding of how the Agency's proceeds of crime work might relate to the pensions business of SPC Members. It was helpful to ascertain that the impact is likely to remain minimal, but the Agency now has the opportunity to contact us if it does have any relevant messages.
- The Chairman of the Sub-Committee has attended one of the periodic briefings organised jointly by the FSA Practitioner and Smaller Businesses Panels.
- SPC, through its Actuarial and Administration Committees, is participating in HMRC and Treasury working groups, advising on technical aspects of valuing defined benefits and on administrative and communication impacts in connection with the restriction on higher rate pension tax relief. ■

The latest new members of SPC

- **Concert Consulting (UK) Ltd**, Bristol
- **ExactVal**, Saint Albans
- **Mn Services**, London EC4

November 4th 2009
Dorchester Hotel, London W1
7.00 pm for 7.30 pm

The attendance for the SPC Dinner is already expected to exceed 300, but it is not too late to book.

Key Information is:

- **Principal Speaker - Dr. Vince Cable**
  (Liberal Democrat Shadow Chancellor and Deputy Leader)
- **Venue**
  The Dorchester, Park Lane, London W1

Duncan Howorth (SPC President and Managing Director, JLT Benefit Solutions) will also speak.

The event promises to provide excellent food and entertainment and, in keeping with one of SPC's key roles, represents a peerless networking opportunity to meet with fellow industry professionals.

Tickets are £155.00 per head and feedback from previous years' Dinners indicates that this is a modest cost which can be re-paid many times over in terms of the useful networking opportunities, which exist to strengthen your business relationships. The price includes pre-dinner cocktails, a five-course meal, half a bottle of wine with dinner, and a liqueur with coffee.

As ever, we are keen to encourage "new blood" at the Dinner and ensure that it continues to offer the broadest possible range of networking opportunities for those attending. To end that, if your company has never previously been represented at the Dinner, the person making the booking will benefit from a special price of £125.00, as will one additional guest.

We have also arranged special hosting for individual bookings, so, even if you are not booking your own table, you will be very much part of the event.

The closing date for ticket applications is October 7th.

As well as the prestige of our principal guest and the excellent value which the Dinner represents, there is now even more reason to book. On the evening, we will be presenting the inaugural SPC Pensions Journalists of the Year Awards, voting for which is currently open

For a Dinner booking form, please click here.

Registered Pension Schemes (Authorised Payments) Regulations 2009

We welcomed the publication of the Registered Pension Schemes (Authorised Payments) Regulations 2009 (SI2009/1171).

Regulation 16 covers "payments of arrears of pension after death", but only if the member had not reached age 75 at death. We can see no obvious reason for this age restriction and its inclusion causes a number of problems. Firstly, we will have a different treatment for arrears payments (rectifying errors) depending on the age at death:

- Before age 75 – authorised – BCE9 - taxed as pension income under ITEPA 2003
- After age 75 – unauthorised – 40% unauthorised payments charge, plus possibly a 15% unauthorised payments surcharge, as well as a scheme sanction charge.

Also, scheme rules might explicitly bar trustees from making unauthorised payments. If so, the only option for such a scheme would be to retain the underpayment, if the member had already attained age 75 by the time of death. This seems unfair from the perspective of the deceased's estate.

Whilst age 75 is already used in the Finance Act 2004, as an upper age limit for lump sum death benefits, this should not be a salient feature in relation to rectifying pension underpayments, which should have been made to the deceased member. For example, SI2006/614 - the Registered Pension Schemes (Authorised Payments - Arrears of Pension) Regulations 2006 – covers arrears of pension to a member whilst still alive, but has no age limitation.

We asked HMRC to comment

It responded that it had considered this point during the consultation on the regulations.

It stated that the reason for the regulation is that certain pension schemes have rules which force them to pay benefits to members when they have died. These are not death benefits as such, because they are not paid as a result of the death of the member. They are paid in relation to that member's rights whilst they were alive.

However, because they saw a read across to the death benefit rules, Ministers wanted to ensure that such death benefits should stop at age 75. HMRC argued that, if it allowed arrears of pension to be paid after age 75, this could lead a member of a defined benefit scheme to refuse to take a pension and, on death after age 75, to get a taxed lump sum benefit. This would give that person the advantage of tax free growth on the investment fund.

