CLIFFORD CHANCE

Briefing note

August 2016

UK: Pensions Update: August 2016

1. Select Committee launches new inquiry into DB pension scheme regulation

Following its investigation into the collapse of BHS, the Work and Pensions Select Committee has launched a new inquiry which invites written submissions on defined benefit (**DB**) pension scheme regulation more generally.

The inquiry will focus on the following:

- The Pensions Regulator's regulation of DB schemes; which will include looking at the adequacy of the Regulator's powers, whether a greater emphasis on supervision and pro-active regulation would be appropriate and whether the pre-clearance system is adequate.
- The Pension Protection Fund (**PPF**); which will include looking at the sustainability of the PPF and the fairness of the PPF levy system.
- The role and powers of pension scheme trustees.
- Relationships between the Pensions Regulator, PPF, trustees and sponsoring employers.
- The balance between meeting pension obligations and ensuring the ongoing viability of sponsoring employers.

The deadline for providing written submissions is 23 September 2016.

At the same time, the Chief Executive of the Pensions Regulator has been reported as saying that a corporate pensions failure of the same scale as BHS could happen again if the Regulator is not given greater powers to block deals involving companies with stressed pension schemes.

Specifically, Ms Titcomb is reported to have said that "*another BHS-type sale could happen because of clearance being voluntary*" and has indicated that a new power to make clearance compulsory in certain circumstances would be helpful (whilst stressing that such a requirement should only apply in a limited set of circumstances and that any such power has to be proportionate).

2. Legal action launched by Lloyds Bank trade union could provide clarity on GMP equalisation

It has been recently reported that a Lloyds Bank trade union is launching legal action on behalf of female members who receive increases at a lower rate than male members due to the pension scheme's failure to equalise Guaranteed Minimum Pensions (**GMPs**). Specifically, the trade union appears to be launching a class action claim to present to the Employment Tribunal on behalf of affected members.

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What's the issue?

As those in the pensions industry will be well aware, the uncertainty around if, when and how GMPs should be equalised has been ongoing for some time now:

- In 2010, the Government issued a statement confirming its view that following the European case of ***Barber***[1] (which held that the principle of equal pay for work of equal value applies equally to pensions as a form of deferred pay) schemes should equalise for the effects of GMPs.
- In 2012, the Government consulted on draft regulations and published guidance detailing a possible method for equalising GMPs. However, this was not progressed.
- HMRC confirmed in July 2014 that work was ongoing with industry representatives to develop proposals to meet the Government's objectives concerning GMP equalisation.
- In July 2015, a Pensions Ombudsman determination[2] gave some comfort to schemes which had not yet equalised GMPs; with the Ombudsman taking the view that failure to equalise GMPs was reasonable and the scheme in question could continue to defer taking action to equalise whilst this issue remains generally unresolved.
- In its response to the consultation on the ***2015 contracting-out regulations***[3] (also published in July 2015), the Government said that GMP equalisation issues "are being explored separately" but did not give any further clues about the timescale involved.

For now, therefore, there is still no definitive legislation or guidance on the position.

What's the impact of the Lloyds Bank case?

In the absence of legislation, guidance from the Government or a court ruling, the vast majority of ongoing schemes has not yet addressed the issue of GMP equalisation and many schemes are instead taking a "wait and see" approach.

It is possible this latest legal action could result in some clarity as to what has to be done regarding GMP equalisation, although it is difficult to see what an Employment Tribunal could say that is different from the Pensions Ombudsman's most recent view on this, in the absence of any further legislation or guidance from the Government.

In any event, even if some clarity is forthcoming, this is unlikely to be for some time yet (the legal proceedings appear to be at a very early stage) and for now, therefore, the existing position remains.

Any progress on the GMP equalisation issue will also need to be viewed in light of the UK's exit from the EU following the UK's 'Brexit' vote in June (given that the proposed requirement to equalise GMPs originally derived from EU law).

