Barnett Waddingham
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SPRING 2016

Current Pensions Issues

TO DO LIST

This edition of Current Pensions Issues includes several actions for trustees. Review the non-exhaustive checklist below with your advisers, following the links in the articles for background information:

- End of contracting-out on 5 April 2016 – actions for formerly contracted-out DB schemes:
  - Consider with employers whether and how to mitigate increased NI costs
  - Notify members by 5 July 2016 that the scheme is no longer contracted-out
  - Consider how to recertify the scheme if it is being used by the employer for auto-enrolment
  - By 5 April 2017, consider whether a rule amendment in relation to GMP revaluation is required and, if so, whether this can be done by employer resolution
  - Review rules and booklets for unintended consequences, including wording issued to members about GMP increases being paid by the state
- Integrated Risk Management: consider with advisers how to approach the new guidance, particularly if an actuarial valuation is in progress.
- Persons of significant control (PSC): corporate trustees should construct a PSC list as soon as possible, submitting it to Companies House with the next annual confirmation statement due after 30 June 2016.
- PPF Levies:
  - Submit appropriate 'Deficit Reduction Contributions' certificates by 29 April 2016
  - Submit 'Block Transfer' certificates by 30 June 2016

The end of contracting-out

Contracting-out of state pension provision is no longer possible, following the introduction of the new state pension system on 6 April 2016. From that date, scheme members who had previously been contracted-out will (subject to earnings) accrue benefits under the new 'single tier' state pension system, with both employers and employees paying higher National Insurance (NI) contributions reflecting lost rebates.

Whilst many employers and trustees will have taken action to mitigate the increased NI costs (some using a statutory amendment power which is still available until April 2021) there are other actions that may still need to be addressed.

BLOG
PMI TV: the rush to contracting out cessation READ MORE >

Auto-enrolment certification: formerly contracted-out schemes

From 6 April 2016, employers will no longer be able to rely on having a contracting-out certificate as evidence that their defined benefit (DB) pension scheme continues to meet minimum requirements as an auto-enrolment (AE) vehicle for active members. It is the employer's duty to determine that the AE quality requirements are met.

The Department for Work and Pensions (DWP) has published guidance on the alternative tests of scheme quality to determine whether a DB or hybrid pension scheme may continue to be used for AE purposes.

The DWP has not granted a period of grace to formerly contracted-out DB schemes, who must now re-confirm that their scheme meets the test as soon as possible (if they have not already).

The government has legislated for a simple test for formerly contracted-out DB and hybrid schemes that considers whether the actuarial value of future service benefits assessed at the last scheme funding valuation meets minimum criteria. To allow for different earnings definitions, the minimum percentages range from 9% to 13% of earnings. However, depending on the definition of earnings used to calculate members' benefits, some schemes may not be able to use this simple test.

> *Instead, employers would have to certify schemes on the basis that the benefits provided meet the minimum prescribed standards.*

There is no prescribed certificate to complete. The employer simply needs to keep a copy of the last actuarial valuation report showing that the contributions are greater than the relevant minimum.

For a transitional period, formerly contracted out schemes may apply this cost of accruals test at overall scheme level (even if there is a material difference in the cost of the benefits accruing for different groups of members), but only:

a) in respect of members who were in contracted-out employment on 5 April 2016; and

b) where the scheme rules have not been materially amended after that date.

The transitional period ends when the scheme's actuary signs off the next valuation report (or 5 April 2019 if sooner).

BLOG

RIP contracting-out: gone but not forgotten

Chinese New Year, the Budget, the Six Nations, Easter and the Cricket T20 World Cup have all come and gone already in 2016. Something else that's been with us for a long time has also finished... rest in peace contracting-out.

READ MORE >

Statutory override for GMP revaluation

Regulations are now in place allowing formerly contracted-out DB schemes to modify their rules in relation to the revaluation of Guaranteed Minimum Pensions (GMPs) before retirement.

Under previous legislation, statutory GMP revaluation was triggered when 'contracted-out service' ended for an individual. The DWP has now updated regulations to avoid having such revaluation apply to active members of contracted-out schemes when all contracted-out service ended on 5 April 2016. Instead, depending on the rules of the scheme, fixed rate GMP revaluation might not apply until the individual leaves the pension scheme (i.e. becomes a 'deferred' member).

A statutory override allows employers to amend rules (where they might otherwise not have the power) so that fixed rate GMP revaluation is only triggered on ending of pensionable service rather than the ending of contracted-out service. The resolution can be passed between 6 April 2016 and 5 April 2017, and can be backdated.

