GODDARD PERRY
CONSULTING

Hot topics in Pensions

Autumn 2016

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1. Pensions and VAT – HMRC extends deadline again

Employers and trustees now have an additional 12 months to make changes to their pension scheme VAT recovery arrangements to reflect HMRC policy changes. HMRC is extending the transitional period during which taxpayers may continue to sue the previous VAT treatment if they prefer. The transitional period will now end on 31 December 2017, although HMRC has said it will review this again nearer the time and may consider a further extension.

HMRC changed its policy on pensions VAT recovery following a number of European Court decisions about whether pension fund management services are VAT exempt and, if not , who can recover the costs. HMRC's new policy no longer distinguishes between administration and investment management costs – VAT can in theory be reclaimed on both, provided the employer contracts and pays for the services. But HMRC briefings on this had raised a number of complications, in particular with regard to an employer's ability to make corporation tax savings. HMRC has now revealed it is taking longer than expected to reconcile the European Court decisions with pensions and financial service regulations, accounting rules and emerging case law. The guidance that HMRC was intending to publish on possible options for recovery has been put on hold whilst it fully considers the wider implications.

For now, VAT can be recovered on fund management costs in line with HMRC guidance issued so far – although HMRC warns that adopting alternative structures could have wider implications, in particular in respect of regulatory requirements and corporation tax deductions. Where employers have already made changes to their structure or contractual arrangements, they may continue with those arrangements (provided employer and trustee agree) or choose to revert back to the previous treatment during the transitional period.

2. General Data Protection Regulation (GDPR)

On 24 May 2016 a new General Data Protection Regulation (GDPR) was adopted by the European Union. It will have direct effect in all European Economic Area (EEA) countries, replacing the Data Protection Act 1998 from 25 May 2018. It will have a significant impact on pensions trustees, and the scale of the changes means that trustees need to start preparing now.

Trustees, or service providers on their behalf, process a great deal of personal data about pension plan members, pensioners and beneficiaries, some of it sensitive. Trustees are "data controllers" of this data, with responsibility for data protection compliance. Some of their service providers are their "data processors". Others, along with product providers, are co-data controllers with the trustees. Although the GDPR builds on the existing data protection legal structure, it extends obligations in a number of key areas. Importantly, penalties for non-compliance will increase by several orders of magnitude. For the most serious breaches, the penalties for trustees are up to ú20 million and, for commercial entities, the higher of ú20 million or 4% of global turnover. If more than one data controller or data processor are responsible for the breach, the Information Commissioner's Office (ICO) can choose to pursue whichever organisation has the deepest pockets. It would then be for that organisation to seek to obtain contributions from the other defaulters. In addition, individuals will have the right to sue data controllers and/or processors, and not for profit consumer organisations can bring a form of "class action" on behalf of groups of individuals.

3. Brexit

There are numerous actions that trustees should consider in light of the Brexit vote. Trustees are legally required to review their statement of investment principles when there is a material change in economic circumstances, and it would be sensible to classify the Brexit vote as a material change. Trustees could ask for details from their investment managers of how they are reacting to Brexit and discuss the adequacy of their approaches with their investment consultant. Trustees should be particularly aware of any "gating" clauses in investment funds which can be activated by fund managers to suspend redemptions; these clauses exist to protect investors but also impact on liquidity.

4. The Regulator's View on Brexit

The Regulator has issued a statement warning trustees against knee jerk reactions to short term market volatility associated with Brexit. The Regulator urges trustees to be alert to matters that may impact upon their pension plans but remain focused on the long term. DB trustees should, in particular, review their employer covenant, speak to the sponsoring employer about the impact on trading, consider the effect of market volatility on the plan's funding position, and assess whether contingency plans are still appropriate. DC trustees should review the suitability of investments made available to members and particularly the default fund.

5. New DC Code and Guidance

The Pensions Regulator's revised code of practice on the governance and administration of DC trust based pension plans came into force on 28 July 2016 accompanied by guidance setting out "best practice". Trustees still face a difficult decision to determine what constitutes a "proportionate" approach to DC governance (including additional voluntary contribution arrangements). Particular challenges arise in the context of establishing security of assets and whether the pension plan offers "value for money". We recommend that trustees consider the new scheme assessment template and assess the need for further action, concentrating first on areas presenting the greatest risk.

6. Growing Deficits

Total deficits in defined benefit (DB) pensions are reported to have reached £1 trillion. This is in part due to the reaction of the Bank of England to the Brexit vote. Whilst reducing interest rates in August, the Bank also announced further quantitative easing by way of additional monetary stimulus. This will involve the purchase of £60 billion of UK government bonds, which has already begun and is driving down gilt yields. The unintended victims of this policy are DB pension plans whose liabilities are measured by reference to gilt yields. The result is higher liabilities and increased pension plan deficits.

7. 21st Century Trusteeship

The Regulator's discussion paper on 21st Century Trusteeship asks how to raise standards of governance and administration in occupational pensions. This could be a catalyst for change in the constitution of future trustee boards. The discussion points include: whether trustees should be required to have qualifications, whether the chair of trustees should meet minimum standards, and whether new trustees should be required to pass all relevant models in the trustee toolkit within six months of appointment. The Regulator is also exploring solutions for pension plans where trustees are unwilling or unable to deliver good governance and good member outcomes.

8. Consultation

Amongst the many government consultations in progress, trustees should watch out for the outcome of the British Steel consultation, in which a legislative change to pensions inflation measures was considered, the consultation on capping early exit charges for pension plans providing money purchase and cash balance benefits; and the secondary market for annuities consultations, which potentially affect any pension plan with annuities. We also await the outcome of the UK Statistics Authority's consultation on inflation measures.

Where can I get further information?

Please contact your Goddard Perry consultant if you would like to discuss the issues raised by this update in more detail. Alternatively contact us via the following:

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