

This is a round-up of topical issues in June 2010

Restrictions on tax relief to be revised

The new Coalition Government announced in the Emergency Budget on 22 June 2010 (see [our summary](#)) that it intends to repeal the restrictions on tax relief for high earners that were legislated for by the previous government in the Finance Act 2010, which it believes could have unwelcome consequences for pension saving, bring significant complexity to the tax system and damage UK business and competitiveness. (The new Finance Bill enables the relevant provisions of the Finance Act 2010 to be repealed, but only before the end of 2010.)

However, the Government is committed to protecting the public finances and introducing reforms that raise no less revenue and has decided to retain the current anti-forestalling arrangements.

The Government believes its objectives might be met better by an alternative approach involving reform of existing allowances, principally by reducing the annual allowance for pension saving.

Provisional analysis suggests the annual allowance would have to be reduced from its current level of £255,000 to somewhere in the range £30,000 to £45,000. In DB schemes, this could catch employees at (say) middle-manager level who are given a promotional pay rise, particularly if they have long service.

Before making any firm decisions, the Government wishes to consult with the pensions industry to determine the best design for the new regime.

As widely feared, the Emergency Budget also confirmed that Employer Funded Retirement Benefit Schemes (EFRBSs) fall within the scope of the anti-avoidance measures that were announced in March's Budget. These measures tackle the use of trusts and other vehicles to reward employees in ways that avoid, defer or delay the payment of income tax and National Insurance Contributions by employees and directors or to avoid restrictions on pensions tax relief.

Comment: We are delighted the Government intends to scrap the idea of restricting the rate at which high earners obtain tax relief on their (and their employer's) pension contributions; the system that was due to come into force in April 2011 was absurdly complicated and broke the concept of not being taxed on the same income twice and would not have provided high earners (particularly those with incomes in excess of £180,000 pa) with any incentive to use pension schemes as a vehicle for saving for their retirement. Even a much reduced annual allowance would encourage all tax-paying earners to make at least some pension provision and keep pension schemes in favour in company boardrooms, but will mean many more employees and employers will be affected.

ACTION: Employers should start gearing up for the administrative implications and review whether they should be making changes to their pension provision and/or communication materials for higher earners and/or long-serving employees.

Regulator stresses importance of strength of employer covenant

The Pensions Regulator issued a statement for trustees about "[Understanding employer support for DB schemes](#)" on 9 June 2010 and followed this up by publishing "[Guidance on monitoring employer support: covenant contingent assets and other security](#)" for consultation until 7 September 2010, as well as revised guidance on internal controls (see below), on 15 June.

The statement stresses the importance of the strength of the covenant afforded by their scheme's sponsoring employer(s) whilst the draft guidance explains:

- the importance of measuring the employer's covenant
- how to understand a group's legal structure and an employer's legal obligations
- what to consider when assessing the employer's financial position
- what to consider when valuing alternative forms of security other than cash payments to the scheme

- when to appoint external covenant assessors and the process to follow in doing so and
- the importance of regular monitoring of covenant, and actions to take based on this.

In particular, the Regulator encourages trustees to establish protocols with the employer so that an agreed set of actions can be taken quickly if and when the strength of the employer's covenant falls below a certain point.

The Regulator added specific guidance for multi-employer schemes by publishing "[Defined benefit multi-employer schemes and employer departures: guidance for trustees](#)" on 1 July 2010 for consultation until 23 September 2010 (see "Employer debt regulations" below).

ACTION: Trustees should familiarise themselves with the guidance and enter into discussions with their scheme's sponsoring employer(s).

Internal controls guidance revised

As part of its focus on improving scheme governance, the Regulator published [revised internal controls guidance](#) on 15 June 2010.

The revised guidance has been especially constructed to assist trustees of smaller schemes by making the guidance more practical and targeted, recognising that they have limited resources at their disposal.

Not being exhaustive, the guidance covers seven key risks:

- a lack of knowledge and understanding
- conflicts of interest
- ineffective relations with advisers
- poor record-keeping
- deterioration in the employer's covenant
- investment risk and
- ineffective retirement processes.

continued overleaf ...