We have asked HMRC to explain its reasoning for the payment of arrears of pension after death only being authorised under the Finance Act 2004 if the member dies before reaching age 75.

HMRC mentioned that certain pension schemes have rules, which force them to pay benefits to members when they have died and that, if it allowed arrears of pension to be paid after age 75, this could lead a member of a defined benefit scheme to refuse to take a pension and, on death after 75, to get a taxed lump sum benefit.

However, regulation 16 falls under Part 3 of SI 2009/1171, which is headed 'Pension Errors'. If a member did refuse to take a pension as suggested, it is difficult – if not impossible – to see how this could be considered as a 'pension error'. In other words, we believe such a situation would fall outside Part 3. Accordingly, we cannot see how this supports the age 75 limit.

In addition, HMRC referred to the person obtaining "the advantage of tax free growth on the investment fund", were the age 75 limitation removed. But, by virtue of subparagraph (1)(a), regulation 16 only applies to pension arrears under a defined benefit arrangement. So regulation 16 cannot involve a member benefiting in such a way.

In essence, regulation 16 is meant to allow defined benefit schemes to pay instalments of pension to a deceased's estate, which should have been made to the member whilst alive (but in error were not). This regulation is clearly required, because the Registered Pension Schemes (Authorised Payments – Arrears of Pension) Regulations 2006 – SI 2006/614 – only covered the payment of pension arrears whilst the member is still alive.

Given that regulation 16 is, in effect, concerned with correcting payment errors, whilst the member was alive, we can see no logic in the inclusion of an age 75 limitation.

We asked HMRC to give further consideration to this, leading to a removal of the age 75 restriction.

We have also raised a question with HMRC on "unwinding" any unauthorised payment tax charges already made under Regulations.

These regulations came into force on June 1st 2009 and, for payments under part 3 or part 4, cover payments made on or after April 6th 2006. On the face of it, these regulations convert payments, which were regarded as "unauthorised payments", into "authorised payments". This would seem to require a procedure to "unwind" any unauthorised payment tax charges already made in respect of such payments (ie any associated unauthorised payments charges, unauthorised payments surcharges, and scheme sanction charges under the Finance Act 2004).

It is possible that the intention was that these regulations would only cover pension or lump sum errors identified, but not resolved, before June 1st 2009. In this case, there would be no unwinding of cases already reported/settled. Whilst we acknowledge that this might be a possible interpretation, we believe that the actual regulations indicate otherwise and the impact assessment for the March 12th 2008 Budget states that the intention is to re-classify the affected payments, which were currently treated as unauthorised payments.

We asked HMRC whether it had any special arrangements to deal with these cases. In particular, is there a process to reclaim any unauthorised payment charges already levied and is there a process to abort any tax collection already in the pipeline?

HMRC has indicated that we are correct, in that payments under the regulations made before the regulations came into force were previously unauthorised payments, but are now authorised payments.

If an unauthorised payments scheme sanction charge has been paid, arising from an Event Report in respect of something where it is believed that the charge is now not due, then the scheme administrator should write to HMRC, Pensions Scheme Services, Fitzroy House, Castle Meadow Road, Nottingham NG2 1BD for the attention of the Service Delivery Team, setting out the facts. ■

Reference scheme test and lifetime allowance lump sums

SPC News No. 1, 2009 on page 5, covered some protracted correspondence between SPC and DWP on the interaction between the reference scheme test under its legislation and HMRC's provision for lifetime allowance lump sums.

DWP has now confirmed its position, that current reference scheme test legislation prohibits lifetime allowance excess lump sum payments and there are currently no plans to review the legislation.

When defined contribution contracting out is abolished in the coming years, DWP might need to consider the consequences this could have for defined benefit contracted out schemes, e.g. in terms of permissible transfers. DWP states that it is possible that it will then be able to review the payments which are permitted under the lump sum legislation.

However, this is not to say that, should any review take place, DWP would necessarily make the changes that would permit the lifetime allowance excess to be taken as a lump sum.

We have decided to draw a line under this correspondence for now. ■

Tax treatment of Financial Derivatives under Tax Bulletin 66

In 2008, SPC wrote to HMRC seeking confirmation of the tax position of financial derivatives under Tax Bulletin 66.

