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NORTON ROSE FULBRIGHT

Essential pensions news

Briefing

July 2017

Introduction

Essential Pensions News covers the latest pensions developments each month.

Proposed pensions changes dropped from Queen's Speech

On *June 21, 2017*, the Queen's Speech was delivered at the State Opening of Parliament. There were no references to pensions.

Conservative Party manifesto pension policies, such as the scrapping of the State pension triple lock from 2020 and future State pension age increases, were absent from the Queen's address to Parliament.

However, background documents released following the speech confirm that the proposed Financial Guidance and Claims Bill will "*establish a new statutory body, accountable to Parliament, with responsibility for coordinating the provision of debt advice, money guidance, and pension guidance*" – see further below, in our legislation section. The aim is to provide greater clarity and make it simpler for customers by having a single body responsible for all public financial guidance. The current public financial guidance service is delivered by the Money Advice Service (MAS), The Pensions Advisory Service (TPAS) and Pension Wise, with services overlapping. Consultation was conducted at the end of 2016 and it is thought that a single body will improve efficiency by reducing duplication and will deliver better value for money.

There is also due to be a Summer Finance Bill (see below) to "*include a range of tax measures including those to tackle avoidance*." While there is no specific mention of either the increase in the income tax exemption for employer-provided pension advice to £500, or the reduction in the Money Purchase Annual Allowance to £4,000, these are to be included, having been dropped from the Parliamentary agenda before the General Election.

There was no mention in the Queen's Speech or the background briefing of the possible timing of a response to the Green Paper on Security and Sustainability in DB Pension Schemes and this may well lose out to the many competing interests for Parliamentary time over the coming months.

View the Queen's Speech and associated background briefing.

Pensions Regulator publishes its funding analysis for Tranche 12 schemes

Of interest to all schemes providing defined benefits (DB), is the publication of the Pensions Regulator's (TPR's) latest annual funding analysis, aimed principally at DB schemes undertaking valuations with effective dates in the period September 22, 2016, to September 21, 2017 (Tranche 12), but of relevance for all DB schemes. In our update for May 2017, we reported that TPR had published its annual funding statement, setting out its expectations of trustees with a focus on what it described as "stressed schemes". We also looked at the funding statement in greater detail in our June 2017 briefing.

TPR's funding statement indicated a more prescriptive approach to the valuation process, emphasising the need for trustees to take appropriate advice and promoting schemes' early engagement with TPR where necessary. TPR stated that the majority of DB pension schemes "*remain affordable but many should do more to tackle increased deficits and reduce risk to pensioners*".

The analysis document looks at the expected positions of Tranche 12 DB pension schemes and confirms that

- Most schemes will have seen their funding liabilities increase at a greater rate than their assets since their last valuation in 2014 when markets conditions were "relatively favourable" compared to current market conditions.
- About 50 per cent of schemes are capable of maintaining the same pace of funding and could also increase contributions if required.
- Over a third of schemes have an employer covenant which TPR considers "adequate" to support the scheme, but that is undermined by current contribution and/or risk strategies posing unnecessary longer term risks.
- Where FTSE350 companies paid deficit repair contributions (DRCs), the ratio of dividends to DRCs declined from around ten per cent to around seven per cent. Broadly, this equates to a significant increase in dividends without a corresponding increase in contributions. The Conservative party manifesto included reference to increased powers for TPR to issue punitive fines for employers who have "wilfully left a pension scheme under-resourced" (but it is now unclear whether this will appear in the redrafted Queen's Speech following the election result).

Commenting on the analysis, TPR's Executive Director for Regulatory Policy, Andrew Warwick-Thompson, said:

"*Having made our expectations so clear in this year's [annual funding statement], if we see a situation where we believe a scheme is not being treated fairly, we are likely to intervene. For example, if a company is paying out more in dividends than in deficit reduction contributions, we will expect to see a short recovery plan. And we will expect that recovery plan to be underpinned by an appropriate investment strategy.*"

Comment
It will not come as a surprise that many schemes' funding deficits have increased since their last valuation, given the current widespread political and economic uncertainty. As the current upheaval shows no sign of abating any time soon, it will continue to be difficult to predict the actual results for those schemes which have yet to complete the valuation process.

View TPR's Tranche 12 analysis.

