BROADSTONE

SPRING INDEX

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BUDGET UPDATE

Phillip Hammond delivered a Spring Budget with very little direct impact on pensions. The biggest change was to the QROPS rules and we will be working with HMRC to ensure our processes are up to date to ensure any overseas transfers are taxed accordingly.

Transfers to Qualifying Recognised Overseas Pension Schemes (QROPS)

For the past few years the government has been making noises about overseas pension transfers and reviewing what it is to be a QROPS. So today they announced that effective from 9 March 2017 there will be a 25% charge on transfers to QROPS ("the overseas transfer charge"). If the Lifetime allowance is exceeded by the transfer the lifetime allowance excess charge of 25% would also be payable.

The new overseas transfer charge of 25% will apply unless one of the following apply:

- The individual and the QROPS are in the same country after the transfer
- The QROPS is in an EEA state and the individual is in another EEA state after the transfer
- The QROPS is an occupational scheme sponsored by the individual's employer
- The QROPS is a public sector scheme
- The QROPS is established by an international organisation

If there are various changes within 5 years then the charge can arise.

It is expected to impact on a small number of transfers but may be an effective method to prevent the use of QROPS as a vehicle for pension scams.

The Government expects to raise £65m in the first year of this charge.

Self-employed NICs

The budget's major announcement related to National Insurance Contributions paid by self-employed workers. It was announced that the main rate of Class 4 National Insurance contributions will increase from 9% to 10% in April 2018 and to 11% in April 2019 to reduce the gap in rates paid by the self-employed and employees, and to reflect the introduction of the single tier state pension.

With the self-employed the subject of the upcoming review on auto-enrolment it could be that the full rise could be avoided if pension contributions are made.

Dividend allowance cut

Mr Hammond reduced the tax-free dividend allowance from £5,000 to £2,000 from April 2018. The dividend allowance allowed each director/shareholder to take £5,000 of dividends out of their company tax free over and above their personal allowance. This does not apply to ISA and pensions and so the use of these as efficient methods for investing may increase.

Lifetime ISA

The government also mentioned in the reams of back-up papers the launch of the Lifetime ISA next month. The FCA have this week finalised their rules on the risk warnings that providers would need to share, including a warning that if you have opted out of your workplace pension to take up a LISA you may miss out on the employer contributions. The absence of a risk warning had been a fear of many in the pensions industry.

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Pension Freedoms

The Treasury originally estimated pension freedoms would raise around £0.3 billion in 2015-16 and £0.6 billion in 2016-17 as people cashed in their pension pots. However, the ability to take lump sums without buying an annuity has resulted in the measure raising far more than anticipated with £1.5 billion in 2015-16, with their latest estimate for 2016-17 at £1.1 billion.

Money Purchase Annual Allowance (MPAA)

The back-up papers also confirmed the change in the MPAA from £10,000 to £4,000 effective from 6 April 2017. The MPAA which is aimed at reducing the ability of people over the age of 55 from taking pension income and then recycling it for more tax relief will go ahead, with the cost of its revenue impact also included in the budget papers.

Green Paper on options for future funding of social care to be launched later this year

In the run up to the Budget there was speculation that the government would announce measures to allow people to access their pension to make a tax-free contribution to the cost of long term health care. This measure was not included but a further consultation on the challenge of long-term care was announced and this may yet form part of that consultation.

JUDICIAL PENSION SCHEME

The Government wanted to change the way that the judicial pension scheme worked in the future. To make the change, younger judges would transfer to a new, less generous, pension scheme whereas those closer to retirement could continue in the original scheme.

This was appealed at an employment tribunal that ruled the steps were discriminatory on age. The Government reasoned that younger members would have more time to make up for the lost pension, or at least be able to prepare for the "necessary lifestyle and financial adjustments". This was deemed not an objective and/or reasonably justifiable aim. The changes also disproportionately affected female and ethnic minority judges and was found to discriminate on sex and race grounds.

The steps taken to change the judicial pension scheme are not exceptional and have been used in the past for public and possibly some private sector pension schemes and so these may yet be challenged by further court cases.

