DLA PIPER

PENSIONS NEWS

OCTOBER 2014

IN THIS ISSUE

INTRODUCTION

Welcome to DLA Piper's Pensions News publication in which we report on recent developments in pensions legislation, guidance and case law, as well as keeping you up to speed on what to look out for in the coming months.

This edition brings you the developments from October 2014 including the following.

- **Budget reforms:** the introduction to Parliament of the Taxation of Pensions Bill; an announcement about the providers of the guidance guarantee; and the draft legislation providing the framework for the guidance guarantee.
- **The Pensions Regulator:** the Regulator's latest report on compliance activity in relation to automatic enrolment; upcoming publications in relation to DB funding and DC reforms; and the Purple Book 2014.
- **Pension Protection Fund:** the consultation on the levy for 2015/16.
- **Department for Work and Pensions:** a consultation on draft regulations on DC governance standards and charges for occupational pension schemes; a consultation on the automatic enrolment thresholds for 2015/16; and an announcement about the timing of the abolition of short service refunds for DC benefits.
- **Legislation:** the progress of the Pension Schemes Bill through Parliament.
- **HMRC:** the latest bulletin about the end of contracting-out which focuses in particular on the Scheme Reconciliation Service.
- **Public service pension schemes:** developments in relation to implementing the public service reforms for the Local Government Pension Scheme, the Teachers' Pension Scheme and the NHS Pension Scheme.
- **Other News:** updates from the Pensions Ombudsman on pension liberation and its new website; and a consultation issued by EIOPA about scheme solvency.

If you would like to know more about any of the items featured in this edition of Pensions News or how they might affect you, please get in touch with your usual DLA Piper pensions contact or contact Cathryn Everest. Contact details can be found at the end of this newsletter.

BUDGET REFORMS

TAXATION OF PENSIONS BILL

Following the August technical consultation on draft clauses for the Taxation of Pensions Bill, the updated version of the Bill was laid before Parliament on 14 October and on 21 October HMRC published an updated version of its accompanying draft guidance.

In this article we report on some of the notable changes made to the Bill since it was published for technical consultation on 6 August. However, it is important to note that the Bill remains subject to change as it continues through Parliament. The Bill received its Second Reading in the House of Commons on 29 October with this debate focusing on the overall principles of the Bill rather than the drafting of specific clauses. The next stage for the Bill is the Public Bill Committee at which the provisions will be debated in greater detail. As at the end of October it was expected that the Public Bill Committee stage would start on 11 November and end on 20 November. This means that the Bill and any amendments to it may move quickly.

Special lump sum death benefits charge

In September the Chancellor announced changes to the special lump sum death benefits charge so that, broadly speaking, from April 2015 the position for DC savings in respect of funds which were uncrystallised or in a drawdown account when the member died will be as follows.

- If the member was under 75 at the date of death, the remaining DC pension can be passed to any beneficiary tax free as a lump sum or through a flexi-access drawdown account.
- If the member was 75 or over at the date of death, beneficiaries will be able to draw down on the pension at their marginal rate of income tax or receive a lump sum payment taxed at 45%. The intention is that this 45% tax rate for lump sums will be changed to the recipient's marginal tax rate from 2016/17.

At the time of this announcement, no legislation was published but the Bill as laid before Parliament contains the amendments in relation to lump sums. These amendments go further than the September announcement suggested because, in addition to the expected changes to uncrystallised funds lump sum death benefits and drawdown pension fund lump sum death benefits, under the Bill the following lump sums will not be subject to tax under the Finance Act where the member died before reaching age 75 and will be taxed at a rate of 45% (rather than 55%) where the member died at age 75 or over.

- Annuity protection lump sum death benefits – this type of lump sum can be paid where a member was being paid a scheme pension or a lifetime annuity in respect of a money purchase arrangement and had chosen to guarantee that a set amount would be provided, but this amount had not been paid when the member died. The lump sum is essentially the balance of the guaranteed amount. Currently a 55% tax charge would apply irrespective of the member's age when they died.
- Pension protection lump sum death benefits – this type of lump sum is similar to an annuity protection lump sum death benefit, but is paid where the member was being paid a scheme pension from a defined benefits arrangement. Currently a 55% tax charge would apply irrespective of the member's age when they died.
- Defined benefits lump sum death benefits – this is a lump sum paid from a defined benefit arrangement following the death of a member, such as where a multiple of the member's salary becomes payable on their death. Currently a 55% tax charge would apply if the member was age 75 or over when they died.
- Flexi-access drawdown fund lump sum death benefits. This will be a new type of lump sum introduced by the Bill which is paid in respect of the new flexi-access drawdown funds.

The Bill states that these amendments will apply to lump sums paid on or after 6 April 2015.

The Government will bring forward further changes in due course to cover the other elements of the announcement made in September.

Serious ill health lump sums

As well as the changes to lump sum death benefits, the Bill contains an amendment to reduce the tax charge from 55% to 45% where a member aged 75 or over is paid a serious ill health lump sum.

Drawdown pensions

The key provisions that were consulted on remain in the Bill as laid before Parliament, so that a new type of drawdown fund – the flexi-access drawdown fund – is introduced, which will not be subject to any limits in relation to withdrawals. Existing flexible drawdown funds will be automatically converted to flexi-access drawdown funds on 6 April 2015, and members can retain existing capped drawdown funds or choose to convert them to flexi-access drawdown funds (or the conversion will be automatic if a payment is made which would breach the cap).

The Bill as laid before Parliament includes a new paragraph so that where a member transfers their capped drawdown funds from one scheme to another as a recognised transfer, they can notify the scheme administrator of the receiving scheme that they wish the transferred drawdown funds to be held in a flexi-access drawdown fund. A corresponding amendment is made in relation to dependants' drawdown funds.

Some further consequential amendments have also been added to the Bill to amend various sets of regulations to add references to flexi-access drawdown. For example, the existing regulations about transfers of drawdown funds are extended to include transfers of member's and dependant's flexi-access drawdown funds.

Uncrystallised funds pension lump sums

The consultation version of the Bill made provision for a new type of lump sum – an uncrystallised funds pension lump sum – which will allow flexible payments to be made to members without them first designating funds to a flexi-access drawdown fund.

The criteria that a payment will have to meet to be classed as an uncrystallised funds pension lump sum have been amended in the Bill laid before Parliament. Most notably, additional criteria have been added so that a lump sum can only be an uncrystallised funds pension lump sum if:

- it is not a pension commencement lump sum;
- it is not a small pots lump sum payment;
- the sums or assets used to provide it do not to any extent represent rights attributable to a disqualifying pension credit. A disqualifying pension credit is essentially one that a person became entitled to at a time when the pension subject to the debit was in payment.

Relaxation of annuity requirements

The consultation version of the Bill proposed relaxations to the criteria that annuities must meet in order to be authorised payments including to remove the requirements that, save for in very limited circumstances, the annuity cannot decrease, and that an annuity cannot be an authorised payment if the member did not have an opportunity to select the insurance company.

Decreasing annuities

A new paragraph has been added to the Bill as laid before Parliament which relates to cases where following the cessation of an annuity the funds are transferred and used to purchase a new flexible annuity. A flexible annuity is essentially one to which the person becomes entitled on or after 6 April 2015, and which allows for, or could allow for, payments to decrease other than in prescribed circumstances. The new paragraph in the Bill is a power for regulations to specify circumstances in which this new flexible annuity will *not* be a lifetime annuity (and therefore will not be an authorised payment). The Explanatory Notes do not give any indication as to how it is intended this new power will be used.

The Open Market Option

As in the consultation draft, the Bill as laid before Parliament removes the requirement that for a lifetime annuity to be an authorised payment, the member must have had an opportunity to select the insurance company. However, the draft HMRC guidance has been updated to clarify that this does not mean the end of the Open Market Option but rather that it ensures that the member will not be subject to tax charges where they are not given the opportunity to select the insurance company paying the annuity. This point was also confirmed during the Second Reading of the Bill in which it was stated that:

- the Open Market Option will continue to be highlighted in the information that schemes are required to provide to their members at retirement; and
- the amendment simply removes the requirement from the tax rules as it is not appropriate for the member to be charged tax because they have been deprived of the opportunity to select an annuity provider.

Statutory override

The consultation version of the Bill contained a statutory override permitting trustees to make the following payments even if their rules prohibit them (however this is framed) from doing so:

- drawdown pension or dependants' drawdown pension;
- payments paid to purchase a short-term annuity or a dependants' short-term annuity; or
- an uncrystallised funds pension lump sum.

Three further types of payment have been added to the statutory override in the Bill as laid before Parliament:

- flexi-access drawdown fund lump sum death benefits;
- a pension commencement lump sum where the person becomes entitled to it in connection with becoming entitled to income withdrawal; and
- a trivial commutation lump sum death benefit paid in respect of an entitlement to receive guaranteed payments payable after the member's death.

Money purchase annual allowance

The consultation version of the Bill contained provisions to introduce a safeguard against abuse of the new rules, in the form of a reduced annual allowance of £10,000 for money purchase pension savings that will apply in certain circumstances.