The letter was sent at the suggestion of HMRC, following a meeting with the SPC Investment Committee, to give it an opportunity to express a view on types of investment strategy and instruments developed since Tax Bulletin 66 was issued in 2003.

After a long delay, HMRC has responded to SPC's letter.

For a copy of the correspondence please click here. ■

Higher rate tax relief and anti-forestalling

We reported on SPC's representations to HMRC on the anti-forestalling measures arising from the 2009 Budget on pages 3 and 4 of **SPC News No. 3, 2009**.

We have now had HMRC's responses which came in two instalments, and which you can read by clicking here.

We have also highlighted one hitherto little noticed consequence of the restriction of higher rate tax relief. This could be to restrict the UK's access to highly talented internationally mobile executives, needed in the UK for specific projects.

Despite the current economic downturn, these key executives can effectively choose on which projects, and in which country, they wish to work. They will expect to be compensated for the effects of the proposed restriction of higher rate tax relief in the UK.

There are ways of achieving this, for example through the use of unregistered pension schemes, but these can involve a deferral of corporation tax relief for the employer concerned, which can call into question the cost benefit value of setting up such an arrangement. ■

DWP consultation on draft scheme order and rules for personal accounts

We have responded to DWP's consultation on the draft scheme order and rules for personal accounts. For a copy of the response please click here.

There are a number of important respects, in which we are concerned that proposals in the consultation document would start the trustee of the Personal Accounts Scheme off in the wrong direction. We cover these concerns in our responses to the consultation questions.

For example, DWP asked whether the wording of the draft order adequately covered the activity, which the trustees would need to undertake to raise awareness of the scheme to employers and prospective members.

We fundamentally disagreed with the approach suggested.

We do not believe that the trustee should have any part in, effectively, promoting personal accounts. This is a role which should be fulfilled, in different ways, by the government and the Pensions Regulator, not the trustees of the scheme. The role of the trustees should be to exercise stewardship over the schemes' assets and to administer it in accordance with the scheme order and rules.

DWP also asks what remedies would it be useful for the trustee corporation to have available, in order to deal with employers who persistently fail to meet the agreed terms and conditions of the scheme.

Again, we can consider this question to be misconceived.

We do not consider that the trustee corporation should have any regulatory role. Dealing with non compliant employers should be a matter for the Pensions Regulator.

DWP asks whether the trustees should have the power to change the scheme rules without the agreement of the Secretary of State.

Contrary to the sentiment expressed in the consultation document, we consider that the trustees should have minimal power to change the scheme rules without the agreement of the Secretary of State.

The government has set up personal accounts with specific objectives, the most important of which is to facilitate pension saving for low to moderate earners, who currently tend not to be members of work place pension schemes.

We would expect the government to oversee the development of personal accounts so as to achieve this aim and to continue to exercise oversight of the scheme in operation, through the Secretary of State.

One way in which this oversight should be exercised is to ensure that any rule changes do not compromise the objectives of the scheme.

Earlier in the consultation document there was a suggestion (which we opposed) that the trustee should have a role in raising awareness of the scheme's existence and the nature of the proposition it offers to employers and to prospective scheme members. Given this role, which would in effect require the trustees to "sell" the scheme, it is certainly not inconceivable that the trustee might be tempted to change the rules to make the proposition more attractive, even if this meant departure from the remit set for it by the government.

It is therefore important that the Secretary of State has the power to veto such changes.

We therefore suggested that the trustees should not be permitted to make any changes without the agreement of the Secretary of State, except any needed to comply with pension legislation generally. ■

SPC responds to DWP consultation on Draft Automatic Enrolment and Delegation of Powers Regulations

We have responded to the DWP consultation on the draft automatic enrolment and delegation of powers regulations.

For a copy of the response, please click here.

The response was critical of some of the fundamentals in the draft regulations and suggested move workable approaches in a number of areas.

We have not yet seen details, but on auto-enrolment it appears that DWP might be attempting to meet at least some of our concerns.