Pensions Regulator publishes 2016/17 annual report and accounts

TPR has published its annual report and accounts for the 2016/17 financial year. Notable points are as follows

- Over the year, TPR's Determinations Panel exercised its powers 42 times, up from 12 in the previous year. This increase is attributed to the exercise of two powers it has not exercised before
  - The power to issue a civil penalty under section 10 of the Pensions Act 1995, which was used 33 times (all in relation to non-completion of the scheme return)
  - The power to require a report to be produced by a skilled person (section 71, Pensions Act 2004). This power was used twice.
- TPR has recovered in excess of £650 million for DB pension schemes, including high profile settlements from both BHS (£363 million) and Coats (£255 million). This takes the total recovered by TPR since 2005 to over £1 billion.
- Over the year, TPR dealt with 47,153 auto-enrolment cases, marking a significant increase from the 7,800 that were handled in 2015/16.
- There was one "serious incident" with regard to data loss, in which an attendee of TPR's Board lost TPR Board papers. While the papers were never recovered, there were no adverse consequences as a result of the data loss. TPR is currently working on the implementation of a more secure, electronic access system to allow protected access to Board and Committee papers.
- TPR acknowledged that it is facing change, especially through the introduction of "tough new powers" to authorise and supervise master trusts, introduced in the Pensions Schemes Act 2017. It is being "quicker and bolder" in the use of its powers, including securing two criminal prosecutions.
- TPR has issued new DB investment guidance.

View the report and accounts.

Comment
The list above merely highlights TPR's principal activities in the past 12 months, showing that it has been a busy year. The foreword to the Report and Accounts highlights the "*seismic shifts in the political landscape and continuing change in the pensions sector*."

In a climate of increased uncertainty, it will be important for TPR to be clear in the way it puts across its messages to the pensions industry, and to continue to evolve to meet future challenges to help achieve the best outcomes for members.

TPR publishes compliance and enforcement bulletins for trustees

On *July 5, 2017*, TPR published two compliance and enforcement bulletins setting out how it has used its powers to tackle non-compliance issues and warning that trustees who fail in their duties can expect to be fined.

TPR's bulletins show how it has used its powers to tackle schemes' non-compliance with legal requirements to complete a scheme return and an annual chair's statement. The aim of the bulletins is to inform the industry of TPR's experience to date and to increase trustees' understanding of these duties.

TPR states that the majority of schemes complied with new legislation obliging them to prepare an annual governance statement, signed by the chair of trustees. During 2016, 85 schemes received a mandatory fine for not preparing a chair's statement. A large proportion of those failing to produce a statement were small schemes with fewer than 100 members.

The second bulletin details the action taken by TPR to achieve compliance with legal requirements to provide TPR with a scheme return.

TPR received 16,963 scheme returns, and after starting enforcement action against trustees received a further 868 returns. A number of trustees failed to comply even after receiving a warning from TPR and fines were subsequently issued to 88 trustees.

Nicola Parish, Executive Director for Frontline Regulation at TPR, said: "*Non-compliance with basic requirements such as completion of a chair's statement and a scheme return may indicate broader governance issues. This is important because ultimately, poor standards of governance can impact the value of members' pension pots. We want all members to be saving in well-run schemes and will take action to help schemes get the basics right.*

Our 21st Century trustee work is focused on raising the standard of trusteeship and our enforcement action is an important part of that ... Our message to [trustees] is that ignorance is no excuse – if you breach your duties, you will face action."

Last year TPR made clear it would act after data showed compliance with basic duties had fallen by 18 per cent. As a result of its focus on scheme return compliance and enforcement efforts, over 97 per cent of schemes are now compliant.

View bulletin on compliance with Chair's statement requirements.

View bulletin on compliance with scheme return requirements.

Auto-enrolment: DWP issues call for evidence on alternative quality requirements for DB schemes and seafarers and offshore workers

The DWP has published a call for evidence in advance of two statutory reviews it is required to conduct into certain aspects of the auto-enrolment legislation. Under previous legislative changes, seafarers and offshore workers became subject to the auto-enrolment requirements if they were "ordinarily working" within the UK, provided they met the other necessary conditions applying to eligible jobholders.

The two reviews concern

- The alternative quality requirements for DB schemes enacted under section 23A of the Pensions Act 2008, including the modified cost-of-accruals test that is available for a transitional period for a formerly contracted-out DB scheme. The DWP is required to review these provisions during 2017.

- The provisions in secondary legislation that extended the scope of the auto-enrolment reforms to seafarers and offshore workers involved in oil or gas extraction. A review of these provisions is required to be conducted by *July 1, 2018*. In the case of offshore workers, the statutory instrument in question will cease to have effect automatically on *July 1, 2020* under a "sunset" provision, and the review must consider whether the instrument is still needed.

The DWP seeks responses to the call for evidence by *August 30, 2017*.

