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PENSIONS FLEXIBILITY: THE “DC SAVINGS” PARALLEL UNIVERSE

PENSIONS

With the rapid progression through Parliament of the Taxation of Pensions Bill, the task of digging into the very small print of the 2014 Budget changes has begun in earnest. The first impression was that most of the cumbersome and restrictive machinery of the annuity-centric pensions universe was being swept away, to be replaced by a simpler environment in which savers would be empowered to take control over their own pensions wealth (to use the term which features strongly in official press briefings).

The actual choices, however, are far from simple, whether you are a saver coming up to retirement, a trustee of a defined benefit (DB) or defined contribution (DC) scheme, or an employer with financial responsibility for one or more legacy DB schemes together with an ongoing DC vehicle. With the principal focus of the changes being on “DC savings”, the contrast between the DB and DC universes regimes has become even more pronounced.

We have attempted to depict the interaction of the post-April 2015 regimes on a single chart. Follow this link as a wormhole into the new pensions universe.

It is not known whether Professor Brian Cox will make himself available to the pensions community again following his appearance at the 2012 NAPF conference. He seems quite busy explaining the origins and future of the known Universe at the moment. Mr Osborne’s pensions “Big Bang” certainly challenges advisers – and the new providers of “guidance”- to have comparable powers of explanation if savers are to make the right choices. For so long as the ability to travel back in time remains confined to the sci-fi bookshelf and to Hollywood films, savers will for the most part have to live (and die) with the consequences of many of their early pensions-spending choices. It all seemed so much easier when there were so many fewer choices to make.

Follow the further links below as we discuss (and attempt to answer) the following questions:

- What are the immediate issues for trustees (and employers)?
- Will trustees have a duty to advise members about the tax implications of their choices? A recent Determination by the Deputy Pensions Ombudsman suggests that she thinks that the answer is “yes”.

Also in this publication, as we approach the festive season we:

- Remind trustees and employers about what they should be thinking about in terms of the joyful matter of the setting of the 2015/16 PPF levy.
- Give a warning about the status of pensions-related documents which you may stumble across in your loft when trying to find the seasonal decorations.

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What are the immediate issues for trustees (and employers)?

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APRIL 2015 – THE "PENSIONS BIG BANG"

We list below just some of the issues which arise in relation to the April 2015 changes, in particular for trustees and employers still operating legacy DB arrangements:

- Will scheme transfer-out rights be extended beyond minimum statutory rights to facilitate access to the parallel DC savings universe?
- Should cash equivalent transfer values be reduced to reflect current funding conditions?
- Should any existing ban on split transfers be abolished, and if so, on what terms?
- Will the new flexibilities be offered through existing occupational DC schemes, or will members have to switch out into a personal product in order to access the full range of new options?
- If trustees want to take advantage of the statutory override rather than amend their rules, to what extent are they safe to do so; should they involve the employer; and can the employer stop them from going ahead?
- How will trustees' additional communication responsibilities concerning the new guidance guarantee dovetail with existing procedures, and how much more should trustees (or employers) tell members about the new regime? See below for comment on a somewhat alarming recent Determination from the office of the Pensions Ombudsman which raises the prospect of trustees having to become tax advisers.

We are working with our clients as they grapple these, and related, issues. There is no single solution. There is no indication that the timetable will slip, despite the fact that a number of the practicalities, not least those surrounding the compulsory sign-posting of the guidance guarantee, remain obscured by the absence of final legislation.

ARE TRUSTEES OBLIGED TO ADVISE MEMBERS ABOUT TAX: A NEW "RAMSEY" PRINCIPLE?

This is the question which the Deputy Pensions Ombudsman (DPO) found herself addressing in a recent Determination *(Ramsey v Honeywell Normalair-Garrett Limited)* [PO-3290].

Mr Ramsey's employer offered a special arrangement to retiring employees in the form of a pensions top-up to match benefits to those which could have been earned had membership continued under a previous arrangement. Mr Ramsey's chosen retirement date fell after 6 April 2011, with the result that the special arrangement – which was to be delivered through the vehicle of another group pension scheme – fell into the new net for the "annual allowance" test as set by the Finance Act 2011.

