Technical update

July 2016

Nigel Oakley
Head of Technical Services

Hot topics

EU Referendum

On 23 June 2016, the British public voted to leave the European Union (EU). Whilst it is still early days with regard to the full impact of the vote and the timing and terms of a withdrawal from the EU, what we do know is that, since the UK joined the EU, its pension legislation, has been influenced by EU legislation.

In the short term, EU laws will remain in place but, after the UK leaves the EU, it will give the UK government the scope to amend legislation that stemmed from the EU and is considered overall to not be in the best interests of the UK. However, there would need to be a justifiable cause and appetite to do so as any change would cost time and money. As such, we believe it's unlikely there will be an immediate and significant reduction in legal requirements for UK pension schemes.

Over time, we would expect to see some changes relating to pension case law, as UK courts may no longer need to consider the views of the European Court of Justice when interpreting legislation. There will also be developments in EU legislation that the UK can choose not to adopt, or may wish to adopt.

The ramifications of the vote to leave in respect of UK pensions will become clearer over the coming months and possibly years, but what is clear is that pension legislation in the UK will continue to change and evolve.

The result led to a weakening in the value of the pound and increased volatility in financial markets. At the time of writing, global equity markets have recovered much of their post-vote losses. However, bond yields have fallen further and future market volatility is possible as the market digests the result.

New Pensions Bill

The Queen's Speech on 18 May 2016 announced that there will be a new Pensions Bill, the main aim of which will be to provide protections for people in master trusts. However, it will also look to remove barriers for consumers who want to access their pension savings flexibly, and restructure the delivery of financial guidance.

The main elements of the new Pensions Bill are expected to be as follows:

- There will be strict new criteria for new master trusts to meet at commencement;
- The Pensions Regulator (TPR) will have increased powers to authorise and supervise master trusts;
- Early exit fees charged by trust-based occupational pension schemes will be capped and unreasonable barriers to accessing pension freedoms will be removed;
- A new pensions guidance body will be created as a combination of The Pensions Advisory Service (TPAS), Pension Wise and the pensions services offered by the Money Advice Service (MAS); and

- A new money guidance body will replace the MAS and will be charged with identifying gaps in the financial guidance market to enable consumers have access to high-quality debt and money guidance.

The Queen's Speech also announced that there will be a Lifetime Savings Bill to provide for the introduction of Lifetime ISAs.

Government consultation on British Steel Pension Scheme

The government recently published a consultation between 31 May 2016 and 23 June 2016 to cover options relating to the British Steel Pension Scheme (BSPS).

Although the consultation issues are specific to BSPS and may not have a direct impact on other pension schemes, it is a development which is likely to be of interest to many involved with occupational pension schemes, including employers.

The consultation is seeking views on various proposals relating to BSPS to assist the sale of steel plants and the viability of an on-going steel industry in the UK. This reflects the thoughts that a purchaser would not currently be willing to take on the pension scheme as a part of any deal, which could jeopardise finding a buyer.

The consultation set out four options for dealing with the BSPS, which are:

1. Using a regulated apportionment arrangement to separate BSPS from its employer.
2. Triggering the section 75 debt due to BSPS (although the consultation suggests that this is not an affordable option).
3. Enabling the BSPS trustees to reduce future pension increases and revaluation under the BSPS to statutory minimum levels. This would involve the government passing legislation to exempt the BSPS from the restrictions under section 67 of the Pensions Act 1995. Trustees would be unable to reduce members' benefits without their consent otherwise.
4. Enabling the trustees to transfer members' benefits to a new scheme which only provides pension increases and revaluation at statutory minimum levels. Again the government would need to pass legislation to enable a transfer without members' consent in these circumstances.

It is the third and fourth options that have been referred to most often in the news and it will be of interest to employers, trustees and pension scheme members to see how the issues raised in the consultation are developed within a consultation response.

Other developments

Secondary annuity market

Following its call for evidence and publication of its response, HMRC and HM Treasury have published consultations seeking views on the potential scope for the operation of a new secondary annuity market. The consultations closed on 2 June 2016 and 15 June respectively.

The proposed changes include allowing existing annuitants to be able to sell their income stream to a third-party (if the annuity provider consents) or surrender it back to the issuing insurer.

The reduced £10,000 money purchase Annual Allowance will apply where an annuity is surrendered or sold, unless these are both 'low value', although what is meant by 'low value' has not yet been defined.

Individuals will be able to receive the purchase price directly or to have the sale proceeds paid into a flexible annuity or flexi-access drawdown account. Whichever route is followed, the seller will be taxed on the amounts they receive under PAYE.

This right is not being extended to individuals in receipt of an income from a defined benefit scheme pension. However, it will be available where such a scheme pension has been bought out as an annuity.

The government intends the market to be implemented by 6 April 2017.

...continued

Pension Protection Fund (PPF) levies – 2015/16 and 2016/17 years

The 2016/17 PPF levy will be based on information submitted in the Scheme Returns and updated information on the Pensions Regulator's online system, Exchange.

The deadlines for the 2016/17 levy year were as follows:

- Scheme returns (including any voluntary section 179 valuations) have been submitted by midnight on 31 March 2016;
- PPF certifiable deficit-reduction contributions have been submitted by 5pm on 29 April; and
- Full block transfers that have taken place before 1 April 2016 will need to be certified and submitted by 5pm on 30 June 2016.

We expect the 2016/17 PPF levy invoices will arrive in September 2016.