Essentially, the trigger for the money purchase annual allowance rules is a member accessing their DC savings flexibly on or after 6 April 2015. The Bill as laid before Parliament adds two additional circumstances in which the member will be regarded as having flexibly accessed their benefits, thereby triggering the money purchase annual allowance rules. In summary, these circumstances are:

- the member receives a payment of a lifetime annuity under a flexible annuity contract (that is, one set up on or after 6 April 2015 and the terms of the contract allow the payments to go down, or they can be varied to allow payments to go down, other than in prescribed circumstances); and
- where a member receives a payment of a scheme pension from a money purchase arrangement where there are fewer than 12 individuals including the member receiving such scheme pensions.

Trivial commutation lump sums

The consultation version of the Bill proposed amendments so that it will only be possible to pay trivial commutation lump sums in respect of defined benefit arrangements (because uncrystallised funds pension lump sums can instead be used for money purchase arrangements) and to reduce the minimum age for payment of a trivial commutation lump sum from 60 to normal minimum pension age. These changes are retained in the Bill as laid before Parliament but in addition:

- it is clarified that the lump sum will only need to extinguish all of the member's entitlement to defined benefits under the scheme; and
- it is stated that such a lump sum could be paid to a member below normal minimum pension age if the ill health condition is met.

The change in minimum age so that it can be lower than normal minimum pension age if the ill health condition is met is also proposed to be made to the regulations governing the payment of small pension pots not exceeding £10,000 on a scheme specific basis.

Trivial commutation lump sum death benefits

The consultation version of the Bill proposed amendments: (i) to increase the limit of the value of benefits that can be commuted from £18,000 to £30,000; and (ii) so that a trivial commutation lump sum death benefit can be paid in respect of entitlements to guaranteed pension payments. It was proposed that these amendments would apply where the member dies after the date the Bill receives Royal Assent.

The version of the Bill as laid before Parliament clarifies that where the lump sum is paid in respect of guaranteed payments of an annuity or scheme pension payable by an insurance company, it will only need to extinguish all entitlements under that contract in respect of the member. The timing of these changes is also amended so that they will apply in relation to lump sums paid on or after 6 April 2015.

Provision of information

The Bill as laid before Parliament contains a new Part in relation to the provision of information. The intention of these provisions is to ensure that the member is aware that they have flexibly accessed their pension rights and the consequences of having done so, and that the scheme administrator for every scheme of which they are a member is also aware. For example, the information requirements include the following.

- A requirement for the scheme administrator to provide specified information to the member when the member first flexibly accesses their benefits.
- A requirement on the member to give notice of this to the scheme administrators of any other registered pension scheme of which they are a member or become a member.
- Where there is a recognised transfer, a requirement on scheme administrators who have reason to believe that the member has flexibly accessed their benefits to provide specified information to the scheme administrator of the receiving scheme.

In terms of timing, this information has to be provided before the end of 31 days beginning with the relevant event.

Amendments are also made to the requirements for the provision of "pension savings statements" to extend the circumstances in which scheme administrators are required to issue a statement to include where they believe the member has flexibly accessed their pension rights and they have money purchase or relevant hybrid arrangement pension input amounts of more than £10,000 in that scheme. The Bill also specifies the information to be provided in a statement issued in these circumstances. The requirements to inform HMRC when a statement has been issued are also amended to reflect this change.

As well as providing an overview of the provisions in the Bill described above, the updated draft HMRC guidance also notes some other upcoming changes in relation to other aspects of the provision of information. This includes that further changes will shortly be made to Real Time Information reporting through secondary legislation. The draft guidance explains the effect the changes are expected to have although it notes that this is subject to change. Within this part of the guidance it is noted that:

- where pension providers make a payment from a flexi-access drawdown fund or from an uncrystallised funds pension lump sum, tax should be deducted using the emergency code unless they have or receive a P45 or tax code in respect of the member; and
- to enable HMRC to know which individuals have received flexibly-accessed pension savings, pension providers will need to provide HMRC with some additional information under Real Time Information about certain payments to individuals.

Overseas pensions

The Bill as laid before Parliament also contains a new Part which makes a number of amendments in connection with overseas pensions.

By way of background, the draft HMRC guidance in relation to these changes explains that existing legislation provides for UK pension tax rules to apply to certain pension schemes set up outside the UK, and that these schemes fall into two broad categories – QROPS (which can receive transfers from registered pension schemes as authorised payments), and currently relieved non-UK pension schemes (where tax relief has been given on or after 6 April 2006 in respect of pension savings under the scheme). The draft guidance states that, collectively, these schemes are known as relevant non-UK schemes (RNUKS).

It goes on to state that to maintain the comparability between registered pension schemes and RNUKS, new clauses in the Bill change the legislation that covers pension savings in overseas schemes, for example, to ensure that a payment from an overseas scheme that would be an uncrystallised funds pension lump sum if paid from a registered pension scheme can be taxed as pension income and to ensure that flexibly accessing pension rights under an RNUKS will trigger the money purchase annual allowance rules.

The draft HMRC guidance also notes areas in relation to overseas schemes where further detail is to come.

- The new provisions in the Bill include powers to require scheme managers of overseas pension schemes, scheme administrators of registered pension schemes and individual members to provide information in prescribed circumstances. The draft guidance explains that the detailed reporting requirements for overseas pension schemes are still under consideration.
- The Bill makes provision to delay the start of the re-notification process for QROPS until 6 April 2016. The draft guidance explains that: (i) the conditions a scheme has to satisfy if it is to be a QROPS are under consideration in light of the increased flexibility available to registered pension schemes and any changes are likely to take effect from 6 April 2015; and (ii) the start of the re-notification process is being delayed until 6 April 2016 which will allow Recognised Overseas Pension Schemes to be clear on what information they need to provide to HMRC and how a scheme may meet the conditions to be a Recognised Overseas Pension Scheme from 6 April 2015.

The fundamental principles of the Bill remain unchanged since the version that was published for consultation. That is, members of a money purchase arrangement will from 6 April 2015 be able to access their benefits flexibly through a flexi-access drawdown fund or uncrystallised funds pension lump sums, and the option of a lifetime annuity will now also have more flexibility, and where members access their benefits flexibly a new money purchase annual allowance will apply. However, some of the detail has been amended and added to, and some further detail and amendments are awaited.

Whilst schemes can start to consider whether, in principle, they wish to offer the new flexibilities, the detail is crucial and therefore it is to be hoped that the final version of this legislation will be in place as soon as possible, as well as the aspects of the reforms that will be in the Pension Scheme Bill.

GUIDANCE GUARANTEE

Announcement about providers

On 18 October, HM Treasury announced the providers of the pension guidance service stating that Citizens Advice Bureau will provide expert face to face guidance, and the Pensions Advisory Service (TPAS) will provide telephone guidance. In addition the Treasury reported that an online service will be designed by the Government as part of the guidance scheme.

Legislative framework

In late October, the Government tabled amendments to the Pension Schemes Bill to add a new Part 20A to the Financial Services and Markets Act 2000 providing the framework for the guidance guarantee. Points in the proposed new legislation include the following.

- Pensions guidance is defined as "*guidance given for the purpose of helping a member of a pension scheme to make decisions about what to do with the cash balance benefits or other money purchase benefits that may be provided to the member*". Cash balance benefits and money purchase benefits for these purposes are as defined in the Finance Act 2004.
- A requirement is placed on the Treasury to take such steps as they consider appropriate to ensure that people have access to pensions guidance.
- TPAS and the Citizens Advice Bureau are named as the bodies to give pensions guidance in accordance with arrangements made with the Treasury, and power is given for the Treasury to designate other providers.
- Provision is made so that it is an offence for a person who is not giving pensions guidance under arrangements made with the Treasury to describe himself as a person who is doing so or to behave, or otherwise hold himself out, in a manner which indicates that he is doing so. It is a defence in proceedings for such an offence for the accused to show that they took all reasonable precautions and exercised all due diligence to avoid committing the offence.
- An obligation is imposed on the FCA to set standards for the giving of pensions guidance by designated providers.
- Provision is included so that the Treasury must notify the FCA of the amount of the Treasury's "pensions guidance costs", and having been so notified, the FCA must make rules requiring authorised persons, or any specified class of authorised person, to make payments to the FCA with a view to recovering the amount notified.

It is useful to know the identity of the providers of the guidance guarantee, but the draft amendments to the legislation (which are subject to the approval of Parliament in any event) provide a framework only and therefore the detail of the service is still to be confirmed. The key to the detail will be the FCA's response to its July consultation about the guidance service.

For trustees of occupational pension schemes, it will be useful to know what the guidance service will entail but the key issue will be understanding new requirements due to be introduced requiring them to signpost members to the guidance service. These requirements are expected to be included in amendments to existing disclosure requirements but, as at the end of October, had not yet been published.

THE PENSIONS REGULATOR

AUTOMATIC ENROLMENT – COMPLIANCE

On 28 October, the Regulator published its latest quarterly bulletin about automatic enrolment compliance and enforcement, which covers the period 1 July to 30 September 2014. The bulletin is designed to help employers, their advisers and the pensions industry as a whole understand the type of compliance and enforcement interventions that follow the Regulator's educative and enabling communications and support.

