Let’s start by confirming that 2015 will be a busy year for all those involved in running pension plans (just in case you are in any doubt). The Government has promised to implement the ‘freedom and choice’ reforms by April 2015 – we suggest that a sprint finish is now required if this is to be achieved. Running alongside this we have other key areas of reform, which will have a significant impact on pension arrangements.

We highlight our top 12 issues for pension plan trustees in the coming year to assist with business planning for 2015.

1. DC Flexibilities – A Race Against Time

The 2014 Budget gave the pensions industry a bit of shock (to say the least!) with its wide reaching reforms regarding access to Defined Contribution pension benefits from April 2015. The main headline-grabbing measure is the option for members to access their entire DC savings by taking one or more lump sums from normal minimum pension age (usually age 55), with the first 25% tax free and the remainder subject to income tax at the member’s marginal rate. Changes also include a new form of drawdown fund (the ‘flexi-access drawdown fund’), a relaxation on some of the restrictions applying to annuities, and a new set of tax avoidance measures (including a DC annual allowance of £10,000 for individuals who flexibly access their pension savings).

The tight timescale for implementation poses a challenge for the Government and for all involved in the pensions industry. During the early part of 2015, trustees of pension plans containing any element of DC (including Additional Voluntary Contribution arrangements) should be assessing, in conjunction with the employer and the administrator, what flexibilities (if any) will be offered to members. The legislation will include a statutory override which will allow trustees to permit members to take advantage of the new flexibilities despite contrary provisions in their pension plan rules.

Trustees should be ready to communicate their decisions to enable members to make choices about accessing their DC pension benefits and get the most from the guidance guarantee service. We now know that the guidance guarantee service will consist of Government online information, telephone guidance provided by the Pensions Advisory Service and face to face meetings offered by the Citizens Advice Bureau. Trustees will need to signpost this guidance to members and consider how their own retirement processes and communications should be updated.

We recommend that trustees, in discussion with the sponsoring employer, make a comprehensive plan to address how the DC flexibilities will be incorporated into their pension plan and communicated to members.

Trustees should exercise caution when using the statutory override. Legal advice is strongly recommended and it is advisable for trustees to consult with the employer on any decisions which may have cost implications or a significant impact on scheme design.

2. DB Transfer Policy – Fit for Purpose?

Trustees of Defined Benefit plans may see an increase in requests from members who are interested in transferring their benefits to a DC plan to take advantage of the new flexibilities from April 2015. This could impact on funding and cashflow positions, and trustees are advised to monitor transfer activity. The Government is to introduce legislation requiring the trustees of a DB plan to ensure that a transferring member has received ‘appropriate independent advice’ before transferring benefits to a non-DB arrangement.

A late amendment to the Pension Schemes Bill indicates that members will have a new statutory right to transfer separate categories of accrued benefits where they have two or more categories of benefits within the same pension plan. The draft provisions are complex, but for example, members of hybrid pension plans with both DB and DC sections would have a right, under the draft legislation, to transfer their DC benefits out of the plan whilst retaining their DB benefits in the plan.

The Government stated an intention to consult on the possibility of allowing full or partial withdrawals directly from DB plans, to avoid the need for members to transfer their DB benefits to a DC plan in order to take advantage of the greater flexibilities to access those benefits. There seems insufficient time now for consultation during the current Parliament, but this issue may reappear during 2015.

Trustees should consider their policies on transfers in anticipation of increased member interest and should monitor developments in legislation. Rule amendments may be required.

Trustees are advised to ensure that member communications clearly explain the implications of transferring out to mitigate the risk of future complaints. Trustees should also obtain appropriate discharges, which confirm the taking of financial advice, particularly for members who do not have a statutory right to transfer where the trustees cannot rely on a statutory discharge.

3. PPF Levy Reductions – A Risky Business

The Pension Protection Fund is currently undergoing a major period of change with the move to Experian’s “more predictive and more transparent basis” for calculating failure scores from 31 October 2014, and consultation on the new levy triennium rules which will apply from April 2015.