View the call for evidence.

Comment

The DWP reveals in this call for evidence that it is aware of only one hybrid scheme making use of the money purchase minimum requirements test in relation to its DB element. This is not wholly surprising, as few employers are enrolling jobholders in DB schemes or DB sections at all. However, there are also technical difficulties in complying with the conditions of the money purchase minimum requirements test set out in regulation 32L of the Automatic Enrolment Regulations, and a lack of helpful guidance about meeting these conditions in existing DWP or TPR publications. Changes may be needed to the requirements if they are to apply more widely in future.

By contrast, it seems possible a larger number of formerly contracted-out schemes may be making use of the modified cost-of-accruals test and it will be interesting to see whether there are calls to extend the period during which the test is available for these schemes.

FCA publishes new proposals on DB transfer rules

Summary

On *June 21, 2017*, the Financial Conduct Authority (FCA) published its new consultation paper on advice relating to transfers of safeguarded pension benefits. The proposed changes include requiring advice to be provided as a personal recommendation. The aim is to reflect the current environment in which there has been an increased demand from members for transfers from defined benefit (DB) to defined contribution (DC) schemes, so as to take advantage of the pension flexibilities introduced in April 2015.

The consultation period ends on *September 21, 2017*.

Legal background

Under the Pensions Act 2015, if a member of a DB scheme (or their surviving beneficiary) wishes to transfer their accrued benefits under a DB scheme to a DC pension scheme in order to access the pension freedoms, the trustees of the transferring scheme must first "check" that the member or survivor has received "appropriate independent advice" (unless the total value of the member's or survivor's benefits is under £30,000 on the valuation date).

This advice requirement applies to "safeguarded benefits" which are defined in the legislation as any benefits other than money purchase benefits or cash balance benefits. To complement the statutory requirements, guidance about complying with the advice requirement has been published by the Pensions Regulator for trustees of occupational pension schemes.

The FCA's proposals

The proposed changes include requiring transfer advice to be provided as a personal recommendation to the member, with the provision of a comparison to show the value of the benefits being given up. The FCA aims to ensure that the advice takes full account of the individual's circumstances so that transferring members are able to reach decisions that are right for them.

The proposals include

- Replacing the current transfer value analysis requirement (TVA) with a comparison showing the value of the benefits being given up.
- Introducing a rule to require all advice in this area to be provided as a personal recommendation, which fully reflects the client's circumstances and provides a recommended course of action.
- Updating the FCA's current guidance on assessing suitability when giving a personal recommendation to convert or transfer safeguarded benefits, so that advisers focus on whether a transaction is right for a particular individual.
- Introducing guidance on the role of a pension transfer specialist.

Comment

Recent surveys (by Royal London and Old Mutual Wealth, to name but two) have highlighted an increase in over 50 per cent in the volume of transfers out of final salary (DB) schemes over the last year. In acknowledging this trend, the FCA is proposing to update its advice to consumers who have safeguarded benefits. They hope to ensure that those wishing to effect a transfer "receive advice which considers all relevant factors". The FCA recognises that the pensions savings environment has changed significantly in recent years. In strengthening its advice requirements, it aims to ensure that, where members wish to use the pension freedoms to access valuable defined benefits, the financial advice they receive should be bespoke and should highlight all the options open to them.

However, such tailored advice does not come cheap and where an individual has a DB fund which is only slightly in excess of the £30,000 minimum, professional advice fees could make an appreciable hole in the saver's pension fund.

PPF publishes strategic plan for 2017–2020

Of interest to all DB schemes is the publication by the Pension Protection Fund (PPF) of its Strategic Plan 2017-2020. Setting out its vision for the next three years, the plan outlines how the PPF intends to achieve its strategic objectives, which focus on funding, customer service and risk.

The document was prepared for publication in April but this was delayed as a result of purdah rules for public bodies in the run-up to the General Election.

In the Plan, the PPF announces its intention to bring Financial Assistance Scheme (FAS) member services in-house over the next three years, having now completed a project to insource PPF member services in 2015. This follows work with DWP to assess the best approach to FAS administration in the long term.

The Plan sets out the PPF's financial projections for the next three years, including an estimated £32 billion in assets under management by 2020. It also confirms that the PPF has successfully completed the first two phases of its project to insource part of its investment management, and plans to insource sections of its private and public market credit portfolio over the next three years. The PPF will also examine the rationale for insourcing passive currency hedging.

The PPF will continue to evolve its insolvency risk model, which is used to calculate the pension protection levy, to ensure the levy is as reflective of risk as possible. It will implement changes for the third levy triennium and will consult on the rules for the fourth levy triennium within the next three years.