The guidance is designed to help trustees to establish and operate internal controls adequate for the purpose of securing that the scheme is administered and managed in accordance with:

- the scheme rules
- the requirements of the law and
- the standard as expressed in the code.

The guidance reminds trustees that a failure to comply with the legal obligation to establish and operate adequate internal controls is a breach of law and could result in regulatory intervention.

ACTION: Trustees should ensure they have established appropriate internal controls for their scheme and review these and the associated risks regularly.

Deadlines set for improvements in record-keeping

As a result of a disappointing voluntary response to the [“Record-keeping: good practice in measuring member data”](#) guidance it issued in January 2009, the Pensions Regulator published [record-keeping guidance](#) on 2 June 2010.

The guidance sets targets for the completeness and accuracy of various aspects of membership data for both (DB and DC) trust-based and contract-based schemes to be achieved by December 2012.

The targets set for the existence and accuracy of “common data” (ie data that is core to all types of scheme) are:

- 100% for new data created after June 2010
- 95% for legacy data (created before June 2010) –in recognition that many schemes will have greater difficulties with older data and may inherit problems.

Trustees are expected to set scheme-specific targets for what the Regulator calls [“conditional data”](#) (which depends on scheme type, structure and scheme design) and “numerical data” (statistics relating to a scheme’s membership). Trustees are also expected to obtain regular reports from their administrators on the completeness and accuracy of the membership records held and put action plans in place where data falls short of the expected standard.

ACTION: Trustees and/or employers should discuss the quality of their scheme’s data with their administrator or providers and agree plans for making corrective actions where necessary.

Regulator turns up heat on “transfer incentives”

In a statement for trustees issued on 9 June 2010 about [“Understanding employer support for DB schemes”](#), the Pensions Regulator said he would be issuing revised guidance on transfer incentives and other situations in which members are asked to consider substituting or converting their benefits.

The [revised guidance](#) was subsequently published on 13 July – details to follow next month.

ACTION: Trustees should familiarise themselves with the revised guidance. Employers should carefully consider whether the potential benefits to them of trying to incentivise members either to transfer out or convert the form of their pension benefits outweigh the cost of ensuring such an exercise complies with the new guidance.



Regulator issues its first Contribution Notice

The Pensions Regulator announced on 29 June 2010 that it had issued its first Contribution Notice. The recipient was Michel Van De Wiele N.V. (VDW), the Belgian parent of Bonas UK Limited, a textile machinery business and the principal employer of the Bonas Group Pension Scheme.

In a nutshell, the Regulator accused VDW of putting Bonas UK Limited through a pre-pack administration in 2006, paying off all creditors other than the pension scheme and buying back the business free of the pension liabilities, which have been dumped onto the Pension Protection Fund (PPF).

It did all this without consulting the trustees or seeking clearance from the Regulator and, seemingly, fully aware that this contravened the anti-avoidance provisions of the Pensions Act 2004.

The Contribution Notice was for the sum of £5.089m, based on an estimate of the Scheme's funding deficit at the time and considerably less than the buyout deficit.

Comment: Given the Regulator's risk-based approach (which suggests an emphasis on larger schemes that have larger numbers of members and pose more of a threat to the PPF) and the time and effort required to put a case to the Determinations Panel, many in the pensions industry were expecting the first Contribution Notice to be issued in a higher profile case.

The lesson from all this is that there is no room for complacency.

ACTION: Even smaller employers should guard against feeling complacent about the risk of the Regulator coming after them if they breach the anti-avoidance legislation.

Government to consult on phasing out of default retirement age

The Government announced in the Emergency Budget on 22 June 2010 (see [our summary](#)) that it will consult shortly on how quickly to phase out the default retirement age (currently 65) from April 2011.

ACTION: Employers should start to prepare for the removal of the default retirement age.

Automatic enrolment to be reviewed

On 24 June 2010 the DWP announced details of a [review](#) to consider whether the current approach to automatic enrolment and NEST strikes the right balance between cost and benefits to individuals, employers and for the tax-payer, particularly in the light of current economic conditions. It will be conducted by an independent team and is to be concluded by 30 September 2010.

ACTION: Despite the uncertainties created by the new Government's review, employers should start thinking about the impact the introduction of NEST and automatic enrolment will have on them and the design of their pension arrangements.

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