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NORTON ROSE FULBRIGHT

Essential pensions news

Updater

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Introduction

Essential pensions news covers the latest pensions developments each month.

HMRC announces postponement of withdrawal of VAT exemption for DB pension fund management services provided by insurers

In a development which will principally affect DB schemes, we reported in our October 2017 update on the publication by HMRC of an unexpected Revenue and Customs Brief 3 which announced that there would be a change to the policy relating to the VAT treatment of services provided by insurers to pension funds without special investment fund (SIF) status. This means that insurers will no longer be able to treat as VAT exempt pension fund management services provided to pension schemes which do not have SIF status – effectively, those provided to DB schemes.

HMRC has now confirmed that the withdrawal of this policy will take effect from *April 1, 2019*, rather than *January 1, 2018*, as previously announced.

See also the item on the High Court judgment in United Biscuits case below, in which it was decided that pension fund management services provided to schemes from companies not authorised to carry out insurance business are not VAT exempt.

View the announcement and updated HMRC brief.

HMRC publishes issue no. 93 of its Pension Schemes Newsletter

On *November 30, 2017*, HMRC published the latest edition of its Pensions Schemes Newsletter. The key contents include

- Autumn Budget 2017
  - Confirmation that the lifetime allowance (LTA) will be increased in line with the Consumer Prices Index for the 12 months to September 2017, meaning the LTA will rise to £1,030,000 from *April 6, 2018*.
  - Confirmation of changes to tax registration for master trusts. From April 2018, HMRC can withdraw existing registration from, or refuse to register, a master trust scheme that does not hold TPR's authorisation, or where one of the sponsors is a dormant company.
- Annual allowance calculator – confirmation that an error relating to the calculation of the carry-forward annual allowance has now been fixed.
- Confirmation that consequential changes in secondary legislation to reflect the reduction in the MPAA from *April 6, 2017*, will be made as soon as possible.

View the Newsletter.

Finance (No.2) Bill 2017 receives Royal Assent

The Finance (No.2) Act 2017 was published on *November 20, 2017*, after receiving Royal Assent on November 16, 2017.

The Act contains two previously announced provisions of relevance to occupational pension schemes

- Section 7: the reduction in the money purchase annual allowance (MPAA) from £10,000 to £4,000.
- Section 3: income tax exemption to cover the first £500 of pensions advice provided to an employee where the advice is paid for by the employer.

Both of these provisions are stated to have effect from the start of the 2017/18 tax year.

Comment

Despite strong representations from the pensions industry against introduction of the MPAA reduction at all and then the proposed back-dating to April 2017, the Government has gone ahead with this unpopular change. Those who had accessed their pensions savings on the understanding that they would have a £10,000 tax free savings limit for the future will be justifiably disappointed.

Financial Guidance and Claims Bill update

The Financial Guidance and Claims Bill 2017/19 had its third reading in the House of Lords on *November 21, 2017*.

The Bill provides for the establishment of a new single financial guidance body (SFGB) to replace the Money Advice Service, the Pensions Advisory Service and Pension Wise. The Government confirmed a number of amendments, including those clarifying the statutory objectives of the SFGB and provisions introducing a debt respite scheme, previously debated in the Lords.

Baroness Altmann raised a question about the ban on pension cold-calling, asking whether the Pensions Regulator or the Financial Conduct Authority, rather than the Information Commissioner, could be responsible for enforcing the ban to ensure that the ban is "as effective as possible". There was no amendment at third reading relating to cold calling, but Baroness Buscombe, Parliamentary Under Secretary of State at the DWP, confirmed that the Government is committed to introducing the required legislation.

The Bill had its first reading (with no debate) in the House of Commons on *November 22, 2017*. A date has not yet been set for the second reading.

Finance Bill 2018 published

The first version of the Finance Bill 2018 was published on *December 1, 2017*, along with explanatory notes. The Bill contains fewer pensions-related provisions than in previous years, reflecting the fact that no major changes were announced in the Autumn Budget 2017.

Included in Schedule 3 of the Bill are provisions to permit HMRC to refuse to register, or to deregister, an occupational pension scheme with a dormant employer, or a master trust that has not been registered with the Pensions Regulator. These reflect previously announced policy decisions.

There is no reference in the Bill to the widening of tax exemptions for employer premiums paid to life assurance and overseas pensions schemes, which was also announced in the Budget 2017. This is expected to be included in the Finance Bill 2018/19 and to come into effect on and after *April 6, 2019*.

The Budget 2017 also included reference to the increase in the lifetime allowance by the Consumer Prices Index (to £1,030,000) for the 2018/19 tax year. This is also not included in the Bill as it was announced at the March 2015 Budget and has been enacted in amendments to the Finance Act 2004 under the Finance Act 2016. The necessary changes are expected to be implemented by statutory instrument, before the start of the next tax year.