3. Court of Appeal orders reference to CJEU on level of PPF compensation

Judgment in the Court of Appeal case of ***Hampshire v PPF***[4] was recently handed down.

This case involved a complaint by a scheme member against the PPF concerning his level of PPF compensation. His early retirement pension was reduced by c.67% on entry to the PPF (due to the combined effect of the PPF compensation cap and the non-indexation of pre-6 April 1997 benefits). The member argued that the statutory cap on PPF compensation levels was incompatible with Article 8 of Directive 2008/94/EC.

Article 8 requires member states to take the "necessary measures" to protect the interests of employees and former employees in respect of rights to immediate or prospective entitlement to old-age benefits (including survivors' benefits) under company pension schemes outside the social security system. In the UK, Article 8 was implemented into national law by establishing the PPF (and the Financial Assistance Scheme).

The member argued that the decisions of the Court of Justice of the European Union (**CJEU**) in two previous cases meant that Article 8 should be interpreted as meaning that UK legislation must ensure every individual member of every scheme receives a minimum of 50% of their benefits in the event of employer insolvency. The PPF argued that Article 8 did not mandate this – it is instead a "system obligation" which does not create obligations owed to individual claimants.

The Court of Appeal concluded the proper meaning of Article 8 was not free from doubt and has therefore referred the matter to the CJEU, in addition to the question of whether Article 8 has direct effect on the PPF.

It will be interesting to see what the CJEU determines (and the extent to which its decision will carry any authority in the UK depending on the timing and progress of the UK's exit from the EU). If the CJEU finds in favour of the member, it could mean changes to the PPF compensation rules.

Note that in this case, the member had a lengthy period of pensionable service (c.27 years) and he had lobbied the Government to make changes to the legislation in respect of long-service workers who suffer significant reductions due to the compensation cap. There are currently provisions in the Pensions Act 2014 which would increase the cap for members with more than 20 years' pensionable service, but these are not yet in force and no concrete timeframe has been given for when this will happen. (Also, they generally do not provide for backdating of increased payments for periods before the cap comes into force).

4. European Commission adopts new EU-US "Privacy Shield"

Background

The decision in October of last year to rule the US "safe harbor" regime invalid with immediate effect means that this can no longer be relied on for transfers of personal data from the EU to the US.

EU data protection laws prohibit transfers of personal data to countries outside the EEA which do not ensure "adequate protection" for the data. The "safe harbor" regime had been a key tool used by businesses to ensure adequate protection. (Please see our December 2015 edition of UK: Pensions Update for more details).

Following the decision in October, representatives of the European Commission and the US Department of Commerce have been negotiating to reach a new agreement which would adequately address concerns in relation to the protection of data transferred from the EU to the US.

This has now been agreed and on 12 July 2016, the European Commission adopted the EU-US "Privacy Shield".

How does the new Privacy Shield work?

The US will be regarded as providing an adequate level of protection for personal data transferred to companies that comply with the requirements of the Privacy Shield.

The Privacy Shield consists of Privacy Principles that companies must abide by and commitments by the US government on how the arrangement will be enforced.

Like the former safe harbor framework, the Privacy Shield is based on self-certification. As part of this certification, companies in the US must commit to the Privacy Principles. Compliance with the Privacy Principles entails, amongst other things, that US companies will need to comply with information and purpose limitation requirements, take security measures and grant individuals access rights to their data.

US companies can certify compliance with the Privacy Principles with the US Department of Commerce from 1 August 2016.

What should schemes be thinking about?

The new Privacy Shield will be relevant to anyone who was previously relying on the safe harbor regime in making data transfers to the US. In a pensions context this could cover both:

- schemes / employers based in the EU which transfer data to the US (e.g. schemes which exchange member data with a US parent company, schemes which transfer member data to a US scheme on a cross-border transfer, or where the administration of the scheme is managed from a US-based company); and
- schemes based in the EU which contract with third-party service providers / administrators who hold scheme data in the US.