Mr Ramsey was not happy about the tax bill (c £7,500) which he incurred as a result of his employer's offer. He was even less happy when he found out that the trustee of the relevant scheme had (along with the employer and the scheme administrator) been in correspondence with HMRC about the potential impact of the 2011 tax changes on the special arrangement, but had (it seems) done nothing to alert members to the issue. Mr Ramsey asserted that if he had known about the problem, he would have taken early retirement in such a way as to avoid the tax charge.

In setting out the respective responsibilities of the parties, the DPO stated that:

"…none of the Company, the Trustee or the Administrator had a legal obligation to contact Mr Ramsey prior to him electing to take his benefits under the Special Arrangement to warn him that he could be subject to a personal tax charge due to changes to the law concerning the annual allowance that came into force on 6 April 2011".

However, she went on to qualify this unexceptionable statement of the traditional legal position by suggesting that if Mr Ramsey actually had been a member of the paying scheme at the time of making his election, the trustees of that scheme would have been under such a legal duty. The DPO reasoned that since trustees owe a duty to act in the best interests of members – and since (citing the 1985 case of *Cowan v Scargill*) this means their financial interests – the trustees would have been obliged to warn Mr Ramsey about the problem, since (by implication) it would have been in his financial interests to find a way of avoiding the tax.

The DPO did not explain whether such a hypothetical breach of duty would have occurred had the trustees not known about the personal tax charge (through its involvement in the correspondence with HMRC), but had simply complied with the scheme rules and made the relevant benefits available in accordance with their strict legal obligations.

The reasoning based on *Cowan v Scargill* is highly suspect. That case concerned the extent of the responsibilities of the trustees of the Mineworkers' pension scheme in carrying out their investment duties. There was no argument about the fact that the trustees had investment duties in the first place.

The DPO's comments in the *Ramsey* case conflate speculation as to whether any "duty to inform" exists, with the degree of care which must be exercised in carrying out that duty (i.e. "in the best interests of the members", according to the DPO).

So trustees apparently have a duty to encourage scheme members to avoid tax. That at least is the upshot of this Determination.

This new decision is not to be confused with the earlier and somewhat more famous Ramsay decision of the House of Lords concerning tax avoidance schemes: *Ramsay v IRC*, 1982. It remains to be seen whether a future court of law will adopt this new Ramsey reasoning when considering the extent to which trustees and providers need to be familiar with the tax consequences of member's personal decisions in the post-April 2015 pensions universe.

PPF LEVIES – 2015/16

The new Experian PPF monthly scores have been up and running since October, and the scores from then until March 2015 will be used for the purposes of calculating the 2015/16 levies.

Trustees or administrators who have not yet logged onto the new web portal as notified earlier in the year by Experian may wish to do so as an escape from other seasonal duties. The complexities of the new system are not for the faint-hearted, and anything simple such as an indication of whether you are doing better or worse under the new system doesn't exactly jump off the screen. It is not helped by the fact that the key designation "PPF Score" does not (currently) provoke a clear response signpost in the PPF's own search engine.

Notable changes have been made to the methodology for calculating insolvency risk in multi-employer schemes that are categorised as "last man standing" (i.e. schemes with neither a requirement nor discretion to segregate on the cessation of participation of an employer). Previously a flat 10 per cent levy discount was applied to such schemes on the grounds that they posed a lower risk to the PPF as the scheme would only enter the PPF once the last employer had become insolvent. The proposal for the 2015/2016 levy year provides a discount of up to 10 per cent for such schemes. In order to benefit from this discount, trustees are required to confirm to the Pensions Regulator by 31 May 2015 that they have obtained legal advice from their solicitors (appointed in accordance with section 47 of the Pensions Act 1995) which confirms that, in the legal adviser's opinion, the scheme's rules do not contain a requirement or discretion for the trustees to segregate assets on an employer ceasing to participate in the scheme.