There are changes to the way in which the risk-based levy can be reduced for 2015/16 and it is important for trustees and sponsoring employers to be alert to the areas that affect them. Changes include the ability for employers to apply to have certain types of mortgage excluded from the risk assessment, and the recognition of asset backed contributions (incorporating any asset type). There are also amendments to the way in which parent/group company guarantees are valued and certified.
Trustees of pension plans registered as 'last man standing' arrangements on Exchange will be contacted by the Pensions Regulator and will be required to certify by 31 May 2015 that they have taken legal advice on the status of the plan.

Trustees should consider the PPF’s levy determination and supporting documents and decide whether action needs to be taken regarding levy reduction measures. In most cases this action will need to be completed by 31 March 2015.

4. Governance and Charge Capping – Route Planner Needed!

New governance legislation for private sector money purchase occupational plans and hybrid plans with money purchase sections will come into force on 6 April 2015.

In summary, the new regulations will require trustees to design default investment arrangements in the interests of pension plan members and keep them under regular review. They must also ensure that core financial transactions are processed promptly and accurately, assess the value of costs and charges borne by members, and appoint a Chair of trustees who will be responsible for signing off an annual statement setting out how the governance requirements have been met.

Trustees or managers of a ‘qualifying scheme’ that is used to satisfy an employer’s automatic enrolment duties must also check that any default investment fund complies with the charge capping requirements expected to come into force from April 2015. These requirements will apply to private sector and public service pension arrangements and under current proposals it (somewhat strangely) appears that they will also extend to DB qualifying schemes with a money purchase AVC facility. Identification of a default fund will not always be straightforward and trustees will need to make an assessment of the funds offered by their own pension arrangements for this purpose. If a default fund does not meet the charge cap, the trustees are expected to provide an alternative default fund which is compliant and offer transfers to members invested in the original default fund.

Compliance with the governance and charging measures will be monitored and enforced by the Pensions Regulator and some new questions will be added to the Scheme Return.

Some of the finer points of the new governance and charge capping requirements are subject to consultation which closed on 14 November 2014. The final regulations are expected to be laid before Parliament early in 2015.

Trustees should familiarise themselves with the new requirements applying from April 2015. We recommend that, as soon as the legislation is in its final form, trustees put in place an action plan for their pension arrangement to ensure that the governance and charging measures are addressed.

5. Automatic Transfers and Refund Abolition – On the Blocks

The Government has issued a statement confirming its intention that from October 2015 it will no longer be possible to pay a refund of member contributions (known as a short service refund) from an occupational DC pension plan, where a new joiner has more than 30 days of ‘qualifying service’.

Many pension plan rules reflect the current legislation and provide for a refund of member contributions if a member leaves the pension plan before completing two years’ service. Trustees of DC plans should check that their rules will be consistent with the amended legislation that the Government intends to bring into force from October 2015. If not, a rule amendment may be required.

The Government has indicated that it intends to introduce the automatic transfer regime from Autumn 2016. Under the new regime many individuals who change employers will have their DC pension pot automatically transferred to their new employer’s pension plan.

Trustees should monitor progress of this legislation, check whether their pension plan rules will require amendment, prepare for any administrative changes and plan communications to prospective members.

6. War on the Scammers – A United Front

Despite the best efforts of industry regulators, Government bodies, criminal investigators and the pensions industry as a whole, pension scammers continue to plague the general public with promises of releasing cash, exploiting loopholes and investing in lucrative new opportunities. It is a shame that they fail to mention drawbacks such as hefty tax charges, extortionate transfer fees and retirement savings disappearing abroad never to be seen again.

At the end of October the Pensions Ombudsman confirmed that it had received around 140 complaints in relation to pensions scams, of which 90% relate to pension providers not allowing a transfer due to suspicions of fraudulent activity. At the time of publishing our update, we are still waiting for the Pensions Ombudsman’s determinations, which are expected “later this Autumn”.