Those who may be affected may wish to consider signing up to the Privacy Shield as an alternative to whatever form of "adequate protection" they currently have in place (which is likely to be use of the EU Model Contracts as a mechanism for justifying the transfer of personal data to the US). The first step for schemes where a service provider holds scheme data in the US is likely to be to consider discussing with that service provider whether they plan to self-certify to the Privacy Shield.

For more information about the new regime, please see our briefing paper of July 2016 entitled "EU-US Privacy Shield in force".

5. New DC Code of Practice comes into force

The revised DC Code of Practice has now been finalised and came into force at the end of July. It has been re-titled: "*Code of Practice 13: Governance and administration of occupational trust-based schemes providing money purchase benefits*".

At the same time, finalised versions of the 'how to' guides (which are designed to supplement the Code) were also published, together with the Pensions Regulator's response to both consultations (one on the Code and one on the guides).

The substance of the guides, and in particular, the Code, is largely unchanged from the versions published for consultation. However, there are some key differences worth knowing about. In particular:

- **Time-frame for investing contributions**: the draft Code included a statement that the Regulator expects trustees, in all cases, to ensure contributions are invested within a maximum of 3 working days following receipt. This has been amended in the final version to reflect concerns that a maximum 3 day period could be detrimental to members where this does not fit with current dealing patterns. The final Code maintains the 3 working day principle, but provides that where the dealing cycle is less frequent than daily, the Regulator instead expects contributions to be invested on the next available dealing date (but within a maximum of 5 working days) .
- **Security of assets and Financial Services Compensation Scheme (FSCS) protection**: the consultation response acknowledges that a number of respondents considered the requirements in the draft Code around security of assets too onerous (the Code requires trustees to assess the extent to which, and in what circumstances, any loss of scheme assets might be covered by a compensation scheme such as the FSCS and that trustees should then communicate their overall conclusion about the security of assets to members and employers). This concern is not directly addressed in the consultation response; but is considered in more detail in the accompanying guide 4 (on investment governance).
- **Value for money and value for members**: the draft Code switched between talking about "value for money" and "value for members"; something which was picked up during the consultation. In its response, the Regulator says it takes the view that there is no practical difference between the two – they both equate to value for money for members and are not limited to only the investment return the member achieves. The Code and relevant guide have been updated to be more consistent in their use of terminology on this.
- **Proportionality**: already a common theme of the draft Code and guides, but something which has been emphasised more explicitly in the final versions is the focus on taking a proportionate approach to meeting the relevant standards; particularly where the only money purchase benefits provided by a scheme are Additional Voluntary Contributions (**AVCs**) (although the proportionate approach itself will depend on the significance of the value of the AVCs relative to members' overall benefits in the scheme) or where the scheme is a 'less complex scheme' with a small number of members and which carries out fewer transactions.

6. The Pensions Regulator publishes discussion paper on 21st century trusteeship

At the end of July, the Regulator published a discussion paper that continues the debate around how best to drive up standards of pensions trusteeship.

The paper sets out what the Regulator is doing to educate and support trustees (of both DB and defined contribution (**DC**) schemes) and considers what more could be done to raise standards.

Key points from the discussion paper

- The Regulator's research indicates that diversity is key and that professional trustees can help improve effectiveness. However, the Regulator notes that there are currently no barriers to entry for professional trustees and asks for views on whether there should be a requirement for professional trustees to be qualified or registered by a professional body.
- The Regulator is reviewing the requirements which apply to trustee chairs and asks for views on whether more needs to be done to raise the standards of trustee chairmanship.
- The Regulator's research suggests that not all trustees have the required standard of Trustee Knowledge and Understanding (**TKU**) and asks for views on options to drive up compliance (including whether to make it mandatory for trustees to complete the Trustee toolkit within 6 months).
- The Regulator is considering whether it would be worth implementing a formal continuous professional development (**CPD**) framework to ensure trustees are keeping up with the pace of change.
- The Regulator's focus over the next year will to be to better

support trustees through a more targeted communication and education strategy..