European pensions legislation

The European Insurance and Occupational Pensions Authority (EIOPA), the European pension regulator, released a response in April 2016 to a consultation on the solvency of pension schemes which suggests that it has ended its work on a solvency-based funding regime for pensions.

This is seen as a good outcome for pension schemes in the UK and Europe as, if implemented in the UK, a solvency-based system was anticipated to have increased the combined deficit of DB pension schemes to £770bn, compared to the already sizeable £253bn under the current UK regime.

EIOPA acknowledged that the introduction of a solvency-based regime would have caused unnecessary confusion without delivering any benefit to scheme members. It now proposes a new reporting regime for pension funds, to run alongside existing regulation.

A separate European development is the progression of the new IORP Directive. The text of this is being finalised in negotiations between the Council of the EU, the European Parliament and the European Commission The text of the final Directive is expected to be available in the autumn.

Both of the above developments, as well as other work progressed by EIOPA or the European Commission in the future, may now be less relevant for UK pension schemes, depending on the timing and terms of the UK's withdrawal from the EU.

Background information

Reduction to the Lifetime Allowance

With effect from 6 April 2016, the Lifetime Allowance reduced from £1.25 million to £1 million. It will then increase in line with inflation from 2018 onwards.

The Lifetime Allowance is the total amount of pension savings that an individual can build up within registered pension schemes during their lifetime, and if it is exceeded tax is charged on any savings over the limit.

There are two protection regimes relating to the 2016 reduction which will mirror previous protections:

1. Fixed Protection 2016 will allow an individual to retain a Lifetime Allowance of £1.25 million, although the individual must not accrue any benefits after 5 April 2016 to have this; and
2. Individual Protection 2016 can provide an individual with a bespoke level of Lifetime Allowance in excess of the situation where that individual has pension savings of at least £1 million on 5 April 2016.

Applications for Fixed Protection 2016 and/or Individual Protection 2016 can be made online from July 2016 and there will be no deadline for applications to register. However, members of pension schemes who wish to use Fixed Protection will need to have opted out of active or contributory membership so that accrual of benefits and/or payment of contributions ceased before 6 April 2016.

An interim process will allow members who want to take their benefits between 6 April 2016 and July 2016 to make a temporary application for protection.

...continued

Reduction to the Annual Allowance

The 2015 Summer Budget announced changes to the Annual Allowance for higher earners.

From 2016/17, those with ‘adjusted income’ over £150,000 now have their Annual Allowance reduced by £1 for every £2 of adjusted income over £150,000. The maximum reduction is £30,000. This is referred to as the tapered Annual Allowance.

As a consequence of the taper, individuals with adjusted income of £210,000 or over will have an Annual Allowance of £10,000.

For this purpose, ‘adjusted income’ is typically based on:

1. An individual’s taxable income; plus
2. The level of that individual’s pension savings, as measured by the pension input amount under Annual Allowance rules.

Typically, those with taxable income below £110,000 will not be subject to the new taper.

The fact that many members of pension schemes will have elements of non-pensionable pay or income from non-employment sources (e.g. income from personal assets such as property) means that there will be some members with pensionable pay considerably lower than £150,000 who are impacted by the tapered Annual Allowance.

Consequently, it is difficult for either employers or trustees to quantify how many members of their schemes may be impacted by the tapered Annual Allowance. Furthermore, for those members who are impacted by the tapered Annual Allowance, it is also difficult to quantify what reduced level of Annual Allowance will apply.

The government had published draft legislation for consultation relating to the provision of pension savings statements to those who may exceed the Annual Allowance under the tapered Annual Allowance regime for 2015/16. This suggested that pension savings statements would be required for all those with ‘pensionable earnings’ of £110,000 or more, although it was unclear how ‘pensionable earnings’ was defined for this purpose. RPMI provided a response to the government on this consultation. Following this consultation, changes were made to the legislation so that a pensions savings statement will only need to be provided if the full Annual Allowance is exceeded.

It is not yet clear whether further legislative changes may be made to cover the provision of pension savings statements from 2016/17 onwards.

A further development relating to the Annual Allowance is that HMRC has clarified that an individual will only have a right to use the scheme pays facility if their Annual Allowance charge for the tax year exceeds £2,000 and the individual’s level of pension savings exceeds the full Annual Allowance of £40,000.

However, it is expected that the scheme pays facility could be operated on a voluntary basis to cover those cases when a member has an Annual Allowance tax charge as a consequence of exceeding the tapered Annual Allowance rather than the full Annual Allowance.

The Pensions Regulator ‘how to’ guides
Following a Pension Regulator consultation on the draft of it, an updated DC Code of Practice was laid before Parliament. The new code is expected to come into force in July 2016.

The response from The Pension Regulator (TPR) to coincide with this indicated that most other respondents were generally supportive of the updates to the code. TPR also highlighted a few changes made following the consultation:

- Some modifications to investment of contributions to allow for schemes which do not have daily dealing cycles;
- Some updates to the code for legislative changes since November 2015; and
- The code is now called “Governance and administration of occupational trust-based schemes providing money purchase benefits” to better reflect the arrangements it applies to.

TPR has also launched a consultation about a series of 'how to' guides which are intended to help trustees implement TPR’s revised defined contribution (DC) code.

The guides have been designed to support the new shorter code and explain to trustees how they can demonstrate compliance with the law. It is expected that the new guides will also come into force in July 2016.