The pensions industry needs to remain vigilant as fraudsters come up with new and inventive lines of attack – for example, there is concern that some scammers are referring to the Government’s guidance guarantee service to dupe the public into believing that this is what they are offering.

The Pensions Regulator has recently updated its information pack on pension scams and is calling for the help of pension plan trustees to ensure that members receive regular and clear information about the risks.

Trustees should continue to be alert to pension scams, should ensure that their transfer processes remain appropriate, and familiarise themselves with the Pensions Regulator’s updated information pack. Legal advice should be sought where fraud is suspected.

7. Holiday Pay Claims – Up in the Air

Employment practice regarding the calculation of holiday pay is currently subject to challenge via a number of claims that collectively consider the impact of overtime, allowances, commission and other fluctuating emoluments.

The Employment Appeal Tribunal’s decision in Bear Scotland Ltd v Fulton & anor concerned the calculation of holiday pay in accordance with the Working Time Directive, in particular whether it should include an amount in respect of “non-guaranteed” overtime (where an employer is not contractually obliged to offer overtime but a worker is contractually obliged to perform it if requested). The
Employment Appeal Tribunal concluded that the “non-guaranteed” overtime should have been taken into account when calculating holiday pay for the purposes of the four weeks’ holiday entitlement that derives from the Working Time Directive; but the scope for workers to recover back payments of holiday pay by unlawful deduction from wages claims is limited.

Employers will be monitoring the implications of tribunal and court judgments affecting holiday pay and assessing the effect on their own payroll practices. This is a rapidly evolving area of law and although its effects will be felt in the employment sphere in the first instance, there are likely to be pensions implications, particularly if pension plan contributions and/or benefits are calculated by reference to a definition of ‘pensionable pay’ that includes overtime, commission and/or other fluctuating emoluments.

Trustees should liaise with employers regarding the impact of the holiday pay rulings on their businesses and any changes to remuneration policies that may have pensions implications.

8. Abolition of DB Contracting-out – On the Horizon

April 2016 may seem like a long way off right now, but the abolition of contracting-out on the reference scheme test basis is fast approaching. Regulations will allow employers to amend pension plan rules without trustee consent to offset the rise in employer national insurance contributions by increasing member contributions and/or reducing future benefits. The employer will need to appoint an actuary to certify that the amendment purely reflects the additional cost to the employer. Trustees have a vested interest in the employer’s plans and early dialogue with the employer is recommended. Trustees should also ensure that a full audit trail is maintained of the amendment process and that any change is communicated to advisers and administrators as well as pension plan members.

Trustees of DB contracted-out pension plans should also consider signing up to the ‘Scheme Reconciliation Service’ which allows Guaranteed Minimum Pension data to be reconciled against HM Revenue & Customs’ records in advance of the ending of contracting-out. We recommend that trustees of pension plans that are contracted-out maintain a dialogue with the sponsoring employer regarding its intentions towards amending the pension plan from April 2016. Trustees should be clear on their own responsibilities in implementing any changes that the employer makes and should seek their own legal advice as necessary.

Trustees should speak to their pension plan administrators regarding the Scheme Reconciliation Service, if this is not already progressing.

9. Same Sex Marriages – Will the Government Say “I do” to Pensions Equality?

The Marriage (Same Sex Couples) Act 2013 came into force on 13 March 2014, allowing same sex couples to marry.

Under the new legislation occupational pension plans must provide, as a minimum, the same survivors’ benefits to same sex spouses as to civil partners. This means that the period of a member’s service on which a same sex surviving spouse’s benefit is based can be restricted to service accrued from 5 December 2005 (other than for contracted-out benefits).