The Regulator is encouraging the pensions industry to respond with their ideas and views. The deadline for submitting responses is 9 September 2016.

The Regulator says it will then review the feedback and continue the dialogue unto the autumn as it develops a "21st century trustee strategy".

7. The DWP and FCA consult on capping early exit charges

The FCA is required to make rules capping "early exit charges" imposed on members of personal pension schemes. (Broadly, charges borne by a member when taking, converting or transferring their pension benefits on or after age 55 but before normal retirement age and which are only imposed/imposed to that extent because they are doing so before normal retirement age).

The FCA has now launched a consultation on the draft rules, which closes this month.

In summary, the paper proposes:

- To cap early exit charges for existing contracts at 1% of the value of the member's policy at the time of exit (although if a provider currently applies charges at less than the 1% rate, they will be prohibited from raising these); and
- To impose a complete ban on early exit charges for new contracts entered into after the new rules come into force.

The FCA is intending to confirm the final rules this autumn, with a view to the rules coming into force on 31 March 2017.

The DWP has at the same time launched its own consultation on an early exit charges cap, with the intention to mirror the FCA's proposed cap for occupational schemes (although its scope at this stage is not exactly clear – in particular, whether will it only apply to members with flexible benefits (and to the extent the member has some non-flexible benefits, whether the cap applies only to the flexible benefits) or whether or not it would apply to all members where the scheme provides flexible benefits in respect of at least some members).

8. Government consults on details of "secondary annuity market"

The Government has launched several consultations on the tax and regulatory aspects of the Government's proposals to launch a "secondary annuity market" next year. The consultations have now closed and responses are currently awaited.

Overview

Last summer, the Government consulted on proposals to extend the DC flexibilities to people who had already retired before 6 April 2015 (and so had little choice except to buy an annuity with their DC pots). In December, it published its response to this consultation; setting out a proposed policy framework for a secondary annuity market.

The proposal is that individuals will be permitted to assign or surrender their annuity in exchange for a lump sum or choose for the proceeds to be transferred to a flexi-access drawdown fund or used for purchasing a flexible annuity (i.e. an annuity where the rate of payments can decrease as well as increase). (Although there will be no obligation on annuity providers to permit assignment of annuity payments in this way).

UK firms operating in the secondary annuity market will need to be FCA authorised and purchasing rights under an annuity will be a regulated activity under the Financial Services and Markets Act 2000.

Although it was originally proposed that annuity providers should be prohibited from buying back their own annuity contracts, the Government has since decided buy-back will be permitted *indirectly* and providers will be permitted to bid for their own annuities through an intermediary/broker. Greater flexibility has been suggested for *low value* annuities and the Government has confirmed that providers should be able to *directly* buy back these. Buy-back (which will also be a regulated activity) could prove helpful for providers in managing their capital requirements as well as providing an opportunity to make administrative savings, particularly regarding smaller annuities.

In terms of consumer protection, the scope of the guidance service, Pension Wise, will be expanded to cover all those who hold annuities. There will also be a financial advice requirement for those with annuities above a certain level (there has been no mention of what this level would be yet) with a requirement for firms to check that this has been obtained prior to sale. The FCA will impose a requirement on firms to recommend that sellers take advice, use Pension Wise and shop around and the FCA is also considering what risk warnings might be appropriate as a second line of defence.

For annuity contracts which include contingent rights for dependants or other beneficiaries, the FCA is considering rules around obtaining consent.

The FCA is also considering the level of charges providers should be able to recover as part of the annuity assignment process.

The intention is for the framework to be in place by next April. HMRC has been consulting on the proposed tax framework; the FCA on the proposed rules and guidance needed to implement the secondary annuity market and HM Treasury on amendments to orders concerning regulated activities and to secondary legislation. These consultations closed in June and responses are currently awaited.