Enforcement activity

The accompanying press release states that the period covered by the report saw a significant rise in the number of employers needing to meet their duties as thousands of medium sized employers (those with approximately 150 to 250 workers) who staged in April 2014 reached their deadline to complete their declaration of compliance at the end of August. The press release also states that as the Regulator deals with smaller employers, it expects to see more who leave compliance too late or do not comply at all, and an increase in the number of times it needs to use its powers.

This already appears evident in statistics in this report which include that, in the period 1 July to 30 September 2014, the Regulator:

- issued eight information notices, whereby the Regulator can demand documents or any other information relevant to the exercise of its functions, bringing the total up to 10;
- issued 163 compliance notices, bringing the total up to 177;
- issued three fixed penalty notices – the Regulator had not previously used this power which enables it to issue a penalty of £400 for failure to comply with an unpaid contributions notice or a compliance notice; and
- made three uses of its power to inspect premises, bringing the total up to six.

Other points in the bulletin

The bulletin also:

- has a section on preventing non-compliance which states that some employers have failed to comply with their duties as a result of not seeking information on certain issues such as affected workers, and duties during a postponement period;
- reports on lessons learned from the Regulator's casework such as understanding staging dates for employers with more than one PAYE scheme and understanding the requirement to declare compliance with the Regulator; and
- notes that research has shown that some small and micro employers do not know when they need to comply with the duties and therefore includes a section urging small businesses to act.

The dramatic increase in the number of compliance notices issued and the first uses of the power to impose fixed penalties are particularly notable and clearly demonstrate the Regulator's intention to take action in relation to non-compliance. It is therefore important for employers to ensure that they understand their duties and avoid the pitfalls noted in this bulletin.

UPCOMING PUBLICATIONS

The Regulator has published the transcript of a speech which its chairman delivered at the NAPF annual conference on 16 October setting out his strategic vision and priorities. The speech noted some upcoming publications from the Regulator including the following.

- In relation to DB funding, the Regulator has organised a number of workshops to support trustees and employers, helping them understand and apply the new code and listening to their thoughts, concerns and experiences. The workshop materials will be put on the Regulator's website in due course and the Regulator will also produce a webinar for those who were unable to attend the workshops.

- In relation to the Treasury confirmation that members will continue to be able to transfer from a DB to a DC scheme when the Budget reforms are introduced, it is noted that this has implications for DB schemes so the Regulator intends to consult on some changes to its transfer guidance for trustees sometime in the New Year.
- The Regulator will be providing guidance in the New Year to help trustees through upcoming DC changes. The accompanying press release states that a series of guides will be published once the details of proposed reforms are confirmed by the Government in areas such as minimum governance standards, charges and the Budget reforms. The speech states that, in the meantime, the Regulator will continue to regulate against its DC Code and will be updating it to reflect changes to legislation.

SECTION 89 REPORT – MG ROVER

Under section 89 of the Pensions Act 2004 the Regulator can publish a report on the consideration it has given to exercising its functions in a particular case and the results of that consideration. On 23 October, the Regulator published a report announcing an £8 million settlement in relation to the MG Rover Group Senior Pension Scheme.

Background

MG Rover Group Limited ("**MGRG**") was the principal employer of the Scheme. The main operations of the MG Rover group of companies were owned by MGRG. On 8 April 2005 MGRG, together with its principal trading subsidiaries, went into administration, and in March 2006 these entities entered into creditors' voluntary liquidation. The Scheme entered into a PPF assessment period following the insolvency of MGRG and the other participating employers.

In May 2005, the Secretary of State for Trade and Industry appointed inspectors under the Companies Act 1985 to undertake an investigation into the affairs of the MG Rover group. The inspectors published their final report in 2009 and the content of this report was relevant to the Regulator's investigation, in particular findings concerning the acquisition of a portfolio of vehicle finance agreements with former customers of MGRG (referred to in the Section 89 Report as the "**Loan Book**").

MGR Capital Limited ("**Capital**") was established in 2001 specifically for the purpose of acquiring the Loan Book. Capital eventually accumulated substantial net assets as a result of the acquisition. Capital was a joint venture company established by certain private individuals (connected to and involved in the business of MGRG) and a subsidiary of HBOS plc. In 2009 Capital entered into members' voluntary liquidation.

The regulatory action

In December 2012 the Regulator issued a warning notice in respect of the potential use of its powers to issue a Financial Support Direction (FSD) to Capital for the benefit of the Scheme. Amongst other factors, the Regulator considered that it would be reasonable to seek an FSD on the basis that the acquisition of the Loan Book could have been structured in such a way as to have been acquired by and be of benefit to MGRG instead of Capital.

The settlement

The section 89 report states that on 20 October 2014, a settlement agreement was reached between Capital and the Scheme trustee whereby the Scheme has received £8.085 million from Capital. In light of this agreement, the Regulator is no longer seeking to issue an FSD against Capital.

It is expected that, with the settlement payment, the Scheme will be able to wind up outside the PPF and there will therefore be no call on the PPF levy payers to fund any of the benefits of the Scheme.

It is interesting to see the approach that the Regulator takes to the use of its powers and to settlement. In the report the Regulator states that its approach to settlement in a particular case will depend on the circumstances and its assessment of how the interests of scheme members and the PPF will best be served in line with its statutory objectives, noting that in this case settlement has avoided more protracted regulatory and legal proceedings which would have resulted in further costs being incurred by all parties.

The Regulator also notes that this case highlights that it will take account of a wide ambit of circumstances when assessing whether it is reasonable to exercise its FSD power, with it having considered the loss of a potential business opportunity by a statutory employer to the benefit of a connected or associated person relevant to its assessment of reasonableness in this case.

PURPLE BOOK 2014

Introduction

The Purple Book is a joint annual publication by the Regulator and the PPF which focuses on the risks faced by DB schemes, predominantly in the private sector, with the main focus being the position at the end of March for the year in question. The Purple Book looks at scheme demographics, scheme funding, funding sensitivities, insolvency risk, asset allocation, risk developments, levy payments, schemes in assessment, PPF compensation and risk reduction.

The Purple Book 2014 was published on 30 October 2014 and is based on information from scheme returns for 6,057 DB schemes, covering 11.1 million memberships and representing 99.8% of PPF-eligible schemes and 99.1% of PPF-eligible universe liabilities. The PPF-eligible universe is estimated to be around 6,070 schemes which is a reduction from 6,225 in March 2013, reflecting schemes winding-up, scheme mergers, schemes entering PPF assessment, schemes transferring to the PPF and block transfers. Findings from the Purple Book 2014 include the following.

Scheme demographics

- The proportion of schemes open to new members and future accrual fell to 13%, from 14% in both 2013 and 2012.
- 53% of schemes are closed to new members compared to 54% for the Purple Book 2013.
- 32% of schemes are closed to future accrual compared to 30% for the Purple Book 2013.
- 2% of schemes were in winding up which is the same proportion as for Purple Book 2013.

Scheme funding and funding sensitivities

- Scheme funding on a section 179 basis improved between the end of March 2013 and the end of March 2014, with the funding ratio rising from 84% to 97%. However, since the end of March 2014, aggregate scheme funding has fallen from 97% to 89% in August 2014.
- The full buy out funding ratio increased from 61% for Purple Book 2013 to 67%.

Levy payments

- The dataset used in this chapter is based on 6,114 schemes which have been invoiced for £577 million in total which is somewhat smaller than the £630 million the PPF expected to collect. This was mainly because under the risk-based levy assessment process the original underfunding and insolvency turned out to be lower than had been assumed.

Risk reduction

- The total number of recognised contingent assets for the 2014/15 levy year was 780 which is somewhat lower than the previous year when it was around 830. This is said to reflect a fall in the number of Type A contingent assets (company guarantees). It is stated that firmer standards of validation introduced by the PPF have led to this decrease in the number of recognised Type A contingent assets.
- The number of Type B contingent assets (security over holdings of cash, real estate or securities) fell slightly.
- By 10 April 2014, approximately £25.6 billion of Deficit Reduction Contributions had been certified to reduce deficits for the 2014/15 levy year.
- In terms of risk transfer business of buy-outs, buy-ins and longevity hedges:
  - between the end of 2007 and the first quarter of 2014, this amounted to £71.8 billion (with just under half of these deals being longevity hedges); and
  - over the year to Q1 2014, the total value of transfer deals was £21.6 billion, of which 49% were longevity swaps, 31% were buy-ins and 20% were buy-outs.

The Purple Book contains a large amount of statistical information and analysis. Further detail on the findings in the areas set out above as well as findings in the areas of insolvency risk, asset allocation, risk developments, schemes in assessment and PPF compensation can be found in the full report which is available on the PPF's website.

PENSION PROTECTION FUND

LEVY 2015/16 – CONSULTATION

Introduction

On 29 May the PPF published a consultation on the second levy triennium of 2015/16 to 2017/18. The main area where change was proposed was in the measurement of insolvency risk with the move to Experian as the insolvency risk services provider, who have developed a PPF-specific measure of insolvency risk. This model consists of eight scorecards differentiated by size of employer, corporate structure and the filing of full or abbreviated accounts.

On 6 October the PPF published a document reporting on responses to the May consultation and the PPF's conclusions in relation to them, and also setting out the levy estimate for 2015/16 and a consultation on detailed rules for the 2015/16 levy.