5pm on 31 March 2015 is a key "contingent assets" date. As before, details of contingent assets will need to be submitted by trustees through the Exchange portal using the appropriate certificates.

Notable points this time around are as follows:

- For groups proposing to put in place a guarantee in certain circumstances, the employer's insolvency score will be replaced by an adjusted insolvency score in respect of the guarantor which takes account of the impact that the guarantee being called upon could have on the guarantor's gearing ratio.
- Adjustments will not be made where the guarantor is the ultimate parent company of the group and its accounts are consolidated to include the sponsoring employers' pension liabilities.
- Groups proposing to put in place PPF-compliant parent or group company guarantees should obtain levy estimates for the 2015/2016 levy year based on both the insolvency risk ratings of the proposed guarantor (if a guarantee is put in place) and the current employers (in the event that the guarantee is not put in place). Steps should also be taken to ensure that insolvency scores and data held by Experian in relation to any proposed guarantor are accurate.
- The trustee certification requirement in relation to parent or group company guarantees has been revised, so that some of the certifications will not look entirely familiar and will therefore need to be checked particularly carefully before being signed off.

The draft levy documents themselves are currently subject to consultation and the final version of the documents should be published imminently. In our experience, there is usually very limited change between the draft and final versions, but it may be different this year given the proposed overhaul of the methodology for calculating insolvency risk.

UPDATE ON *DESMOND* CONTRIBUTION NOTICE LITIGATION: ARE RETAINED PENSIONS DOCUMENTS PRIVILEGED?

It is now over four years since the Pensions Regulator issued warning notices against two former controlling shareholders of the Northern Irish company Desmond & Sons Limited in connection with intended exercise of its contribution notice (CN) jurisdiction. It is over 10 years since the events which gave rise to the notices.

The most recent procedural skirmish in the challenge to the warning notices has concerns the issue of whether documents held by one of the CN targets, a Mr Gordon, were subject to legal professional privilege. This is the status accorded by the courts to documents containing confidential legal advice received by a person (including a company), which normally exempts the documents from compulsory disclosure in the context of litigation.

The Upper Tribunal has held that since the company which had received the legal advice set out in the documents had been dissolved, privilege could no longer be asserted to prevent them from disclosure.

Beyond its importance in the context of the lengthy legal wrangles over the Desmond CNs, this decision resolves an interesting issue in the general field of corporate insolvency. If you are offered documents by a company liquidator, don't assume that if they contain legal advice to the company they will remain subject to legal professional privilege while kept in your garage or loft.

The full appeal against the CNs in the Desmond case is yet to be heard. The procedural wrangles to date would merit a diagram of similar complexity to the April 2015 changes chart. That is perhaps a project which can usefully be postponed for the New Year.

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DECEMBER 2014

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This note is intended to provide general information about some recent and anticipated developments which may be of interest.
It is not intended to be comprehensive nor to provide any specific legal advice and should not be acted or relied upon as doing so. Professional advice appropriate to the specific situation should always be obtained.