Points of particular interest

- Although originally driven by a desire to extend access to the flexibilities to those with DC-originated benefits, both annuities purchased from DC pots and those purchased from DB benefits will be in scope, but, in either case, only where the annuity is held in the individual's own name (e.g. where a transaction has progressed to buy-out).
- Annuities held by occupational schemes and not in the name of the individual will not be in scope. However, HMRC's consultation on the tax framework recognises there are some individuals receiving payments under annuities "purchased in the name of the scheme" (i.e. still held by the trustees) and that trustees may, if they wish, assign the rights to receive these payments to the individual members. The paper indicates this will continue to be permitted, although the papers are not entirely clear on this – we suspect this is a point which will be drawn out as the consultation progresses.
- It will also be interesting to see what level of interest there is from annuity-holders:
  - The tax implications of cashing in an annuity for a lump sum (rather than, for example, having the proceeds transferred to a drawdown arrangement) are likely to make this option unattractive to members with large annuities as the whole lump sum is to be taxed at the individual's marginal income tax rate.
  - However, there may be some for whom cashing in their annuity would be beneficial, for example, to respond to a change in personal circumstances or to meet a particular financial need.

9. Glitch in contracting-out regulations regarding the trivial commutation of GMPs

There is a glitch in the ***2015 contracting-out regulations***[5] (which came into force on 6 April 2016); which is giving schemes pause for thought regarding the payment of trivial commutation and small lump sums to members with GMPs who are below GMP age.

Whilst unlikely to cause a problem in practice, it is worth being aware of the issue.

Background

A general point raised during the consultations on the abolition of contracting-out was the issue that the provisions of the ***1996 contracting-out regulations***[6] did not sit well alongside the general trivial commutation provisions in the Finance Act 2004. This is because the 1996 regulations measure triviality based on the size of the annual pension, whereas the 2004 Act measures triviality based on the value of the lump sum payable.

This has been the position for some time and was recognised during the consultation process. The Government said it would be considering and consulting on appropriate changes in due course, but there was not time to address this issue in the new 2015 contracting-out regulations.

The new issue

A related, but new issue has arisen due to the drafting of the 2015 contracting-out regulations. The issue arises because the wording of regulation 25 of the 2015 contracting-out regulations, which replaces regulation 60 of the 1996 contracting-out regulations, does not exactly replicate the wording of regulation 60.

Specifically, regulation 25 omits the words "*For the purpose of paragraph (1)(b)*" at the beginning of regulation 25(4)(a)). As a result, it could be argued that when a GMP is being commuted for a lump sum before the member has reached GMP age, the value of the GMP as *revalued* to GMP age must be factored into an assessment of whether the member's benefits falls within the HMRC commutation limits (i.e. is small enough to be trivially commuted) as is the case currently, *but also* should be factored into the calculation of the lump sum itself (resulting in a higher lump sum).

Schemes may need to consider the impact on their own rules.

10. Court of Appeal hands down judgment in case concerning implied contracts and liability for section 75 debt

The Court of Appeal's judgment in the case of ***MF Global***[7] was published at the end of June.

This case considered whether there was an implied contract for the provision of staff from a services company to an operating company (within the same corporate group) and if so, whether that contract included an obligation on the operating company to indemnify the services company for its obligations under section 75 of the Pensions Act 1995.

The High Court's original decision (that there was such an implied contract and its terms did cover a section 75 indemnity) was upheld and the appeal dismissed.

Regarding the practical application of the judgment, this case is fact-specific and the rationale for concluding there was an implied contract was very much based on the Court of Appeal's consideration of the specific circumstances. In particular, it had never been doubted that the operating company would reimburse the services company for all costs and expenses in relation to the seconded staff and this is what had happened in practice.

Vos, LJ commented that it was "*a significant step to infer a contract between well-advised substantial commercial companies within a corporate group*" and that this was the first reported case where a contract has been inferred by this kind of conduct. However, in the end, the established relationship between the two companies and the size of the payments which had been made in the past was only explicable in the particular circumstances on the basis that it had a contractual foundation.