For a copy of the DWP consultation, please click here. ■

Pensions Regulator Material Detriment Code now in force

The Pensions Regulator's Material Detriment Code of Practice has been approved by Parliament and came into force with effect from June 29th 2009. The material detriment test elements of the Regulator's new anti-avoidance powers, which were introduced by the Pensions Act 2008, also came into force on June 29th 2009, although these apply retrospectively to acts and failures since April 14th 2008. The new powers allow the Regulator to impose a Contribution Notice (CN) where the new material detriment test has been met (broadly, where a sponsor's actions or failures have a materially detrimental effect on the likelihood of members receiving their benefits) and the Code of Practice indicates the circumstances in which this could happen.

To complement the new Code of Practice, the Regulator has published material intended to provide additional guidance to employers, trustees and advisers "to enable responsible management of risk transfers in a changing landscape". By "risk transfer", the Regulator means actions, which can reduce or transfer the costs of providing benefits under the pension scheme away from the company balance sheet, for example using a buy in (when certain pensions are provided via insurance policies held in the trustees' name) or a partial buy out (when the pensions are provided via insurance policies held by the individual member). The Regulator's message to trustees is that the risk transfer must cause no reduction in member security. Where the risk transfer is to an individual member, the trustees must ensure that the member understands the risk they are being asked to take on and the value of the rights (if any), which are to be given up.

The material includes:

- Brief high-level guidance regarding corporate transactions and the Regulator's powers in respect of the material detriment test. Where such transactions are a possibility, trustees and employers should refer to the Regulator's guidance, which is more comprehensive.
- Brief illustrative examples demonstrating how the material detriment test for Contribution Notices and the Material Detriment Code of Practice might be considered by the Regulator in practice. This includes examples of situations, which would not normally be considered materially detrimental to the likelihood of benefits being received (for example, a partial buy out of pensioner liabilities following due diligence on selection of the provider), and examples of situations, which might be materially detrimental, including:
  - substitution of the sponsor's covenant for that of a weak and/or shell company, or group restructuring which achieves the same result, and
  - an employer and trustee decision to gamble the assets of the scheme on an inappropriate investment strategy because of the existence of PPF and the employer's desire to profit from any upswing (here the risk of a CN would lie with the sponsor, rather than the trustees).
- A new module of the Trustee toolkit, 'Buy-ins and partial buy-outs', to provide guidance to trustees considering transferring pensions risk to insurers.
- In addition, the Regulator's clearance and abandonment guidance have also been updated "for accuracy". ■

Forthcoming draft regulations and consultations from DWP

DWP has supplied a list of forthcoming draft regulations and consultations and you can obtain a copy by clicking here. ■

Abolition of defined contribution contracting-out and protected rights

We have written to DWP on a number of matters related to the abolition of defined contribution contracting-out and protected rights. The letter covers interaction wit the lifetime allowance, inconsistent requirements for member signature, serious ill health commutation, proportioning between protected and non-protected rights and annuity purchase.
For a copy of our letter please click here. ■

The legislation on employer-related investment is changing

The legislation on employer-related investments is changing.

Amongst other things, the Occupational Pension Schemes (Investment) Regulations 2005 cover the rules on employer-related investments. Such investments should generally not exceed 5% of the value of the total scheme investments, but there are some exemptions, as set out in the regulations.

The government is not permitted to allow the exemptions to continue beyond September 23rd 2010 and the regulations have therefore been amended to start to address this. Therefore, with effect from September 23rd 2010, the following investments will no longer be exempt from treatment as employer-related investments and will thereafter count towards the 5% limit:

- Investments derived from the payment of voluntary contributions by members
- Where the investment is in certain 'specified qualifying insurance policies' and the issuing insurer is the employer
- Where the investment is with 'a person who has permission to accept deposits' (for example, a bank) and that person is the employer

Certain other exemptions remain for the time being, but the government is expected to cover these at a later date via further amendments to the regulations. ■

SPC responds to parts of FSA consultation document on the Retail Distribution Review

These were the two questions in the above consultation document, on corporate pension advice, on which responses were required by the end of July. The relevant parts of the consultation document are available by clicking here.

We have the rest of the consultation document under consideration, with a view to replying by the deadline of October 30th.

Our response to the two questions on corporate pensions advice was as follows:

Question 5 (paragraphs 2.30 and 2.31): What are your views on removing this GPP exemption?