GMP increases paid by the state

The National Audit Office (NAO) has published a report on the impact of state pension reforms on individuals with GMPs – i.e. those who contracted-out on a salary-related basis at some time between April 1978 and April 1997.

Under the new state pension, the government will no longer make explicit adjustments to state benefits relecting inflationary increases on pre-88 GMP, or inflation above 3% on post-88 GMP, as it had under the old system.

The NAO's report notes that the way this will impact on individuals will "depend on their particular circumstances". The impact will also depend on future government policy for state pension increases and future rates of inflation.   Their analysis suggests that, in 2015/16 prices, individuals may receive between £34 per week more and £11 per week less than under the old system, depending on how they built up their pension entitlement and future inflation rates.

Under the new state pension, the NAO says that those individuals where the majority of their GMP was accrued after 1988 will be comparatively better off.   People will also fare better where their new starting state pension is higher than they would have got under the current system, because the increase from the annual uprating of the new state pension should offset the amount notionally lost in GMP increase top-ups.

The NAO also notes that individuals will be comparatively worse if inflation is above 3%.

Budget 2016

On 16 March, George Osborne delivered his eighth budget speech in the House of Commons. While there had been much speculation in the weeks beforehand about what the government's anticipated response to the Green Paper on pensions tax relief might say, the Treasury's pre-emptive announcement that there would be no such reforms announced in Budget 2016 meant that anticipation had been effectively curbed. For now.

Following on from the government's Green Paper on "Strengthening the incentive to save" (see News on: Pensions – August 2015), the Chancellor had been expected to lead the Treasury's response and set out plans for the future of pensions tax relief. The main options being considered included:

- **A shift to a single-rate of tax relief** perhaps in the form of a system of 'matching contributions', incentivising basic-rate tax payers, but leading to a reduction in tax relief for higher-rate tax payers.
- **Moving from an Exempt-Exempt-Taxed (EET) to a Tax-Exempt-Exempt (TEE) system**. It was suggested his might take the form of a 'Pensions ISA' scheme where contributions are made from taxed income and top-ups paid by the government.
- **Retaining the current system**, but with modifications. For example, the Association of British Insurers (ABI) had suggested the Treasury could consider removing the Annual Allowance (AA) for DB schemes and the Lifetime Allowance (LTA) for defined contribution (DC) schemes in order to reduce complexity.

While, as part of the 2016 Budget, the Treasury published a Summary of Responses to the Consultation on Pensions Tax Relief there has yet to be an indication of how tax policy in this area might develop in the future.

Other pension issues that were raised in the 2016 Budget included:

- Salary sacrifice arrangements continue to be under review, although such schemes covering pensions contributions, health-related benefits and childcare costs will be allowed to continue;
- Pension Commencement Lump Sums will continue to be payable tax-free despite speculation to the contrary;
- Employer contributions to public sector pensions will rise, reflecting changes to the valuation discount rate as widely expected; and
- The government will push forward with plans to launch a pensions dashboard so that individuals can view all their pension savings in one place, and which will be available from 2019. This was one of the recommendations set out in the Financial Advice Market Review (FAMR) by HM Treasury and the Financial Conduct Authority (FCA) – see below.

BUDGET 2016 OVERVIEW

Everything you need to know

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TPR Guidance: Integrated Risk Management

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TPR: Integrated Risk Management

The Pensions Regulator (TPR) has issued regulatory guidance to help trustees and employers develop an Integrated Risk Management (IRM) framework, which the regulator views as 'an important tool' for managing the risks associated with funding DB pension schemes.

TPR's IRM approach focusses on modelling, understanding and mitigating the interaction between risks in three key areas, with which trustees will already be familiar (i.e. funding, investment and employer covenant).

The idea of collectively monitoring these three risks as an important part of an overall strategy is not new. TPR's Code of Practice on funding DB schemes, for example, devotes an entire chapter to IRM, noting that 'trustees should adopt a proportionate integrated approach to risk management'.

TPR is keen to emphasise that IRM is an ongoing process and that trustees should consider its introduction 'wherever the scheme lies within its valuation cycle'. Trustees are encouraged therefore to discuss with their advisers how risk management processes could evolve to take account of TPR's latest publication. Schemes may already have a risk-management framework in place to use as a starting point, though many will have to undergo an 'initial investment' to get IRM up and running.

As well as detailing the key stages of IRM, the guidance explores a variety of possible risk-assessment approaches that trustees and employers may take, including 'stress testing', 'scenario testing', 'scenario projections', 'stochastic modelling' and 'reverse stress testing'.