A total of 122 responses were received to the consultation which is the highest level of response since the initial consultation on the levy in 2005. This number is said to reflect in large part the move to Experian, although it is also noted that there were a considerable number of comments on the proposals in relation to asset-backed contributions.

Response to consultation

Points of note from the response include the following.

The PPF specific model

The great majority of comment was supportive of the move to the PPF Specific model and the greater predictiveness it delivers. The PPF will be moving ahead with the new model, although it has considered some changes to the model in response to comments, and Experian has also taken advantage of the opportunity to make some improvements to the model. For example, the PPF has made a change to address the most significant risk of scorecard arbitrage, and Experian has made a change to how parent company data is captured which should increase the proportion of ultimate parent companies correctly identified.

Transitional protection

The May consultation noted that the new model is anticipated to lead to a large redistribution of the levy, with those who will experience an increase in the levy expected to see bigger changes than those experiencing decreases. The consultation therefore sought views on the question of whether transitional protection should be introduced. A clear majority of those responding were opposed to this, with reasons given including that the Experian score is a more accurate prediction of risk and therefore schemes seeing a large increase would have generally been paying less than their share of the levy and transitional protection would simply extend this. The PPF reports that, on balance, the benefit of introducing transitional protection is outweighed by the downsides and it will not therefore be introduced.

Asset-backed contributions (ABCs)

The PPF reports that responses to consultation did not support the proposal in the May consultation of limiting recognition to property based ABCs, and that it has listened carefully to stakeholders' views here and has decided to allow potential recognition for all ABCs.

However, the PPF remains concerned to ensure that ABCs are not given undue weight in the levy and its aim is therefore to ensure that the value recognised for levy purposes more closely reflects what the investment might be worth in the situation relevant to the PPF, that is, where the employers and guarantors have suffered an insolvency event. Trustees will therefore be required to obtain a valuation annually on this insolvency basis on which the PPF can rely and which complies with specified requirements. Essentially, in order to assess the value of an ABC for PPF levy purposes, the PPF will expect trustees to certify the lower of: (i) the insolvency value of the interest in the Special Purpose Vehicle (including taking account of the

stressed insolvency value of the underlying asset(s) using the PPF's standard asset stresses); and (ii) the fair value reported in the most recent scheme accounts. Coupon payments made after the most recent section 179 valuation up to the date of the latest accounts will also be credited if reported on the voluntary certificate.

Also in relation to ABCs, the accompanying draft guidance on ABCs has a section on requirements to obtain legal advice. For example: (i) advice will be needed to inform the valuer's assessment of the ABC investment; and (ii) trustees will need to certify their belief in certain matters, having regard to "appropriate legal advice", for example that the ABC arrangement is legally binding, valid and enforceable.

Contingent assets

As proposed in the May consultation, the PPF has concluded that it is appropriate to require schemes to certify contingent assets with a fixed sum – the "Realisable Recovery" – which they are confident the guarantor could pay if required.

A new form of wording will be adopted for the certification which will be: "*The trustees, having made reasonable enquiry into the financial position of each certified guarantor, are reasonably satisfied that each certified guarantor, as at the date of the certificate, could meet in full the Realisable Recovery certified, having taken account of the likely impact of the immediate insolvency of all of the employers (other than the certified guarantor, where that certified guarantor is also an employer)*".

Also in relation to contingent assets, the PPF will apply an adjustment to guarantor scores based on the change in gearing implied by the contingent liability were it to fall due, except where the guarantor is the ultimate parent and files consolidated accounts. The approach to adjusting guarantor scores has been modified to that proposed in the May consultation in order to address a potential double counting issue.

Last man standing schemes

The PPF will implement the approach it consulted on in May in relation to last man standing schemes including requiring schemes to confirm that they have taken legal advice to support the conclusion that they are last man standing schemes.

The October Consultation

The October consultation states that the Levy Estimate for 2015/16 is £635 million, which represents a 10% reduction on the 2014/15 Estimate. The PPF states that, based on expectations of how the funding position of schemes will improve over the second triennium, it expects that levy collections will fall in each of the succeeding two years, although it notes that the exact path of the levy is uncertain as it will move with changes in measured risk.

The PPF also states that how much it will actually collect for 2015/16 is significantly more uncertain than in a "normal" year in light of the move to Experian, noting that it is aware from the early years of using Dun & Bradstreet that once scores are used in levies, schemes and employers act to correct data and fill in gaps, and there will be a degree of behavioural change to reduce levies. Whilst the PPF will allow for this in setting the levy scaling factor, it notes that the impact is impossible to predict with certainty.

In relation to contingent assets, the consultation document notes that two responses to the May consultation included the suggestion that the class of Contingent Assets could be extended to cover surety bonds. The PPF states that it has concluded that it could well be feasible for it to accept surety bonds provided they follow its standard form Type C(ii) contingent asset document. On 24 October the PPF reported on some updates to the Levy consultation which included that the Type C(ii) Contingent Asset Agreement has been updated to allow for surety bond agreements in line with the proposals.

The consultation also sets out the proposed key dates that will impact on PPF levies for 2015/16. The proposed deadline for submission of information to be taken into account in the levy calculation is 5pm on Tuesday 31 March 2015 aside from a few exceptions (for example, certification of deficit reduction contributions).

The consultation closes on 13 November 2014. The PPF will publish its conclusions and the final Levy Rules before Christmas.

UPDATED VALUATION GUIDANCE

On 16 October the PPF announced that, following its July update of the section 179 guidance to reflect the coming into effect of the new definition of money purchase benefits, it has updated its guidance on other types of valuation. Updated versions of the following guidance were published.

- The guidance for undertaking valuations in accordance with section 143 of the Pensions Act 2004. The PPF also published an updated version of its booklet on additional information for carrying out a section 143 valuation.
- The guidance for undertaking the actuarial valuation of a closed scheme in accordance with Section 156 of the Pensions Act 2004.
- The guidance for actuaries undertaking the valuation under section 152 of the Pensions Act 2004 and the Statement setting out how the Board of the Pension Protection Fund will make a funding assessment under Section 152(10C) of the Pensions Act 2004. This guidance had previously been updated in September but a further updated version was published in October.

The PPF states that the updated guidance will assist schemes that are currently in, or have completed, a PPF assessment period.

DEPARTMENT FOR WORK AND PENSIONS

DC GOVERNANCE STANDARDS AND CHARGES

Background

For some time now, the DWP has been looking at the issues of statutory governance standards and charges for DC schemes, with a Call for Evidence on scheme quality published in July 2013 and a consultation published on charges in October 2013. In March 2014 the DWP published a consultation outcome covering both of the two previous papers and setting out the Government's proposals in these areas, asking further consultation questions in some cases.

In October the DWP built on this previous work by publishing a Command Paper setting out responses to those further consultation questions asked in March and launching a further consultation on draft regulations on governance and charges in occupational pension schemes. The Paper also refers to corresponding provisions being made or due to be made for workplace personal pension schemes (the Independent Governance Committee proposals for providers of workplace personal pension schemes and an upcoming consultation from the FCA on charges in workplace personal pensions which was subsequently issued on 30 October), but in this article we focus on occupational pension schemes. A summary of some of the key aspects of the proposals in relation to occupational pension schemes is set out below.

Minimum governance standards

Scope of the standards

The Government intends that the governance standards should apply to occupational pension schemes which are money purchase schemes and, in certain respects, to schemes which are not money purchase schemes but which provide some money purchase benefits.

The Paper explains that, in the case of "hybrid" schemes where there are both defined benefit and money purchase benefits (for example, where there is a DB section closed to new members who instead accrue money purchase benefits), some of the new governance provisions (for example, those concerning the default arrangement and the assessment of charges and transaction costs) will only apply in relation to the provision of money purchase benefits, but because of their nature, other governance measures (such as the requirement for there to be a chair) have to apply to the scheme as a whole.

However, there are some schemes that it is proposed should *not* be covered by the governance arrangements, including schemes which provide no money purchase benefits other than benefits which are attributable to the payment of Additional Voluntary Contributions.

The standards

The Paper sets out the provisions that the Government intends to include in legislation which include the following requirements.

- Trustees must ensure that default arrangements are designed in members' interests.
- Trustees must carry out a review of their default arrangement strategy and of the performance of the underlying funds at least every three years and without delay after any significant change in investment policy or the demographics of scheme membership.
- Trustees must ensure that core scheme financial transactions are processed promptly and accurately.
- Trustees must calculate the charges and transaction costs borne by members and assess the extent to which they provide good value for members. However, in recognition of the fact that trustees may not be able to access all of this information on transaction costs in the first reporting period, it is intended that trustees will be required to report on those transaction costs about which they are able to get information. They will also have to explain in the Chair's Statement where they have not been able to obtain information, along with an explanation about how they will obtain fuller information in the future.