While we understand the technical arguments for why the exemption might, as the consultation paper suggests, not be necessary, we suggest that it would be far better, since there is doubt, to retain it, at the very least by referring to it in guidance, in view of its practical value as a "safe harbour" for those involved in this area of business.

Question 14 (paragraphs 4.60 – 4.65): Do you agree that Adviser Charging should be applied, where individual advice is given on GPPs? Do you think that the principles of Adviser Charging should be applied to non-advised GPP business, and, if so, how?

We would answer the first part of this question in the affirmative.

On the second part, the consultation paper itself recognises the need to, as far as possible, maintain parity of regulatory treatment of trust-based and contract-based schemes. This should be kept in mind when deciding how to apply Adviser Charging to non-advised GPP business, so that advice on all work based pensions is on the same regulatory basis. Our suggested approach would be that adviser remuneration should be agreed with the employer and covered through product disclosure, as is the case for commission.

We do not believe that it is the intention, but it is essential that the position is not created, where charges have to be negotiated with each member of a GPP. ■

PPF: Changes to valuation assumptions

PPF is consulting on changes to assumptions for S.143 and S.179 valuations.

For details, click here.

We have considered the changes and informed PPF that they appear to be reasonable. ■

Consultation Paper on a Technical Actuarial Standard for Pensions

The Board for Actual Standards has produced a consultation paper on a Technical Actuarial Standard for pensions.

For a copy of this please click here.

As this issue of SPC News went to print, we had the document under consideration. ■

Foster Wheeler (Court of Appeal decision - Equalisation of Benefits)

This is an equalisation case which is very specific to its own facts, but nonetheless establishes that the principle of minimum interference applies when considering how to amend scheme rules to comply with European law. This means that changes to the scheme rules to comply with European law should only have the minimum effect on the scheme. This is good news to employers as it means that the additional costs of any amendments necessary to comply with Barber requirements are likely to be kept to a minimum.

This case is an appeal by the company from the decision of the High Court. It rests on the specific wording of the scheme's rules which, until they were amended in 2003, did not specify that early retirement reductions will be applied for retirements between age 60 and 65 for any of the members who had Barber window service. Before the amendment, the rules only allowed early retirement from active service with company consent and with an actuarial reduction between the early retirement age and age 60.

The High Court decided that pensions were payable for members who had Barber window service from age 60, and the benefits accrued by reference to a normal retirement date of 65, are payable from age 60 without actuarial reduction for early payment ("deemed consent").

The Court of Appeal decided that in giving effect to European law rights, the court should take a pragmatic approach and that the substantive effect of any changes should only interfere with the scheme rules in a "minimum manner".

The Court of Appeal considered that, in this scheme, one way of complying with European law was to apply the early payment for deferred pensioner rule, so that members with benefits accrued by reference to normal retirement dates of 60 and 65 take early payment of pensions as deferred members in relation to their benefits accrued by reference to a normal retirement date of 65 when they retire between age 60 and 65. The rule, which allows early payment of deferred pensions, allows members to do so with company consent, but with actuarial reduction. It was therefore decided that, if a member of the scheme with benefits accrued by reference to normal retirement dates of 60 and 65, decides to retire between 60 and 65, he/she will be entitled to a single pension, comprising the benefits accrued with a normal retirement date of 60 and with an actuarial reduction of that part of the pension for which the normal retirement date is 65. ■

DBERR publishes consultation paper on Implementation of Agency Workers Directive

The Department for Business, Enterprise and Regulatory Reform has published a consultation paper on implementation of the agency workers Directive.

It is available at www.berr.gov.uk/files/file51197.pdf.

Parts of it (paragraphs 4.18, 6.1 – 6.5 and 7.1 – 7.5) will be relevant to the work of many SPC Member – organisations.

We have responded to the relevant parts and you can read our response by clicking 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.

The Society of Pension Consultants

St Bartholomew House
92 Fleet Street
London EC4Y 1DG
TELEPHONE: 020 7353 1688
FACSIMILE: 020 7353 9296
EMAIL: john.mortimer@spc.uk.com
WEB: http://www.spc.uk.com

SPC News is produced by the SPC Secretary and contributors from Mercer