Creating a secondary annuity market

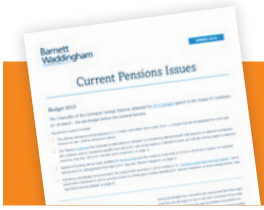
The Treasury and DWP have issued a joint response to their earlier call for evidence on creating a secondary market for annuities.

From April 2017, pensioners will be allowed to sell the income from their annuity to a third party, subject to the agreement of the original provider. In exchange, they will receive a cash lump sum either paid directly to them or into a drawdown arrangement. The penal tax charges that currently apply on cashing in annuities will no longer apply and individuals will instead be taxed on the proceeds at their marginal rate of income tax.

Only those with individual annuities written in their own name may re-assign them. This includes annuities purchased by a pension scheme that have been assigned to the individual following a 'buy-out' with an insurer. The government currently has no plans to bring 'buy-in' annuities (purchased in the trustees' name, within an occupational pension scheme) within scope.

The creation of a tertiary market will be permitted, allowing annuities to be re-assigned more than once. This will potentially allow investors to combine several secondary annuities to sell on in bulk. The original annuity provider will be allowed to buy back annuity contracts, although this will have to be done indirectly through a regulated intermediary. This is a change from the government's original proposal that buy-back would not be allowed.

A number of measures will also be undertaken to improve consumer protection. These include developing an online tool to provide estimates of annuity values to policyholders, extending Pension Wise to incorporate guidance on selling annuities, making independent financial advice compulsory for individuals selling annuities above a certain (as yet undefined) value and requiring that annuity purchasers and intermediaries are authorised by the FCA.



See our Current Pensions Issues – Spring 2015 for more information >

Financial Advice Market Review

HM Treasury and the FCA have published the final report on their Financial Advice Market Review (FAMR). FAMR was launched in August 2015 "in light of concerns that the market for financial advice in the UK was not working well for all consumers". In particular, an 'advice gap' was identified where (in part due to the ending of commission-based remuneration in certain advice markets) consumers are unable to obtain the advice they need at a price they are willing to pay.

28 recommendations for market reform are made in the report, on which the FCA and Treasury are expected to consult in due course. The recommendations included:

- TPR and the FCA should create a factsheet to help employers and trustees understand what help they can provide to employees / pension scheme members on financial matters, without being subject to regulation.
- HM Treasury should consider improving the existing £150 income tax and NI exemption for employer-arranged advice on pensions (an increase to £500 was announced during the 2016 Budget), and should explore allowing consumers to access a small part of their pension pot before the normal minimum pension age, to pay for pre-retirement advice.
- HM Treasury should challenge the industry to create a 'pensions dashboard' (a consumer-friendly digital interface allowing consumers to access their pensions savings data at any time) by 2019. (In progress - see Budget 2016 article).
- The Treasury and FCA should jointly report in 12 months' time on the progress made towards implementation (against the proposed timeline included in the report), and conduct a review of outcomes from FAMR in 2019.

News in brief

TPR / PPF: 2015 Purple Book

TPR and the Pension Protection Fund (PPF) have published the tenth edition of their annual Purple Book. The report summarises recent trends and the risks faced by PPF eligible DB pension schemes.

The report notes that the aggregate deficit of PPF-eligible schemes has risen significantly (from £39.3 billion at 31 March 2014 to £244 billion at 31 March 2015).

Although the total number of contingent assets in place for 2015/16 dropped by about 20% compared with 2014/15, a continuing trend of de-risking and diversification is noted.

PPF: contingent asset guidance

The PPF has published its annual Guidance in relation to contingent assets. The 2016/17 guidance is broadly unchanged from the previous levy year, but includes an additional note citing examples which may help trustees assess guarantor strength according to the PPF's requirements.

PSC requirements

From 6 April 2016, company law requires most unlisted UK companies to take reasonable steps to find out if there is a person or entity with "significant influence or control" over them, and to maintain a register of those persons.

This requirement is expected to apply to most pension trustee companies. The Principal Employer will be a 'person with significant control' (PSC) in many cases.

The information will have to be provided to Companies House from 30 June 2016, as part of the trustee company's filing of annual information.

DWP: early exit charges and transfers

Following consultation, the government is to consider how existing powers to limit pension charges can be used to implement a cap on early exit charges in trust-based DC schemes in a comparable way to that which it is proposing for contract-based schemes.

Meanwhile, the DWP considered whether further guidance and regulation is required in respect of transfer of members' benefits from occupational pension schemes.

In particular, TPR is expected to introduce new guidance for trustees to ensure transfer values are processed promptly and accurately, with ongoing benchmark reporting a possibility.

PPF: levy deadlines

PPF levies for 2016/17 will be based on information submitted via scheme returns before 31 March 2016, and on Experian scores at month-ends between April 2015 and March 2016.