The Bill's second reading took place in the House of Commons on *December 11, 2017*.

Regulation of master trusts: consultation on draft secondary legislation

The DWP has published draft regulations to be made under the Pension Schemes Act 2017, setting out further details about the new regime for regulating master trusts in the UK. The consultation runs until *January 12, 2018*.

From *October 1, 2018*, a master trust will prohibited from operating unless it has been authorised by the Pensions Regulator (TPR). An authorised master trust will then be subject to TPR's ongoing supervision, and those failing to meet the standard required will run the risk of being required to wind up and transfer their members to an alternative scheme. In order to obtain authorisation, master trusts will have to meet five criteria, which are

- The arrangement being run by "fit and proper" persons
- Being financially sustainable
- Having scheme funders which meet specific requirements
- Having sufficient systems and processes to run effectively
- Having an adequate continuity strategy.

Among other things, the draft regulations reveal the likely level of the fee that a master trust will be required to pay when applying for authorisation. The DWP anticipates an existing scheme in operation before October 1, 2018 will have to pay up to £67,000, while a new scheme established on or after that date will have to pay up to £24,000. The difference reflects the DWP's judgement that substantially more work will be required for TPR in authorising an existing master trust.

Further details are also given about the regime's scope. The DWP confirms that industry-wide and not-for-profit schemes will have to obtain authorisation, as expected. Schemes that will be exempt from the authorisation requirement will include certain mixed benefit schemes established on the privatisation of state-run utilities. According to the DWP, these schemes are less exposed than others to the risks facing master trusts.

View the consultation paper and draft regulations.

The Occupational Pensions (Revaluation) Order 2017 published

Of interest to schemes providing final salary benefits is the publication of the latest statutory revaluation Order, which comes into force on *January 1, 2018*.

The Order specifies the minimum revaluation percentages that must be applied to deferred pensions for members of occupational pension schemes who reach their scheme's normal pension age (NPA) in 2018. The appropriate revaluation percentage for a member depends on the number of complete years between the date the member left pensionable service and the date on which they reach NPA. Different revaluation provisions govern guaranteed minimum pensions.

Under the statutory limited price indexation formula, the percentage increase for the most recent calendar year must match the increase in the consumer prices index (CPI) for the 12 months to September 30, capped at five per cent or 2.5 per cent according to whether pensionable service was completed before or after *April 6, 2009*.

CPI inflation was three per cent for the 12 months to *September 30, 2017*, and therefore the higher revaluation percentage for early leavers' pensions has been fixed at three per cent and the lower revaluation percentage has been capped at 2.5 per cent for the 2017 calendar year revaluation period. Revaluation percentages for calendar years running back to 1986 are also adjusted by the order to take the most recent year into account.

DWP consults on alternative approach to PPF compensation for members entitled to bridging pensions

Of interest to DB schemes offering bridging pensions is the DWP's recent consultation on technical provisions in the draft Pension Protection Fund (Compensation) (Amendment) Regulations 2018 (the 2018 Amending Regulations). There was a very short consultation period, which closed on *December 3, 2017*.

In our September 2017 update, we reported that the DWP had published a consultation paper on draft legislation to allow the Pension Protection Fund (PPF) to take account of bridging pensions, accompanied by a set of draft amending regulations, the Draft Pension Protection Fund (Compensation) (Amendment) Regulations 2017.

Currently, PPF compensation payments do not take account of anticipated changes to a member's pension entitlement after the date that a pension scheme enters PPF assessment. As a result, members entitled to a higher rate bridging pension at the assessment date have their PPF compensation fixed at that rate for life, whereas if the scheme had not entered assessment, the member's pension would have decreased when the bridging pension ceased to apply under the original scheme rules. This treatment applies to pensioner members in receipt of bridging pensions at the time of assessment and to deferred members where a bridging pension is the default retirement benefit payable under the scheme rules. As a result, such members may be financially better off in the PPF than they would have been under the rules of their scheme (if the scheme had not entered the PPF).

To address this anomaly, the PPF consulted in August 2017 on two options

Smoothing

Under this approach, an actuarial calculation would convert the bridging pension to a flat-rate lifetime-equivalent compensation amount for each affected member (subject to PPF indexation).

Mirroring

Under this approach, the PPF reflect the scheme provisions and pay compensation based on a higher rate until the relevant date specified under the scheme, usually when the member reaches state pension age, when the compensation would be recalculated and paid at a lower rate.

The draft regulations published for consultation in August 2017 were drafted on the basis of the smoothing option, which was the DWP's preferred approach.