It is therefore important to remember that each case will depend on the specific circumstances and conduct of the parties in determining whether there is an implied contract.

However, of more general application is the courts' interpretation of the wording of the services agreement in place between the services company and holding company (the implied contract between the services company and the operating company held to be on the same terms).

The agreement used the term "*Payroll Costs*" which was defined as follows:

> *"**the aggregate costs in relation to each of the Secondees in the period of any assignment under this [Services Agreement] of all salary, bonus, and contractual and discretionary cash and non-cash benefits including, but not limited to**, medical insurance, **pension contributions**, employee insurance benefits, company cars or car allowance, statutory and contractual leave entitlements, staff restaurant costs, relocation allowances, payments made on termination of employment and any tax and national insurance contributions thereon and any third party and/or employer's liability insurance cover which [MF Services] or the relevant Man Financial operating company may reasonably or lawfully require in respect of the employment and/or use of the Secondees."*
>
> (Emphasis added)

The High Court held that this wording was broad enough to cover a section 75 debt. In particular; just because a section 75 debt was not described in the legislation as a "*contribution*" did not mean that it could not fall within "*pension contributions*". In any event, the focus should not just be on the term "pension contributions" because the definition of "*Payroll Costs*" was wider than this and included the other wording in bold above which naturally included pensions as a form of deferred remuneration. The Court of Appeal agreed.

This case highlights the importance of ensuring that the wording around employment/employee/secondment/payroll costs in a supply of services agreement expressly deals with the issue of who is responsible for contributing to the seconded staff's pension arrangements; both in terms of ongoing contributions (for a DB or DC scheme) and for a DB scheme, deficit recovery contributions and any potential section 75 debt triggered in relation to those seconded staff.

11. Judgment on rescue package looks at considerations for actuary on bulk transfer without consent certificate

The High Court's judgment in ***Pollock v Reed***[8] was recently published; a case which involved a Part 8 application by the trustees of the Halcrow Pension Scheme to seek court declarations on a number of legal issues regarding a proposed restructuring of the scheme and the sponsoring employer's group.

Facts

- The Halcrow scheme had a large deficit. The scheme's sponsoring employer was struggling and insolvency was imminent.
- The proposal was for a transfer of the assets and liabilities to a new scheme which would provide the same benefits, but with deferred revaluation and pension increases reduced to the statutory minimum. The intention was to implement this by way of a bulk transfer without member consent.
- A bulk transfer without consent requires, amongst other things, the scheme actuary to provide a certificate under the ***Preservation Regulations***[9] certifying that, in the actuary's opinion, the transfer credits to be acquired under the new scheme are "*broadly, no less favourable than the rights to be transferred*".
- The key question was whether in reaching this opinion, the actuary should take into account the security of the benefits in each scheme and thus the likelihood the benefits would actually be paid.
- Although the value of the headline benefits in the new scheme would be lower than in the Halcrow scheme, if the transfer did not proceed it was likely the scheme would go into the PPF, in which case only PPF levels of compensation would be available (which would be lower than the value of the headline benefits in the new scheme).

The High Court's decision

- The judge decided that the Preservation Regulations do not provide for the security of benefits as a factor to be taken into account in the certification process and there is no scope for a different construction where the transferring scheme is in winding-up.
- In summary, Asplin, J took the view that the meaning of the Preservation Regulations was clear. No express reference is made to the security of the rights or the transfer credits and had it been intended that this be taken into account, the Preservation Regulations would have said so..

What does this tell us?