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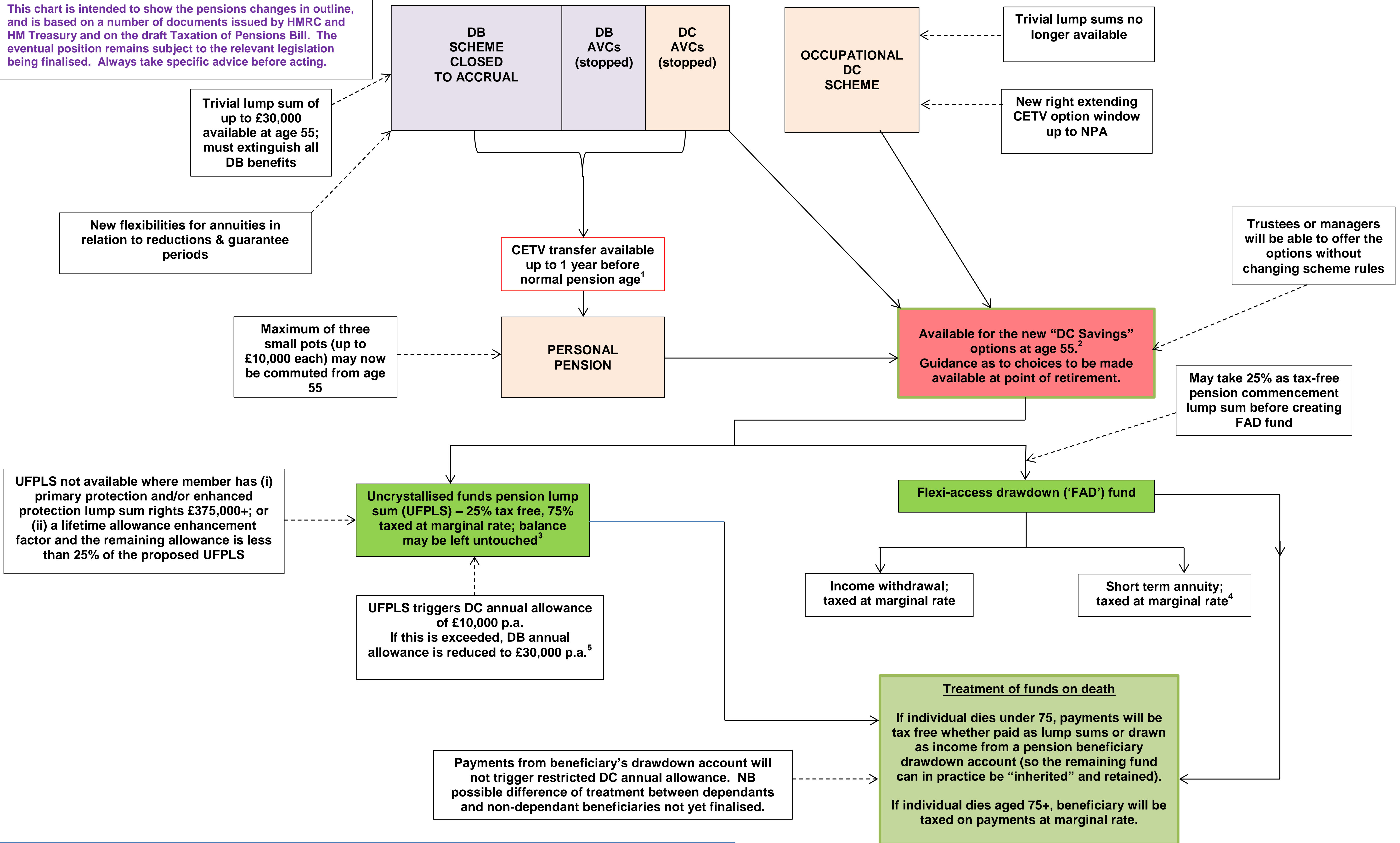
APRIL 2015: THE NEW PENSIONS LANDSCAPE

This chart is intended to show the pensions changes in outline, and is based on a number of documents issued by HMRC and HM Treasury and on the draft Taxation of Pensions Bill. The eventual position remains subject to the relevant legislation being finalised. Always take specific advice before acting.



1 Conditional on professional independent advice being received by the member and paid for by the member (unless transfer is "employer–initiated").
2 Lower age available if ill-health condition satisfied or if member has a lower protected pension age.
3 Must have lifetime allowance in excess of UFPLS if age <75. Must have lifetime allowance at least equal to UFPLS if aged 75+. and (ii) UFPLS not available from same funds once drawdown fund has been created.
4 Any short-term annuity must be purchased from an insurer, and must be for no longer than 5 years.
5 Total annual allowance of £40,000 (plus any carried-forward allowance) retained, but no more than £10,000 will be payable as DC savings in any year without incurring annual allowance charge.

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