PENSIONS ADVICE ALLOWANCE

Individuals will soon be able to withdraw up to £500 from their DC pension pots towards advice received concerning pensions and retirement. The Government is now consulting on the final details with some surprising developments:

- Individuals will be allowed three withdrawals of £500, so £1,500 in total
- However, they are only entitled to £500 per tax year
- Can be used against the cost of regulated financial advice
- Can be used together with the £500 employer arranged advice exemption from tax and NI
- Withdrawal can only be made against DC benefits
- Available from 6 April 2017
- Providers do not have to offer the facility nor report it when used
- Individuals will self-declare usage

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DWP DEFINED BENEFIT GREEN PAPER

The Government have published a lengthy Green Paper (as promised) looking in detail at the DB pensions system amid calls that there is an affordability crisis.

The Government rejects this claim based on a number of different ratios, primarily the level of dividends paid compared to deficit recovery contributions.

The paper looks at the DB system across four sections, summarised below:

Funding and Investment

- The paper addresses the issue of discount rates used when valuing liabilities and whether these are too pessimistic, the Government concludes that this is not the case.
- Funding flexibilities – the Government did not see a strong case for reviewing or amending the current flexibilities in the system.
- The paper discusses whether the 3 year valuation cycle is still appropriate and, while it plays with the idea of various exemptions, no changes are proposed.
- The investments area is a little less clear, with the government interested in how trustees can make better investment decisions.
- Further research will be undertaken.
- The paper does discuss whether trustees are being too risk averse (whilst at the same time recognising that trustees may not be sufficiently skilled in the investment marker) and this may yet develop into new guidance from the pensions regulator.

Employer contributions and affordability

Given the Government does not think there is a systemic issue, the focus has turned to look at how struggling employers can be helped.

- The paper mulls over various options to help employers, including allowing employers to leave the scheme, change benefits, and regulatory powers to assist in winding-up schemes. However, the "moral hazard" issues are seen as too great at the moment, although views on this are sought.
- Conditional indexation gets a run out and remains on the table for stressed employer/schemes.
- The paper also touches on the CPI/RPI debate with a statutory override not ruled out, even though it would create some knock-on issues with gilt issuance.
- The paper also discusses how stressed schemes could be managed, including interim funding targets, enforced separation, more flexibility in regulations, the potential for schemes to run without employers, and relaxing tax rules on trivial commutation.

Member Protection

- The Government discusses the powers of the regulator and whether these can be extended, bearing in mind the regulator's limited resources
- They want to know whether the regulator should be given greater powers to comment on the risk-taking and whether funding levels are appropriate and prudent. There will be a further consultation asking whether this should be established with legislation setting out the requirements or give the regulator the power to set binding standards and schemes to "comply or explain"
- The paper discusses strengthening the position of trustees in terms of the information provided to them, particularly where schemes are severely underfunded, to provide additional safeguards
- Mandatory pre-clearance for corporate exercises was rejected, although a system for certain incidents to require pre-clearance was discussed and further evidence will be gathered in this area

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Consolidation of schemes

- Small schemes are a concern, due to the higher administration costs and inability to access economies of scale
- Consolidation is discussed at length and the conclusion appears to be a de-regulation to make voluntary consolidation easier
- The government rejects the idea of compulsory consolidation and also a government run super-fund as disproportionate.
- Partial wind-up of schemes to allow the payment of WULS only is also under consideration

The paper does also discuss member communications and the idea of a DB Chair's statement (akin to the DC Chair's statement) edges closer. A revamp of member communications is also on the cards primarily on the way details of the funding and status of the DB pension promise are communicated.

NEW LEVY FOR 'ZOMBIE' SCHEMES

The PPF is proposing a new levy for schemes that have become separated from the sponsor. The current methodology of which employer failure is an element is not appropriate and the scheme is directly exposed to the failure of the scheme's investment strategy.

The proposals include an acknowledgement that other levy payers will probably pick up some of the slack here, but there is concern that, if this becomes more common, a wider review of the levy system would be required. That said, the PPF believe a scheme with no sponsor will pose a bigger risk to a scheme with an employer.

This hints at further developments in employers being allowed to break links with their schemes.

BHS CONCLUSION

The Pensions Regulator, Sir Philip Green and the Trustees of the BHS Pension Scheme have reached an agreement for the future of the scheme and the members. This new plan has the backing of The Pensions Regulator and will mean a new scheme is created to continue without a sponsoring employer but will remain eligible to enter the PPF in the future if funding levels become too low.