- This is not a surprising outcome, particularly in a world where struggling employers with large schemes in deficit are becoming more commonplace and, if given the chance, may wish to follow suit.
- It is interesting to note that one of the options being considered as part of the DWP's ongoing consultation on options for the British Steel Pension Scheme is for new regulations to be introduced to allow a bulk transfer to a new scheme with lower levels of revaluation and indexation *without* requiring member consent. If the judge had reached a different view in this case, new regulations would not be necessary and it would potentially open this route up to many others as a method for reducing benefits without active consent from members.
- Following publication of the judgment, it was announced that the Halcrow scheme has gone out to members (in a deal approved by the Pensions Regulator) to ask them whether they want to move into a new scheme or go into the PPF i.e. the transaction is proceeding on a *with-consent* basis.
- The Pensions Regulator has also published a section 89 report regarding its involvement in the restructuring; in which it comments that it is unusual for the Regulator to get involved in private court proceedings in the way it did in the ***Pollock v Reed*** case, but that it will get involved where it believes the issue is likely to have a "*material industry-wide impact*".

12. Supreme Court orders reference to CJEU as to whether historic UK requirement for transgender individual to be unmarried to qualify for state pension is in breach of EU Directive

Judgment in the Supreme Court case of ***MB***[10] was recently handed down.

This case involved a person who had changed gender from male to female; sought to claim the state pension at age 60 (the relevant state pension age for women at the time) and was refused on the basis that she had not obtained a full gender recognition certificate under the Gender Recognition Act 2004.

At the time, the 2004 Act required a person who has changed gender to annul their marriage in order to obtain such a certificate; which MB refused to do. (N.B. this case pre-dates the Marriage (Same Sex Couples) Act 2013, which enables a certificate to be obtained without annulment, provided the applicant's spouse consents.)

The Supreme Court was asked to decide if the requirements of the 2004 Act were compatible with the provisions of Council Directive 79/7/EEC on the Progressive Implementation of the Principle of Equal Treatment for Men and Women in Matters of Social Security. This is concerned with state benefits, including state pensions, and Article 4 provides that there shall be "*no discrimination whatsoever on ground of sex either directly, or indirectly by reference in particular to marital or family status…*". (N.B. there is an exception which allows member states to exclude from scope the determination of state pension age – which allows the UK to have historically imposed a higher state pension age for men than women).

The Supreme Court was divided on the question and has ordered a reference to the CJEU on the question of whether Council Directive 79/7/EEC prevents a member state from imposing a requirement in national law that in addition to satisfying the physical, social and psychological criteria for recognising a change of gender, a person must also be unmarried in order to qualify for a state pension.

Whilst this case is of limited relevance to private pensions (given the introduction of equal marriage and the requirement to equalise benefits (and normal pension ages) for both genders); it will still be interesting to see where the CJEU comes out on this.

13. VAT recovery on pension scheme management: where are we now?

Background

As those in the pensions industry will be well aware, HMRC published guidance in 2014 and 2015 for DB schemes which makes clear that there is now no basis for differentiating between administration/management costs and investment costs and that HMRC will only accept VAT as being deductible by the employer if the services in question are: (i) provided to the employer; (ii) the employer is a party to the contract for those services; and (iii) the employer has paid for them.

This was taken to mean that tripartite agreements would need to be entered into among the trustees, employer and service provider (meeting stringent requirements) so an employer can benefit from VAT recovery.

Due to difficulties with the tripartite agreement approach, some alternative options have been considered by HMRC: (i) a supply of scheme administration services by the trustees to the employer (essentially a back-to-back supply of services); (ii) bringing the trustee within the employer's VAT group; and (iii) a supply of scheme administration services involving a services / holding company. However, these alternatives are not without issue.

What's the current status?

HMRC confirmed in October 2015 that further guidance would be published in 2015. However, to date, this has still not been forthcoming.

Whilst we understand draft guidance has been shared with select industry bodies for comment, this is yet to be finalised and made public. The "wait and see" period therefore continues as it is likely to make sense to wait until HMRC's further guidance is published before taking action (currently, there is no clear consensus within the industry as to the best way forward).

However, having said this, the end of the transitional period (previously extended to 31 December 2016) is approaching, and in the absence of further guidance from HMRC in the next couple of months, or a further extension of the transitional period, trustees and employers are likely to want to take some action.