- Schemes will be required to have a chair of trustees, subject to a three month period of grace for existing schemes and in cases where a chair resigns, dies or is removed. The chair will have an additional regulatory responsibility above and beyond the scheme's other trustees to sign off an annual Chair's Statement to be included in the scheme's annual report.
- The Chair's Statement must contain specified information about how the minimum governance standards have been met and will also have to include an assessment of how the combined knowledge and understanding of the trustees, together with the advice which is available to them, enables them to properly exercise their functions as trustees.
- Additional requirements are also proposed in the case of master trusts, for example that they must have a minimum of three trustees, with the majority, including the chair, being independent of the providers used by the scheme. The March paper had proposed seven as the minimum number and this latest Command Paper states that the Government intends to use guidance to set out its expectation that most master trusts are likely to need at least five trustees to provide the appropriate breadth and depth of oversight.

Further work on transparency

The Paper states that, in 2015, the Government will build on the new reporting requirements set out above relating to costs and charges by consulting on draft regulations to drive further transparency, with a view to the further regulations coming into force in 2016.

Also in 2015 the Government will examine whether regulation for further transparency in DB schemes is required.

Charges

Scope of the provisions on charges

The measures on charges will apply to money purchase benefits within schemes used as qualifying schemes for automatic enrolment. There will be some exceptions, such as certain small self-administered schemes. However, the Paper states that there will be some schemes that are **not** subject to the governance measures described above, which may still be subject to the charges measures where they are used as a qualifying scheme and provide money purchase benefits, and one of the examples given is schemes where the only money purchase benefits are attributable to AVCs.

Detailed proposals

The Paper describes how the DWP has moved from the core charges measures announced in March to the detailed policy set out in the draft regulations.

Areas of policy which are set out in more detail include:

- who has responsibility for complying with the charges measures – it is proposed that the legal duty should rest with the trustees;
- defining member-borne deductions that fall within the cap;
- defining the default arrangement – it is proposed that this will cover any arrangement into which workers' contributions are directed without them having made an active choice as to where contributions are directed as well as certain arrangements into which 80% of the workers are contributing; and
- when the cap applies, to whom and on what funds.

The implementation timetable is confirmed in the Paper, with key points to note including the following.

- From April 2015: (i) the charge cap will be introduced in the default arrangements of qualifying schemes set at 0.75% of funds under management; and (ii) member-borne payments for advice to employers (consultancy charges) will be banned from all qualifying workplace personal pension schemes.
- From April 2016:
  - member-borne adviser commission and consultancy charges will be banned from qualifying schemes with a consultation on the commission ban for occupational pension schemes to be issued in 2015.

(Originally consultancy charges were due to be banned from all qualifying schemes from April 2015 but, as noted above, that earlier date now only applies to personal pension schemes. The DWP notes that the Government and regulators are not aware of any consultancy charges in occupational pension schemes and that, in any case, many trust deeds and rules would not allow such charges.)

  - Active Member Discounts will be banned from qualifying schemes, with the intention being that any member who makes a contribution to a qualifying scheme after April 2016 whilst a worker of the employer must not be charged more when they cease contributing than they would if they were still making contributions to the scheme.

- In 2017, the level of the default arrangement charge cap will be reviewed to see whether the level should be lowered and whether it should include some or all transaction costs.

Regulatory approach and compliance

The Paper also contains proposals in relation to the regulatory approach. Additional information will have to be disclosed in the scheme return – the name of the chair of trustees, whether the trustees have produced the Chair's Statement and whether the scheme complies with the charge cap and the measures banning certain charges.

The draft regulations also contain provisions about enforcement activity. For example, they require the Regulator to issue compliance notices where the Chair's Statement has not been produced or where there has been non-compliance with the charges provisions, and state that the Regulator must issue a penalty notice where it is of the opinion that the person has failed to comply with a compliance notice or certain specified provisions.

The DWP states that it recognises that for a minority of occupational pension schemes that are already being used as qualifying schemes, compliance with the charges measures could be more difficult than for other schemes. A mechanism is therefore proposed so that, if trustees identify that there is a risk that they may be unable to comply with the cap over the charges year, they should use their best endeavours to become compliant but, if despite this they are unlikely to be able to comply over the charges year, they can invoke an 'adjustment measure' which will be available between April and October 2015. Under this measure trustees would initiate a process whereby they give at least one month's notice of an 'adjustment date' and, from that date, members' contributions are diverted into a compliant fund in that scheme or the employer is informed that it has to re-enrol jobholders into a different scheme which is compliant with the cap. The existing arrangement is closed to future contributions and is not subject to the cap from the 'adjustment date'.

The Regulator's Statement

The Regulator issued a Statement in relation to the Paper reporting that it has been working closely with the DWP to ensure that the new regulations complement what it has already set out in its current DC Code. The Regulator goes on to acknowledge that trustees are experiencing a great deal of change and states that it will be providing guidance as soon as possible but, in the meantime, trustees should continue to follow the DC Code. The Regulator will update the DC Code once the new legislation is in place.

Next steps

The consultation closes on 14 November 2014. It is intended that, in early 2015, regulations will be laid in Parliament for the charges and governance measures as they apply to occupational schemes. The regulations are intended to come into force on 6 April 2015.

April 2015 is set to be a busy time for the trustees of schemes with DC benefits with the majority of these measures to be introduced at the same time as the Budget reforms. We will provide a further update designed to help trustees understand their new obligations on governance and charges and what action they need to take once the final form of the regulations has been confirmed.

In the meantime, as an initial step trustees can start to identify: (i) whether their schemes are likely to be affected by the changes, in particular noting that some schemes will be caught by the charges reforms but not the governance reforms; and (ii) whether they think that their current governance processes and charging structures are likely to need amending. In relation to governance, we would expect that well run schemes will already comply with many of the new requirements but the requirement for the Chair's Statement evidencing this will be new. If you would like any further information or training on the proposals to assist with these initial considerations, please get in touch with your usual DLA Piper pensions contact.

AUTOMATIC ENROLMENT THRESHOLDS

On 15 October, the DWP published a consultation about its proposals for changes to the earnings thresholds for automatic enrolment for 2015/16.

Automatic enrolment qualifying earnings trigger

This is the trigger which jobholders have to exceed in order to qualify for automatic enrolment and for the current tax year it is set at £10,000 in line with the PAYE personal tax allowance.

The DWP states that it would like to test whether maintaining the alignment between the earnings trigger and the income tax threshold remains right in the light of proposed increases to the threshold (in the 2014 Budget the Chancellor set out his intention to increase the threshold to £10,500) and suppressed earnings growth.

The consultation therefore seeks views on the following four options for the 2015/16 earnings trigger.

- Option 1 – freeze the trigger at its current level of £10,000.
- Option 2 – raise the trigger by indexation, either by CPI (which would give a figure of £10,183) or by growth in earnings (which would give a figure of £10,045).
- Option 3 – increase the trigger to £10,500 in line with the threshold for paying income tax.
- Option 4 – use the Pension Commission benchmark replacement rate (that is, the ratio of income in retirement to income in work) to determine the trigger.

The consultation explains that the Pension Commission benchmark replacement rate for people earning less than around £10,000 is 80%. It states that, based on an illustrative new State Pension start rate of £148.40, the DWP expects the majority of people working today to receive around £7,700 in retirement from the State Pension, which means those currently earning £9,876 or less will meet the benchmark replacement rate of 80% with the State Pension. However, it is said to make sense to automatically enrol those earning more than £9,876 so that their income in retirement does not fall short of this benchmark. The consultation states the actual 2015/16 rate is likely to be higher than £9,876 due to uprating of the Pension Credit standard minimum guarantee.

Qualifying earnings band – lower limit

This is the lower limit of the band of qualifying earnings on which the minimum contribution requirements are measured, and is also the earnings threshold which workers who are eligible to opt-in rather than be automatically enrolled must exceed if they are to be entitled to an employer contribution. The figure for the current tax year is £5,772.

In the consultation document the DWP states that its view is that the National Insurance Contributions Lower Earnings Limit should be the factor (as is currently the case) that should determine the value of the bottom of the qualifying earnings band for 2015/16.

Qualifying earnings band – upper limit

This is the upper limit of the band of qualifying earnings on which the minimum contribution requirements are measured. The figure for the current tax year is £41,865.

In the consultation document the Government states that its provisional view is that the National Insurance Contributions Upper Earnings Limit at its announced value of £42,285 for 2015/16 is the factor that should determine the top of the qualifying earnings band. This is the factor that currently sets the upper limit of the qualifying earnings band.

Next steps

It is recognised that whilst any changes will not come into effect until 6 April 2015, software providers will need advance notice in order for as much of the process as possible to be automated and therefore the DWP intends to respond to the consultation in December, around the time of the Autumn Statement (which is scheduled for 3 December).

Once the new thresholds have been confirmed, employers will need to ensure that they adapt their processes so that they are ready to comply with the new thresholds once they are introduced. The proposal to confirm the Government's decision later this year is therefore useful in order to give employers and their software providers sufficient time to make any changes needed.

CONSULTATION ON NEST RESTRICTIONS

In the September edition of Pensions News, we reported that the Minister for Pensions had announced that a short technical consultation on draft legislation would be commenced this autumn to remove the annual contribution limit and bulk transfer restrictions on 1 April 2017, and that the Government retains the option to remove the individual transfer restrictions from 1 October 2015.