The key points from the agreement are below:

- Sir Philip Green will make a payment of £343m to the pension scheme with £20m also available for expenses and costs in implementing the member options.
- The BHS scheme has, since March 2016, been in PPF assessment with benefits in payment reduced to PPF levels
- Members will be written to offering 3 options:
  - Transfer benefits to the new scheme (BHS2) that will no longer be linked to BHS and will pay out higher benefits than would be payable by the PPF.
  - If members' benefits satisfy the requirement for a winding up lump sum they will have the option of receiving a lump sum in lieu of any further benefits.
  - Remain in the scheme and transfer to the PPF
- It is estimated that the benefits in the new scheme will be around 88% of the original benefit value, but still higher than would have been paid by the PPF.

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GENERAL DATA PROTECTION REGULATION

This EU regulation will become law on 25 May 2018 and replaces the Data Protection Act.

Key points:

- Increase in penalties up to €20 million (from £500,000) or 4% of global turnover if corporate.
- Data processor (service providers such as administration and payroll processors) will have direct liability for data protection breaches
- Data breaches will have to be reported to Information Commissioner's Office (ICO) within 72 hours (currently no obligation to advise)
- Schemes should have a breach response plan
- New contracts that will still be in force post May 2018 should reference the new GDPR
- Member's should be communicated with to confirm what data is held and why
- This will have a significant impact on Trustees and employers and something Trustees should begin to plan for

GMP EQUALISATION

The Government has issued a consultation document on how schemes should equalise their GMP. This has been a long running issue and there is still a difference of opinion between a consensus of pensions lawyers (who believe GMP is exempt from equalisation) and the Government which takes the contrary view.

The Government issued a methodology in 2012, which was withdrawn in a wave of criticism from the pensions industry.

The new method is designed to be a one-off exercise and will also include the ability to convert the equalised GMP into non-GMP benefits ensuring it does not need to be reviewed again.

We shall monitor the consultation and advise the outcome in due course.

21ST CENTURY TRUSTEE

The Pensions Regulator has issued a discussion paper on what it is to be a trustee of a DB or DC scheme in the 21st Century.

The discussion papers ask some questions of the pensions industry as well as exploring ways of changing the communication methods used by the Regulator.

Some question areas:

- Exploring the role of the trustee Chair
- Awareness of trustee Knowledge and Understanding Framework
- Whether professional trustees should be required to be qualified or registered by a professional body,

The Regulator goes on to make a number of observations across a wide range of topics:

- Effective trusteeship and governance are key underpinning factors in achieving good member outcomes – it is essential that those responsible for running pension schemes and entrusted with members' savings are the right people with appropriate knowledge and skills and have the right scheme management processes in place.
- Trustee boards should reflect a diverse and balanced range of skills and experiences; this would include a balance of professional and lay trustees.
- The rise of professional trustees correlated with the rise in governance requirements is an area of focus from the Regulator.

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- A more formal role for the Chair of a DC scheme's board of trustees has developed and the Regulator mulls over expanding the DB Chair's position. Standards may also be improved by the Regulator imposing a minimum level of experience, qualification or requirement that the Chair is a member of a professional body.
- There are concerns around the awareness of the trustee Knowledge and Understanding programme.

The Regulator is considering making it mandatory for Trustees to pass all relevant modules within 6 months of appointment or six-month probationary period for prospective trustees to complete the modules before the appointment is formalised.

- The Pensions Regulator does not expect all trustees to be professional but expects them to act professionally
- Conflicts of Interest remains a major issue, with a large number of trustees "volunteered" by the employer and half of Chairs selected by the employer. The area of conflicts of interest is up for review
- Online tools will be reviewed to help trustees get what they need from their advisers. Small and medium schemes will also be assisted in getting more involved with administration, record keeping and investment governance
- What do Trustees have in store?
- More help to trustees to identify training needs
- Help in setting investment strategies and identifying risks
- Tools to help Chairs get more out of their advisers
- The Regulator also makes a rather ambitious suggestion that sub-standard schemes (DB and DC) could be consolidated