Some pension plans provide this minimum level of benefit, whilst others have chosen to provide equal benefits for same sex spouses, opposite sex spouses and civil partners. We recommended in a previous communication that pension plan documents should be amended soon after 13 March 2014 to clarify the intentions of the employer and trustees.

The Government undertook to publish a review into the differences in survivor benefits in occupational pension plans for opposite and same sex spouses, civil partners, widows and widowers by 1 July 2014. In this review, the Government concluded that it would need to think “very carefully” about whether the law should be changed to require equal benefits to be provided to same sex and opposite sex spouses, or whether the difference in treatment can continue. Hopefully, we will get some definitive answers in 2015.

Separately, differences in survivors’ benefits from pension plans for same sex couples could be subject to legal challenge. We await a judgment from the Court of Appeal on this issue in 2015.

Trustees should ensure that the pension plan rules reflect the intended level of benefits to be provided to same sex spouses. Where a pension plan provides the statutory minimum level of benefits for same sex spouses and civil partners, trustees should continue to monitor developments.

10. Shared Parental Leave – More Complicated than Child’s Play

A new form of family leave known as ‘Shared Parental Leave’ will be available for parents whose child is due to be born or is adopted on or after 5 April 2015. This new form of leave is intended to offer parents greater flexibility in sharing childcare responsibilities for children under one, or in the year following adoption, and parents will be able to take up to 52 weeks of leave between them. Many pension plan rules will not accommodate the intended level of benefits for members on Shared Parental Leave and may need updating.

Trustees should review pension plan rules and employer family leave policies to ensure that the correct level of pension benefits is provided for members on Shared Parental Leave.

11. Commutation – All Change!

From April 2015, the age at which a member can convert his pension benefits into a lump sum under the trivial commutation rules and ‘small pot’ commutation rules will decrease to normal minimum pension age (usually age 55), or earlier if the member satisfies HMRC’s ‘ill-health condition’. It is proposed that only DB schemes will be able to pay trivial commutation lump sums. In the meantime, trustees who wish to allow members to take advantage of the new higher limits for commuting pensions into lump sums, which have been available since March 2014, should ensure that their pension plan rules allow this.

Trustees should review pension plan rules on trivial commutation and the commutation of small pots to ensure that these reflect the practice that they wish to operate.
12. HMRC Guidance – VAT’s All Folks!

HMRC has issued further guidance on the VAT treatment of costs incurred by pension funds following two decisions of the Court of Justice of the European Union. (See our blog on this subject for more information.)

In summary, DC pension plans will benefit from VAT exempt administration and fund management fees but in some cases service providers may trigger price adjustment clauses in contracts to allow for irrecoverable input tax and/or seek pricing adjustments.

DC pension plan trustees can ask service providers to refund VAT previously charged on fees but can only look back four years in doing so. If the employer has previously recovered the VAT as input tax this would need to be unravelled.

HMRC is also changing its policy on the recovery of VAT input tax for fees incurred in the management of DB pension plans. In order for employers to benefit, HMRC considers that employers will need to be party to the pension plan management contracts. Contracts may need to be restructured to secure the higher VAT recovery, so trustees and service providers may be involved in discussions to facilitate this during 2015. In the meantime, sponsoring employers of DB pension plans can continue with their current practice of VAT recovery under transitional arrangements until 31 December 2015.

Also, from April 2015 …

… trustees of DC plans should note that statutory transfer rights are to be extended to allow individuals to transfer their benefits from a DC arrangement at any age.

… trustees should also note that the 55% tax charge which can, in some circumstances, be levied on a lump sum paid from a pension scheme to a beneficiary on a member’s death will be removed (although in some cases a 45% tax charge will still apply).

And there’s more to come …

… we are still waiting for further guidance from the Government to help trustees with the longstanding issue of how they should deal with GMP equalisation.

… the issue of solvency in occupational DB pension plans has reared its head again following consultation issued by the European Insurance and Occupational Pensions Authority (more debate to follow, no doubt).

…and there is also the small matter of the general election in 2015!