On 9 October the DWP published the technical consultation on two draft statutory instruments – the National Employment Savings Trust (Amendment) Order 2015 and the Transfer Values (Disapplication) (Revocation) Regulations 2015. The consultation (which closed on 29 October) seeks views on whether the two draft statutory instruments achieve the policy intention of removing NEST's annual contribution limit and transfer restrictions from 1 April 2017.

At this stage the draft statutory instruments do not make reference to the restrictions on individual transfers coming into force earlier than April 2017. However, the consultation notes that confirmation received from the European Commission that the lifting of these particular restrictions as early as 1 October 2015 would be compatible with State aid means that the Government could bring forward the timing of the removal of these restrictions, subject to the relevant Parliamentary procedures.

SHORT SERVICE REFUNDS

Background

Under current legislation if a member of an occupational pension scheme has at least three months but less than two years' qualifying service under a scheme when their pensionable service terminates, the member can receive a refund of their employee contributions (a "short service refund") or transfer the benefits. Where a member has at least two years' qualifying service they are instead entitled to short service benefit under the scheme.

The DWP reports that money purchase occupational pension schemes currently make around 20,000 short service refunds every year and that this figure was forecast to grow with the continuing roll-out of automatic enrolment. The Government has therefore previously stated its intention to abolish short service refunds for such schemes and to introduce a system of automatic transfers of small pots in money purchase schemes.

To this end, the Pensions Act 2014 contains amendments to the existing legislation which would essentially have the effect of abolishing short service refunds for money purchase benefits, save for where the member has less than 30 days' qualifying service. These amendments have not yet been brought into force and whilst it was previously indicated that they would be brought into force some time in 2014, no definite announcement had been made.

The DWP's October announcement

On 22 October, a formal announcement was made on the timing of these amendments with the DWP stating that it intends to bring these changes into effect from October 2015. This is said to represent a further measure to boost pension saving, and to lay the ground for wider Government plans to make workplace pension saving easier by introducing automatic transfer arrangements.

Further detail about the changes

The amendments in the Pensions Act 2014 relate to cases where the member:

- has at least 30 days' qualifying service (as opposed to the current two years) and all of the benefits "*would necessarily be money purchase benefit*"; and
- the person's active membership began after the changes come into force in October 2015 (or the person re-joins the scheme after this date having previously received a short service refund or made a cash transfer sum).

In such cases, the member will be entitled to short service benefit immediately after completing the 30 days' qualifying service. Short service refunds will still be payable if a member leaves within the first 30 days of qualifying service. However, on completion of the 30 days' qualifying service, the member will cease to be entitled to receive a short service refund, although they will still be able to request a transfer.

The DWP states that setting a 30 day qualifying period means that schemes will still be able to offer those who have joined the scheme through their contract of employment a refund of their contributions if they leave within the first month of membership. This therefore gives broad parity with those who are enrolled into the scheme under the automatic enrolment legislation and have a statutory right to opt out within one month and receive a refund.

The interaction with the Finance Act 2004 is also worth noting. The criteria for a sum to be a "*short service refund lump sum*" authorised payment under the Finance Act 2004 include that the member is *not* entitled to short service benefit. This means that the members who will be entitled to short service benefit by virtue of having completed 30 days' qualifying membership will not meet this criterion of a short service refund lump sum. This effectively prevents schemes from continuing to allow refunds under their scheme rules if there is no entitlement to them under the legislation, because to do so would result in an unauthorised payment and tax charges.

Whilst this change to the legislation is not due to take place for almost a year, it is important for schemes to be aware that it is on the horizon so that they can make changes to their scheme rules if needed (which will depend on how the rules on these points are currently drafted) and change their administrative processes in time for October 2015. In making these changes, it will be important for schemes to correctly identify which members will be impacted – in particular, identifying whether all of a particular member's benefit would "necessarily be money purchase benefit", and ensuring that the right is only removed for members who began their relevant service after the changes come into force.

LEGISLATION

PENSION SCHEMES BILL

Introduction

This is the Bill which will introduce legislation to facilitate the development of models of Defined Ambition schemes and to enable collective schemes to be developed. This is also the Bill which it is intended will reflect certain aspects of the Budget reforms – the ability to prohibit transfers from unfunded public service schemes to DC schemes, the introduction of the guidance guarantee and new safeguards for individuals who wish to make a DB to DC transfer.

In this article we provide a brief update on some of the key developments in relation to the Bill which took place during October.

Progress through Parliament

During October, the Pension Schemes Bill continued to progress through Parliament, with the Public Bill Committee stage commencing on 21 October.

The debates on 21 and 22 October took the form of oral evidence to the Committee, for example from the Regulator, the Pension Protection Fund, the Financial Conduct Authority, The Pensions Advisory Service, the Money Advice Service, the Association of British Insurers, the National Association of Pension Funds, and the Minister for Pensions. Further debates followed on 28 and 30 October, during which the detailed provisions of the Bill were debated, with further debates in early November.

During a debate on 28 October, it was stated that it is hoped that the Bill will receive Royal Assent around March.

Timing in relation to Defined Ambition

During the debate on 22 October, the Minister for Pensions stated that it is hoped that the provisions of the Bill on Defined Ambition will be available from April 2016. This point was reiterated in an information note produced for the Committee stage which was published on 23 October. The note, entitled "*Pension Schemes Bill Information Note – Defined Ambition pensions and Collective Benefits*", states that the aim is for the required secondary legislation and any additional tax changes to come into effect for April 2016, so that employers considering options at the time of the ceasing of contracting out have more options available to them than at present.

Notices of amendments

During October the Government tabled a number of amendments to the Bill. A key set of amendments was those to introduce the framework of the guidance guarantee which will form part of the Budget reforms. (Further information on this is set out in the "Budget Reforms" section of this newsletter.)

The other amendments are largely technical in nature concerning the requirements which will apply to Defined Ambition and/or collective schemes. For example:

- amendments are proposed to the subsisting rights provisions (i) to replace the existing regulation making power with a broader power to provide for cases in which the subsisting rights provisions do not apply, for example, in relation to collective benefits, and (ii) so that any proposal to modify a scheme which would or might replace a right to income with a right to a non-income benefit would be a protected modification; and
- amendments are proposed to the Pensions Act 2004 to set out how certain powers of the Regulator apply in respect of collective benefits and to make it clear how the new scheme categories apply in relation to scheme funding and PPF eligibility.

Interaction with the Budget reforms

A note published on 17 October to give information about the Bill for the House of Commons Committee stage provides a brief overview of the Bill and also addresses the interaction between Defined Ambition and the new flexibilities announced in the Budget. In relation to this interaction, the note states that:

- the Defined Ambition legislation will not restrict individuals from accessing the new Budget flexibilities – there will often be more than one type of benefit arrangement within a Defined Ambition scheme and the policy intention is that members will be able to access those arrangements flexibly, either directly or through a transfer to a DC arrangement;
- similarly, the policy intention for members of schemes offering collective benefits is that they will be able to access these benefits flexibly, either directly or through a transfer to a DC arrangement;

- legislation to provide for this will be considered in the future; and
- while there may be different requirements on the scheme in terms of the advice or guidance that must be offered for different types of benefit arrangement within the scheme, the individual will have the choice over what to do with their savings.

The part of the Bill which has the most immediate significance is the introduction of the framework for the guidance guarantee. Looking further ahead, it is useful to now have confirmation on the expected timescale of April 2016 for the legislation on Defined Ambition and collective schemes. The legislation in relation to these areas remains subject to change with a large number of amendments proposed during October which continued to be discussed by the Public Bill Committee in November. As the legislation becomes more settled in this area, we will provide a more detailed report on the provisions relating to Defined Ambition and collective benefits.

HMRC

BULLETIN ON THE END OF CONTRACTING-OUT

On 22 October HMRC published the third in its series of Countdown Bulletins providing updates about activities linked to the end of contracting-out.

This edition looks mainly at the Scheme Reconciliation Service, which trustees and administrators can use to reconcile their records for non-active members against HMRC records in advance of the end of contracting-out. As well as providing information on some specific aspects of the Service, the bulletin reports the following more general points.

- There has been a positive take up of the Scheme Reconciliation Service and HMRC has received 1,889 requests and issued records for 1,175 schemes.
- Following the sharing of membership data with schemes, HMRC is now beginning to receive queries from a small number of schemes where there is a discrepancy between HMRC records and those held by the scheme. However, the volume of queries received to date is much lower than HMRC anticipated. The Bulletin states that although schemes have requested reconciliation, "*they do not appear to be looking at the data*". HMRC states that any delay in providing queries to HMRC shortens the timescale for schemes to reconcile the data, and therefore asks that schemes start reconciling and raising queries with HMRC as soon as possible.

The bulletin also has a section about the requirement that has applied since 6 April 2014 for employers to show the Scheme Contracted-Out Number (SCON) as well as the Employer's Contracting-out Number on their Full Payment Submissions when submitting contracted-out National Insurance Contributions for employees who have been in a contracted-out scheme during the tax year. The bulletin reports that HMRC will be withdrawing the facility for employers to use a temporary SCON at the end of the 2014/15 tax year, so these employers will need to take action to report the correct SCON from April 2015.

UPDATES TO THE RPSM

On 3 October HMRC published updates to the Registered Pension Schemes Manual, with changes made including the following.