AUTO-ENROLMENT - WHO IS MISSING OUT

The auto-enrolment review that is getting started will be tasked with looking into how people who are currently excluded from the programme can be included. There are some startling statistics showing that:

- According to the Pensions Policy Institute (PPI), half of working age people are not eligible for automatic enrolment - 5.3 million of whom are employed, but do not meet the criteria - plus 4.6 million self-employed workers
- There is also no doubt from the results so far that certain groups miss out more than others. The PPI research also found that a high proportion of ineligible workers are women and part-timers, including many with several jobs
- Individuals under the age of 22 and those over the State Pension Age (SPA) are also excluded from automatic enrolment, and there have been calls for this to be revisited, particularly the lower age limit. Young people will be allowed to save via the Lifetime ISA from age 18, which may increase opt-out rates when they reach age 22. It may therefore make sense to bring these limits in line, so that younger workers can benefit from employer contributions from an earlier date

This is clearly a massive challenge for the government to tackle if it is to make auto-enrolment a success.

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KEY DATES FOR YOUR DIARY IN 2017

31 March: Pensions Dashboard

The Government tasked the pensions industry with launching a prototype Pensions Dashboard by March 2017. This would be a solution to stop people losing track of their pension pots by having them all visible in one place. It will also enable people to see what they've got when planning for their retirement.

1 April: Auto-enrolment staging date

If an employer does not pay their employees through PAYE they must begin auto-enrolment by 1 April. This date is important for employees paid through service contracts or where the employer does not deduct tax.

5 April: Revaluation of GMP

With the end of contracting out on 5 April 2016 schemes with GMPs which revalue on a fixed rate basis would have to change their rules to ensure that the fixed rate would apply from the date the member left the scheme rather than the date the scheme ceased to contract out. The Government allowed trustees to pass a resolution to ensure that the previous practice could continue. The deadline for the resolution is 5 April 2017.

6 April: PPF compensation cap

The PPF compensation cap will be amended to reflect long service so that anyone with more than 20 years' service will be entitled to an increase on the compensation they receive.

6 April: Money Purchase Annual Allowance (MPAA)

We may have more changes coming from the Spring Budget (see above) but we already know that from this date anyone who has (or does) access their Defined Contribution benefits in a flexible manner will become subject to the Money Purchase Annual Allowance. This will now be £4,000 (as opposed to £10,000). This has the potential to catch many people currently in their employer's pension scheme and who accessed some DC pensions after age 55.

October: Early exit charge cap

The Government, in a bid to ease access to the pension flexibilities, will impose a cap on early exit fees from 1 October. This cap will be set a 1% for existing schemes with no early exit fees permitted on new schemes.

31 December: VAT transitional period ends

VAT on pension scheme costs is an issue that has been around for a number of years and has resided in HMRC's "too difficult" box. The current method for reclaiming VAT will cease at the end of the year. However, we fully expect the government to kick the can again.

Government consultations and initiatives

State pension age

The Cridland Review is ongoing and the Government Actuary's Department are also currently preparing reports on State Pension Age. The Government will have to report on how State Pension age will increase after 2028 during 2017.

Pension scams

Legislation is expected in the year to toughen up the rules on statutory transfers to enable trustees to stop transfers that may not be to a bona fide pension scheme.

Salary sacrifice

Restrictions on the benefits that are able to be paid via salary sacrifice will take effect from 6 April 2017. Note that pension contributions remain eligible for salary sacrifice.

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Auto-enrolment

The government are also conducting a review into the success of auto-enrolment and how it could be improved to encourage access for self-employed and cope with those with multiple low-paid jobs.

Employer funded advice

The government will pass legislation to enable employers to contribute £500 tax and NI free for pensions guidance received by employees.

PPF Deadlines

Midnight on 31 March 2017 for the compulsory submission of scheme returns (including voluntary section 179 valuations), and certification/re-certification of asset-backed contributions, mortgages (to Experian), contingent assets and the new accounting standard change.

5pm on 28 April 2017 for certification of deficit reduction contributions; and

5pm on 30 June 2017 for certification of full block transfers that have taken place before 1 April 2017.

Broadstone Trustee Toolkit dates for 2017

25 April - London

10 May - Sheffield

13 July - London

12 September - Sheffield

2 November - London

CONTACT US

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