The DWP subsequently published a technical consultation which notes that the "vast majority" of respondents to the August 2017 consultation agreed that the Government should legislate to correct the PPF bridging pension anomaly. However, a "significant proportion" of respondents expressed a preference for the mirroring option. The main reason was that the original approach would have led to an immediate drop in income for pensioners, which could result in financial hardship where the bridging element constituted a high proportion of their overall pension.

As a result, the DWP has now decided to address the bridging pension anomaly by "more closely aligning with the approach that schemes would have taken" and this revised approach is set out in the draft 2018 Amending Regulations, which have a proposed implementation date of *February 24, 2018*. They are stated to apply to members of schemes with bridging pensions where the assessment period begins on or after that date.

Comment

The approach set out in the 2018 Amending Regulations is not the DWP's preferred approach. In its August 2017 consultation, the DWP noted that addressing the anomaly by adopting the option under which scheme rules were mirrored "*would represent a step change in the way that the PPF operates and is likely to be significantly more complex for it to administer*".

United Biscuits (Pension Trustees) Ltd and another v HMRC [2017] High Court decides pension fund management services from non-insurers not exempt from VAT

In a judgment handed down in the High Court in *United Biscuits (Pension Trustees) Ltd and another v HMRC [2017]* on November 30, 2017, it was decided that pension fund management services from service providers other than insurers are not exempt from VAT. This is the latest in a series of cases relating to possible exemption from VAT of management and investment services provided to pension schemes.

Facts

The United Biscuits Pension Fund (UBPF) was a DB occupational pension scheme for employees of United Biscuits (UK) Ltd. UB Pension Investment Fund (UBPIF) was a collective investment fund in which the assets of UBPF were invested from 1989 to 2006.

The trustees of UBPF and UBPIF, who were the claimants in the case, received pension fund management services from various investment managers, comprising both companies that were authorised to conduct insurance business in the UK (insurers) and companies that were not so authorised but which provided pension fund management services (non-insurers). All of the contracts between the claimants and the investment managers provided for the payment by the claimants of fees plus VAT on those fees "if applicable". Thus, the claimants paid VAT, in addition to the fees, to the non-insurers.

The claimants considered that the services provided by the non-insurers should, in fact, have been exempt and sought from HMRC recovery of the VAT paid. HMRC disputed the claim on the ground that the supplies by the non-insurers were not exempt from VAT and the claimants brought a claim for recovery of the disputed amounts in the High Court.

Decision

The Court dismissed the claimants' action, holding that the services provided by the non-insurers were not exempt from VAT, as the provision of pension fund management services did not comprise "insurance" for the purposes of the relevant EU VAT law, and therefore the VAT exemption did not apply to the provision of such services (whether by insurers or non-insurers).

The Court rejected the claimants' arguments that management of pension funds attracted VAT exemption on the basis that this was "insurance" within the meaning of "direct insurance" under the relevant Directive.

Comment

There have been several cases in recent years concerning the VAT treatment of various services provided to pension schemes. In *Wheels Common Investment Fund Trustees Ltd and others v HMRC*, the ECJ ruled that a DB scheme would not generally be regarded as a special investment fund (SIF) and thus third-party investment management fees would not attract VAT exemption under EU law. This litigation provided a life-line in *Wheels* in that the First-tier Tribunal allowed an application by the taxpayers to amend the existing grounds of appeal to include arguments (advanced in this case) that the principle of fiscal neutrality required similar supplies to be treated in the same way, irrespective of whether those supplies were made by an insurer or a non-insurer.

The decision in *United Biscuits* has now rejected the notion that because HMRC has incorrectly allowed insurers to exempt pension fund management services supplied by them in the past, such supplies by non-insurers should also attract exemption on the grounds of fiscal neutrality.

HMRC has now reconsidered its practice of treating pension fund management services as insurance, and has now announced that it will be withdrawing its policy of allowing insurers to apply VAT exemption to supplies of pension fund management services made to pension funds without SIF status.

Although the Court stated that the exemption should not be applied to pension fund management services supplied by insurers, it seems unlikely that HMRC will revoke the postponement of the extension of the withdrawal date to *April 1, 2019*, although this is unconfirmed.

In future, it must be correct that fiscal neutrality requires supplies of pension fund management services by insurers and non-insurers to attract the same VAT treatment. Given the decision in *Wheels*, it seems inevitable that this should be taxation rather than exemption. This will no doubt be unwelcome to insurers, but non-insurers are likely to see it as levelling the playing field. As for trustees, they may take some comfort from the fact that they have enjoyed exemption on pension fund management services supplied by insurers for longer than they may have expected.

There is no indication yet whether the decision in *United Biscuits* will be appealed, but given the sums involved such an appeal would be unsurprising.

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