- Changes to the section on registration, for example, so that these pages now also cover scheme administrator requirements including the requirement introduced by the Finance Act 2014 which came into force on 1 September for the scheme administrator to be fit and proper for the role.
- Amendments have been made to reflect other provisions in the Finance Act 2014 such as changes to the limits on trivial commutation, small pots and drawdown which were announced in the 2014 Budget, and the introduction of individual protection 2014.

PUBLIC SERVICE PENSION SCHEMES

LOCAL GOVERNMENT PENSION SCHEME

Background

In June 2014 the Department for Communities and Local Government (DCLG) published a consultation on draft scheme governance regulations for the new Local Government Pension Scheme which came into force on 1 April 2014. The draft regulations relate to provisions of the Public Service Pensions Act 2013 designed to achieve the policy objective of raising the standard of management and administration of public service pension schemes and to achieve more effective representation of employer and employee interests in that process. They included provisions in relation to local pension boards and the scheme advisory board. The consultation closed on 15 August.

October consultation

On 10 October the DCLG published a further consultation proposing a new Part 3 (Governance) to the Local Government Pension Scheme Regulations 2013.

Governance

The draft regulations include provisions on scheme governance that were the subject of the June consultation, although it is noted that, in light of discussions with the shadow scheme advisory board and comments from other interested parties, those draft regulations have been revised. This latest consultation is said to provide a second opportunity to comment on these provisions alongside other provisions that are being proposed on cost control.

Cost control

The provisions in relation to cost control cover the following.

- Provision for the employer cost cap, although at this stage the cap is not set out in the regulations. It is reported that, during the period of the consultation, a draft valuation report prepared by the Government Actuary's Department will be issued which will include the proposed employer cost cap figure.
- Provision for an additional function for the Scheme Advisory Board whereby the Board obtains scheme cost assessment and, where the overall cost of the scheme is above or below the target overall cost of 19.5% of pensionable earnings of members of the scheme, the Board may make recommendations to the Secretary of State as to the steps to take to bring the overall cost back to the target.

Next steps

The DCLG states that the comments received in response to the June consultation will be taken into account with those received in response to this consultation. This consultation closes on 21 November 2014. The regulations are proposed to largely come into force on 1 April 2015 although some provisions are proposed to come into force on 1 January 2015 for limited purposes (for example, for the purposes of appointment of members of local pension boards and the scheme advisory board).

TEACHERS' PENSION SCHEME

Background

In March 2014 the Teachers' Pension Scheme Regulations 2014 were made which are the main regulations which implement the new scheme from April 2015 in line with public service pension reform.

However, there are some areas not covered by those regulations and therefore the Department for Education published a consultation in April on further changes covering issues such as scheme valuations and the operation of the employer cost cap; member contribution structure; consequential amendments to the Teachers' Pensions Regulations 2010; and miscellaneous and technical amendments to the Teachers' Pension Scheme Regulations 2014. The consultation closed on 18 July.

Response to consultation

On 3 October the Department for Education published the response to that consultation setting out a summary of the main points raised under each section and question of the consultation, along with the Department's final position.

It also notes areas where changes will be made to the final form of the regulations following the consultation. For example, amendments to build on what was included in the draft regulations so as to make clearer the respective roles of the Secretary of State and the Scheme Advisory Board in the process for dealing with breaches in the employer cost cap.

It is also worth noting that whilst the Department stated that it remains of the view that the proposed structure and arrangements for member contributions are appropriate, it also said that further reviews of the arrangements will be carried out in line with the timetable for future valuations.

Two sets of regulations to give effect to the changes (the Teachers' Pensions (Miscellaneous Amendments) (No. 2) Regulations 2014 and the Teachers' Pension Scheme (Amendment) Regulations 2014) were laid before Parliament in October and come into force on 1 April 2015.

Next steps

The response to consultation reports that whilst the amending regulations complete the reform picture for the main Teachers' Pension Scheme, further amendments are needed to the associated Premature Retirement and Additional Voluntary Contribution arrangements in order to ensure they continue to work effectively when the reform arrangements are introduced. In the case of the AVC regulations, it is also reported that the Department for Education intends to take account of the changes announced in the Budget and provide members with more flexibility on how they access their funds.

The Department for Education states that it will provide more details on the proposals later in 2014 and intends to lay amendments to the Premature Retirement and AVC regulations in time for them to come into effect on 1 April 2015.

NHS PENSION SCHEME

Background

On 1 August the Department of Health published an update in relation to the April 2015 reform of the NHS Pension Scheme. The update stated that the regulations to give effect to the reforms are being prepared and would be the subject of a consultation in the autumn. In the meantime the update set out the proposals for the detailed design of the 2015 scheme and transitional arrangements.

In October, two consultations were issued in relation to regulations to give effect to the reforms.

Main regulations

On 20 October the Department of Health published a consultation on the draft National Health Service Pension Scheme Regulations 2015 which are to provide the legal basis for the 2015 scheme and implement the detailed scheme rules. The regulations are proposed to have effect from 1 April 2015.

The consultation (which closes on 5 December 2014) explains the purpose and effect of the provisions set out in the draft regulations. It follows the structure of the draft regulations and is divided into nine parts which cover: preliminary points (scheme establishment and commencement); governance; scheme membership; contributions; members' benefits; survivor benefits; transfers; independent providers; and general.

Transitional and consequential regulations

On 31 October the Department of Health published a further consultation which looks at the draft National Health Service Pension Scheme (Transitional and Consequential Provisions) Regulations 2014. These draft regulations cover three areas.

- Disapplying certain procedural requirements that would otherwise apply under the contracting-out legislation (such as the requirement to give formal notices to earners) in order to ensure that transferring members and new members of the 2015 scheme remain in contracted-out employment until contracting-out ends in April 2016.
- Preventing members of the current scheme from gaining rights as early leavers under that scheme when they transfer to the new scheme.
- Ensuring that members do not suffer unexpected tax consequences as a result of the way the Government has chosen to structure the ill health provisions of the new scheme.

The consultation closes on 25 November 2014 and it is anticipated that the proposed regulations will be subject to parliamentary debate at the start of 2015 and the regulations will come into force on 1 April 2015.

OTHER NEWS

NEWS FROM THE PENSIONS OMBUDSMAN

Pension liberation

On 24 October the Pensions Ombudsman Service published an update on the number of pension liberation complaints it has received. This provides the following updates.

- To date around 140 complaints have been received in relation to pension liberation.
- Nearly 90% of these are from people whose pension provider has not allowed a transfer because the provider believes that its purpose is pension liberation.
- Over 70 of the complaints are about transfers to two different arrangements, which the Pensions Ombudsman is already investigating.
- The other complaints are from people who did transfer their benefits but the scheme they transferred to is no longer contactable or their pension benefits in the new arrangement have since been effectively "frozen" because of regulatory action.

It remains the case that the Ombudsman expects to be able to publish its decisions later this Autumn.

Website

On 28 October, an update was issued announcing that the Pensions Ombudsman has launched a new website to provide simpler, clearer information about what it does and how it can help. The update goes on to report that:

- an improved search function on the website makes it easier to find previous decisions;
- guidance and case studies have been included on how common issues are dealt with;
- the casework correspondence has also been reviewed and improved;
- over the next few months additional IT security measures will be introduced which will mean that people can communicate with the Ombudsman's office electronically during the application and case investigation process;
- the changes are a first step in a long term aim of sharing more knowledge and experience, and providing a more accessible, responsive service; and
- as part of this the Pensions Ombudsman and PPF Ombudsman are now called the Pensions Ombudsman Service, although this change of name does not affect the investigation process or the statutory roles.

Recruitment

On 17 October the DWP issued a press release stating that it will shortly commence recruitment for a new Pensions Ombudsman and Deputy Pensions Ombudsman.

The press release notes that the Ombudsman will stand down from his post in late spring 2015 and that the Deputy Ombudsman's second term ends next autumn. It goes on to state that both post holders will be flexible about their departure dates to ensure a smooth transition and that the Deputy Ombudsman is aligning her departure with that of the Ombudsman to enable the DWP to launch a combined recruitment exercise for the roles.

EIOPA WORK PROGRAMME

On 1 October the European Insurance and Occupational Pensions Authority (EIOPA) published its Work Programme 2015 dated 29 September 2014. Points of note within the programme in relation to occupational pensions include the following.

- In 2015, depending on the progress of the IORP II Directive, EIOPA will prepare advice to the European Commission in those areas of responsibility which may be given to EIOPA under the new Directive. Areas listed in relation to this advice are pension benefit statements, the risk evaluation for pensions, remuneration of the governing body of IORPs, and other areas as required.

- EIOPA will look at solvency topics for occupational pensions and advice will be given to the Commission on solvency of IORPs in Q4. (Further detail on progress on this issue is set out in the article later in this newsletter.)
- EIOPA plans to run its first stress tests in 2015 for the occupational pensions sector, and the delivery for this is stated to be Q4. In a speech to the NAPF annual conference later in October, the chairman of EIOPA explained that the stress test will assess the resilience and behaviour of IORPs in adverse market developments such as a prolonged low interest environment, and will also incorporate stresses in longevity as one of the major risks in pension funds' overall financial condition. It was also stated that the stress test will be conducted in parallel with EIOPA's work on solvency in order to avoid the duplication of calculations and limit the burden on pension funds and supervisory authorities.
- In relation to transferability of pension rights, the programme refers to finalising advice to the Commission and producing a good practice report. The delivery timescale for the report is stated to be Q3.