Invoicing will start in the autumn. In the meantime, 2016/17 levies may still be affected by submitting a formal certificate of 'Deficit Reduction Contributions' (by 5pm on 29 April 2016), or certifying 'Block Transfers' during the last levy year (by 5pm on 30 June 2016).

Annual and lifetime allowances

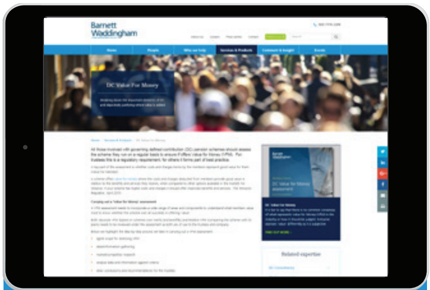
The Finance Bill 2016 has been published which, when enacted, will bring into force reforms announced in the 2015 budget and autumn statement. This includes the reduction in the LTA to £1 million from 5 April 2016 and the various protections available to individuals with pensions savings valued above this revised allowance.

The tapering of the AA for higher earners (from £40,000 down to £10,000 for individuals with total 'income' above £210,000 pa) was incorporated into the Finance Act 2015. See our website for further information.

DC Code of Practice

TPR is considering responses to its consultation on a revised Code of Practice for DC schemes (reflecting pension reforms introduced last year). TPR is aiming to ensure that all of the requirements for trustees of DC schemes are in one place.

The Code applies not just to DC and hybrid schemes but also to DC Additional Voluntary Contributions (AVCs) within DB schemes. The revised code is expected to come into force in July 2016, alongside supporting guides setting out how to meet the standards set out in the code.



For more information about how our Workplace Health and Wealth team can perform a value-for-money (VFM) assessment of your DC scheme, please see our WEBSITE >

PPF Ombudsman: late levy payment

The PPF Ombudsman has rejected a challenge made by the TT Group (1993) Pensions Scheme after late payment interest became due on their PPF levy, which had remained unpaid while it was in the appeals process. The PPF maintains that schemes should still pay levies subject to appeals as it will start calculating interest from the twenty-ninth day after the levy invoice date regardless of its status.

EIOPA: pensions stress test

The European Insurance and Occupational Pensions Authority (EIOPA) has published results of its first EU stress test for the occupational pensions sector. The stress test considers the impact of market and longevity shocks on both DB and DC schemes with results showing that pension schemes are affected more by the adverse market shocks tested than by the longevity shock.

EIOPA intends to continue to develop a 'Common Methodology' for risk assessment, but has now effectively dropped plans for a 'one-size-fits-all framework' for funding.

IFoA note for users of actuarial advice

The Institute and Faculty of Actuaries (IFoA) has published a note for trustees and pension scheme sponsors setting out the professional responsibilities of advisers when performing actuarial calculations and using actuarial software.

You may find the following Barnett Waddingham briefing notes and blog posts interesting:

BLOGS

- Has Osborne given saving a new LISA life? >
- A switch from Scheme Reconciliation Service to Shared Workspace: something to worry about or a surprising benefit? >
- Single-tier, flat-rate: a fresh start for the new state pension? >
- Lifetime ISA or pension: which is better? >
- Contracting out: here's looking at you kid >
- Last Man Standing schemes – the PPF's re-invoicing plan >
- Budget 2016: Pensions tax doesn't have to be taxing… does it? >
- Why the tapered annual allowance could cost more than you think >
- In, out, shake it all about: Britain and the EU hokey-cokey >

BRIEFINGS

- How to survive the EU referendum? >
- Buy-outs and buy-ins – Spring 2016 >

Forthcoming events

Pensions Outlook Conference

Glasgow - 8 June 2016

2016 looks set to be a year of political and economic uncertainty for Scotland and the UK. During our Glasgow half day conference our expert speakers will consider the significant impact these changes will have on the world of pensions. REGISTER >

Employer Pensions and Benefits Conference 2016

Leeds - 14 June 2016 REGISTER >
London - 21 June 2016 REGISTER >

At a time of continual change in the pension and wider business landscape our half day, morning conference will help employers navigate this journey focusing on three fundamental principles; investment, engagement and governance.

Trustee Training (DB Schemes)

Leeds - 23 June 2016 REGISTER >
London - 8 September 2016 REGISTER >

Barnett Waddingham's one day courses in Leeds and London are designed to give trustees a thorough grounding in pensions matters and the confidence to complete TPR's trustee toolkit.