Based on the material seen from HMRC so far, the most practical approach may be to put in place a supply of scheme administration services agreement between the scheme trustees and the principal employer. However, this route is itself not problem-free and there are a number of issues which need to be worked through if this is the chosen path.

There have been murmurs throughout the pensions industry that HMRC is considering a further extension of the transitional period, in light, particularly, of the UK's recent vote to leave the EU. It would therefore make sense to wait a little while longer before taking action.

14. Other updates in brief

- ***Walker v Innospec***[11]: the Supreme Court is to hear an appeal in the same sex survivor benefits case of ***Walker v Innospec***, following the Court of Appeal's rejection of Mr Walker's appeal at the end of last year. (Please see our December edition of UK: Pensions Update for more details).
- **Applying for lifetime allowance protection**: HMRC's pension schemes newsletter 80 sets out details of its new online service for members to apply for

lifetime allowance protection. This service replaces the interim paper process for applying for fixed protection 2016 and individual protection 2016 and replaces the online form for applying for individual protection 2014.

- **Consultation on salary sacrifice**: HMRC has launched a consultation on limiting the range of benefits in kind that attract income tax and National Insurance contributions advantages when they are provided as part of salary sacrifice and flexible benefit arrangements. However, employer pension contributions and employer-provided pension are to remain unaffected. The consultation closes on 19 October 2016.
- **Consultation on new LGPS investment regulations closed and awaiting response**: In November, the Government launched a consultation on proposals to introduce a new approach to the investment strategy in the Local Government Pension Scheme (**LGPS**) and published the draft ***Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016***. If passed as currently drafted, the new regulations will specifically name 'derivatives' as a permitted investment for LGPS funds. However, at the same time, the draft regulations may limit LGPS funds' ability to enter into stock lending arrangements (it is not clear whether this is intended). The consultation closed on 19 February 2016, but a response has not yet been published.
- **Ban on corporates having corporate directors:** the ***Small Business, Enterprise and Employment Act 2015*** will impose a ban on corporates acting as directors of UK companies when the relevant provisions come into force. This could cause an issue for pension schemes where the corporate trustee has a corporate director; as is often the case where one of the trustee directors is a professional trustee. In recognition of this issue, the Department for Business and Innovation and Skills has said in the past that an exemption should apply for pension schemes. However, a date for the implementation of the provisions imposing the ban is still to be confirmed and the regulations on the exemptions have not yet been published either.

[1] ***Barber Guardian Royal Exchange Assurance Group [1991] 1 QB 344***.

[2] In the case of ***Kenworthy v Campden R.A. Pension Trust Limited and Trigon Pensions Limited (PO-4579.)***.

[3] ***The Occupational Pension Schemes (Schemes that were Contracted-out) (No. 2) Regulations 2015.***

[4] ***Grenville Holden Hampshire v the Board of the Pension Protection Fund [2016] EWCA Civ 786.***

[5] ***The Occupational Pension Schemes (Schemes that were Contracted-out) (No. 2) Regulations 2015***.

[6] ***The Occupational Pension Schemes (Contracting-out) Regulations 1996***.

[7] ***Heis & others v MF Global UK Services Limited [2016]***.

[8] ***Pollock v Reed (Halcrow Pension Scheme) [2016] 041 PBLR (043).***

[9] Regulation 12 of and Schedule 3 to the ***Occupational Pension Schemes (Preservation of Benefit) Regulations 1991.***

[10] ***MB v Secretary of State for Work and Pensions [2016] UKSC 53***.

[11] ***Walker v Innospec and others [2015] EWCA Civ 1000***.

Contacts

Hywel Robinson
Partner

E: hywel.robinson@cliffordchance.com

Imogen Clark
Partner

E: Imogen.clark@cliffordchance.com

Clare Hoxey
Partner

E: clare.hoxey@cliffordchance.com