EIOPA CONSULTATION ON SOLVENCY

Background

In April 2013 the preliminary results of a Quantitative Impact Study (QIS) were published. The QIS looked at proposals for a "holistic balance sheet" and the calculation of assets, liabilities and capital requirements. The aim of the holistic balance sheet is to make the valuation of assets and liabilities more comparable and transparent across Europe rather than the current system where schemes are subject to different national rules.

The preliminary results included that the potential impact of the introduction of the holistic balance sheet was, for a benchmark scenario, a shortfall for UK schemes of around £450 billion. However, the results were heavily caveated, with it being noted that further work still needed to be completed which may lead to adjustments to the figures, including further work on the way that sponsor support is quantified.

It was therefore welcome news for sponsoring employers of UK schemes when in May 2013 the European Commission announced that provisions on solvency would not feature in its proposals for a revised IORP Directive. In the announcement, the European Commission stated that more comprehensive data was needed before a decision could be taken on this issue. The prospect of new solvency requirements had not been dropped entirely as it was stated to remain "*an open issue*".

When the draft IORP II Directive was published in March, as expected, no provisions were included on solvency although accompanying FAQs reported that the European Insurance and Occupational Pensions Authority is carrying out detailed technical work in this area. EIOPA's intention to continue its work in this area was also set out in its Work Programme for 2015.

October 2014 consultation

On 13 October EIOPA published a consultation paper on its "*Further Work on Solvency of IORPs*". The consultation paper constitutes the first step of the further work on solvency of IORPs that EIOPA is "*undertaking on its own initiative*".

The three main sections of the consultation paper cover the following areas.

- An introduction which provides a more elaborate description of the background and scope of the consultation. Within this section it is noted that:
  - EIOPA's work is **not** related to the Commission's March 2014 proposal for a revised IORP Directive;
  - the areas being looked at in the consultation were chosen because of concerns expressed by stakeholders, and because of their impact on the holistic balance sheet and due to the effect they might have on the technical specifications in other areas;
  - the consultation paper does not and is not intended to pre-empt any decisions on the possible uses of the holistic balance sheet but provides a preliminary analysis of the effects it would have on protection

of members and beneficiaries, functioning of the internal market, economy and national IORP systems; and

– in the end, it is the prerogative of the Commission to decide whether or not to take the advice into account and whether or not to take any legislative initiatives in this area, including the establishment of a legal basis, which would have to be agreed by the European Parliament and the Council.

- A section on "*Valuation of the holistic balance sheet*" which proposes improved definitions and methodologies to value the holistic balance sheet in the areas of contract boundaries, discretionary decision-making, benefit reduction mechanisms and sponsor support.
- A section on "*Supervisory responses*" which is said to discuss the possible uses of the holistic balance sheet and options for the various components of the underlying supervisory framework.

Next steps

The consultation closes on 13 January 2015. EIOPA states that it will consider the feedback received and expects to publish draft technical specifications by early 2015 for a quantitative impact assessment. Following this assessment, EIOPA will develop technical advice to the European Commission on EU solvency rules for IORPs.

Whilst the May 2013 announcement did not completely withdraw the proposals on solvency meaning that it is not entirely surprising that a further consultation has been issued, this continued focus on the holistic balance sheet will nevertheless be disappointing news for sponsoring employers given the potential impact that any new solvency requirements could have. However, it is worth noting that EIOPA makes numerous references in the consultation document to this work being something it is undertaking "on its own initiative", and as EIOPA also notes, it will ultimately be up to the Commission and the European Parliament and Council whether to adopt any legislation in this area. What will therefore be key is the Commission's reaction to the advice which EIOPA intends to deliver in the final quarter of next year.

ON THE HORIZON

- **Exceptions to automatic enrolment duties.** A consultation was expected to be published in early 2014 but, as at the end of September, had not been issued.
- **Equalisation for GMPs.** It had previously been expected that guidance on conversion of GMPs would be published in the spring but, as at the end of September, this had not been published. An HMRC Bulletin on the end of contracting-out issued in July reported that the DWP understands that schemes are waiting for GMP conversion guidance but it thinks it is important to develop fully considered proposals, and guidance will be published when this critical work is completed.
- **Annual Allowance Order.** 27 August was the closing date for comments on a draft Order proposing technical improvements to the legislation on the annual allowance. The draft Order does not state a coming into force date.
- **Pension liberation.** The Pensions Ombudsman expects to be able to publish its decisions on cases concerning pension liberation in the autumn.
- **The end of contracting-out.** The consultation on draft regulations in relation to the power for employers to increase employee contributions or alter future accrual to offset increased national insurance contributions closed on 2 July. It is expected that these regulations will come into force in the autumn.
- **Public service schemes.** The Regulator's consultation on the draft Code of Practice and regulatory strategy for public service pension schemes closed on 17 February 2014. It is anticipated that the Code will be laid before Parliament in the autumn.
- **VAT treatment of pension scheme administration and fund management services.** In the autumn, HMRC will publish guidance about how it will implement the judgments of the Court of Justice of the European Union in the *PPG* and *ATP* cases.
- **Guidance guarantee – levy.** The FCA will consult on draft levy rules in its annual fees policy consultation in October.
- **Guidance guarantee.** The FCA's consultation on the elements of the guidance guarantee for which it is responsible closed on 22 September and the FCA intends to publish a Policy Statement in late autumn.
- **Automatic enrolment thresholds.** The DWP intends to respond to its consultation on the automatic enrolment earnings thresholds for 2015/16 in December 2014.
- **PPF Levy.** In October 2014 the PPF published a consultation on the detailed rules and the levy estimate for 2015/16. The PPF will publish its conclusions on the consultation and the final rules before Christmas 2014.
- **DB to DC transfers.** In light of the Treasury announcement that, following the Budget reforms, DB to DC transfers will continue to be permitted (save for in respect of unfunded public service schemes), the Regulator intends to consult on changes to its transfer guidance in the New Year.
- **DC reform guidance.** The Regulator intends to publish guides on DC reform (the Budget changes, governance standards and charges) in the New Year.
- **Solvency.** Following its consultation on further work on solvency of IORPs (which closes on 13 January 2015), EIOPA will consider the feedback received and expects to publish draft technical specifications by early 2015 for a quantitative impact assessment. Following this assessment, EIOPA will develop technical advice to the European Commission on EU solvency rules.
- **Review of survivor benefits.** The review of different treatment of survivor benefits under occupational pension schemes required to be completed under the Marriage (Same Sex Couples) Act 2013 has been published, although no date has been given for when the Secretary of State will announce whether or not any amendments will be made to the legislation. The Employment Appeal Tribunal's judgment in the *Walker v Innospec* case concerning the restrictions placed on benefits payable to civil partners is the subject of an appeal to the Court of Appeal, with a hearing due to take place on 23 or 24 February 2015.

- **DC regulation.** The Regulator expects trustees of occupational pension schemes to assess the extent to which their scheme complies with the DC quality features and publish a governance statement in relation to this assessment at the end of the 2014/15 scheme year.
- **DC reform.** The far-reaching DC reforms announced in the Budget will come into force in April 2015. The Taxation of Pensions Bill, which contains provision for the tax aspects of the reforms, was laid before Parliament on 14 October 2014.
- **DC scheme quality and charges.** Statutory quality standards for DC schemes, a cap on charges for default funds in qualifying schemes, a ban on consultancy charges in qualifying workplace personal pension schemes and reporting requirements in relation to charges are proposed to come into effect in April 2015. Draft regulations to give effect to this are expected to be laid before Parliament in early 2015.
- **Transparency of DC charges.** The April 2015 measures on charges include some reporting requirements in relation to charges and transaction costs. The DWP intends to build on this in 2015 with a consultation on regulations to introduce further transparency in 2016.
- **Short service refunds.** It is intended that short service refunds will be withdrawn from money purchase schemes in October 2015.
- **Automatic transfers.** An announcement in September about the restrictions on NEST and an announcement in October 2014 about the abolition of short service refunds indicated that the system of automatic transfers may be introduced from 1 October 2015.
- **DC charges.** From April 2016, it is proposed that member-borne commission payments and Active Member Discounts will be banned from DC qualifying schemes.
- **End of contracting-out.** The reform of state pension which will result in the end of contracting-out is due to take effect in April 2016.
- **Defined ambition.** The Pension Schemes Bill which contains provisions to enable the development of Defined Ambition and collective schemes has been laid before Parliament and is expected to receive Royal Assent around March 2015. It is expected that the provisions on Defined Ambition and collective schemes will be available in time for the end of contracting-out in April 2016.
- **IORP II.** The draft updated IORP Directive published in March 2014 proposed that Member States would have to transpose the new IORP Directive into national law by 31 December 2016. However, an updated draft published in September deletes this date and does not replace it with a new date.
- **DC charges.** In 2017 it is proposed that the level of the charge cap will be reviewed, as will the question of whether any transaction costs should be included in the cap.

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