Upcoming webinars

You may also be interested in Barnett Waddingham's range of online seminars. Upcoming webinars include:

- Medically underwritten bulk annuities (26 May 2016) REGISTER >

Recordings of previous webinars (including one on pensions tax changes from April 2016) are available on our BrightTalk channel.

WHAT ELSE IS ON? >

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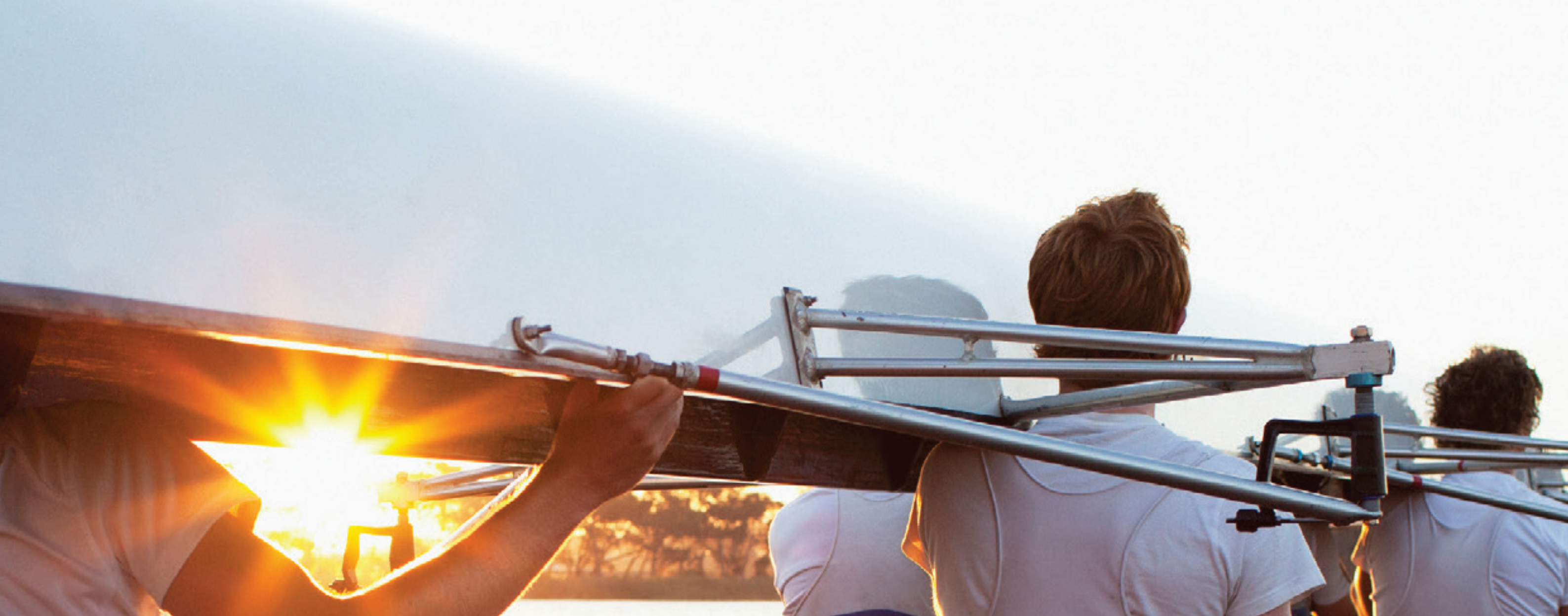

As one of the UK's largest independent providers of actuarial, administration and consultancy services, Barnett Waddingham offers:

- Advice relating to DC pension schemes – trust, master trust and contract
- Scheme Actuary and associated services to DB pension schemes – in the Public and Private Sectors
- Accounting for UK and international companies
- Consultancy and administration services to companies on all wellbeing policies
- Consultancy to the Higher Education sector, across a top-tier client list spanning the UK
- Business insights through practical, risk-based solutions
- Administration services including pensioner payroll, preparation of annual accounts, secretarial services and administration consultancy
- Investment strategy reviews and advice on investment managers
- Employer support regarding insurance arrangements (group life insurance and PHI), and education for senior executives regarding retirement options
- Analysis and modelling of mortality and longevity risk for insurance companies, reinsurance companies, investment banks and pension schemes.

Barnett Waddingham is also a leader in the provision of self-invested personal pensions, small self-administered pension schemes and other retirement arrangements.

This newsletter is intended as a summary of recent pensions-related events. Whilst we have taken care to ensure all information is correct at the time of going to press, the content of this newsletter should not be relied on as advice to act, or refrain from acting, in relation to any of the subjects contained herein. Before taking any such action (or deciding not to act) you should seek appropriate professional advice.

Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail.
Alternatively contact us via the following:

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