View the PPF's Strategic Plan.

FCA publishes final report in asset management market study

On *June 28, 2017*, the FCA published its final report on its asset management market study (MS15/2.3).

The focus of the market study is on how competition between asset managers is working for both retail and institutional investors that use funds and segregated mandates managed in the UK and/or provided and marketed to UK investors. The final report confirms the FCA's interim findings, published in November 2016, that price competition is weak in a number of areas of the industry. Despite a large number of firms operating in the market, there is evidence of sustained, high profits over a number of years. The FCA also found that investors are not always clear what the objectives of funds are, and fund performance is not always reported against an appropriate benchmark. Finally, the FCA found concerns about the way the investment consultant market operates, for example, in dealing with conflicts of interest.

The FCA is proposing a significant package of remedies aiming to improve competition in this market. Implementation of the remedies will take place in a number of stages, with some requiring consultation. The proposed remedies include a strengthened duty on asset managers to act in the best interests of investors, introducing an all-in fee so that investors in funds can easily see what is being taken from the fund, a number of measures aimed at helping retail investors identify which fund is right for them, clarifying and strengthening the use of benchmarks and providing tools for investors to identify persistent underperformance.

To help improve the effectiveness of intermediaries, the FCA will launch a market study into investment platforms and recommends that HM Treasury considers bringing investment consultants into the FCA's regulatory ambit.

With its interim report, the FCA consulted on whether to make a market investigation reference to the Competition and Markets Authority (CMA) on the investment consultancy market. The FCA considered that competition was being adversely affected in the institutional advice market by a weak demand side, persistent levels of concentration, high barriers to entry and vertically integrated business models. It has now provisionally decided to reject suggestions offered by the three largest investment consultants in lieu of a market investigation reference to the CMA.

The FCA invites comments on that decision by *July 26, 2017*, and will announce its decision in September 2017.

View the final report.

State pension – DWP announces plans for accelerated increase in State Pension Age to 68

The DWP has announced its intention to bring forward the planned increase in State Pension Age (SPA) from 67 to 68 following the first review of SPA to be conducted under section 27 of the Pensions Act 2014.

In line with the recommendations made by John Cridland CBE in March 2017, the DWP plans to increase state pension age from 67 to 68 over the period 2037 to 2039, seven years earlier than set out in existing legislation. This change will affect everyone born between *April 6, 1970*, and *April 5, 1978*.

The DWP says the move will "*maintain fairness between generations in line with continuing increases in life expectancy*". However, before legislating for the change, the DWP will await the outcome of its next section 27 review, which is due to be conducted in six years' time, and which will have the benefit of more up-to-date life expectancy projections. In the interim, the DWP will analyse the impact of SPA changes already in train, such as equalisation at age 65 and the increase to age 66.

HMRC publishes pension schemes newsletter no. 88

On *June 30, 2017*, HMRC published the latest edition of its pension schemes newsletter. The contents include

- Change of address – the Pension Scheme Services address is now HMRC, BX9 1GH.

- Relief at source for Scottish Income Tax – draft technical information on the look up service for pension scheme administrators is now available. This will enable administrators to establish whether or not a member is a Scottish resident for tax purposes.

- Annual return of individual information – a reminder of the July 5, 2017 deadline. Subsequent interim tax repayments will be held pending receipt by HMRC of the outstanding information.

- Pension scheme transfers – requests for confirmation of a receiving schemes' registration status should be sent only once, by post or email but not both. HMRC will only confirm registration status where the receiving scheme is both registered with HMRC (and not subject to a deregistration notice) and the information HMRC holds does not indicate there is significant risk of the scheme being used for pension liberation. However, confirmation of registration does not amount to HMRC approval of a transfer request.

- Updates of various forms – including those relating to Scottish Income Tax and transfers to QROPS.

- Lifetime allowance – the promised lifetime allowance administrator look-up service should be available in "early Summer", along with an additional member function for online notification to HMRC where lifetime allowance protection has been lost.

View the newsletter.

HMRC publishes issue 25 of its Countdown Bulletin

Of interest to all formerly contracted-out DB schemes is the latest edition of HMRC's Countdown Bulletin. Contents include

- Changes to DWP legislation regarding late payments of CEP – from *April 6, 2017*, new contribution equivalent premiums (CEP) provisions came into force under the Occupational Pension Schemes and Social Security (Schemes that were contracted-out and Graduated Retirement Benefit) (Miscellaneous Amendments) Regulations 2017. They allow late payments of CEPs to the DWP through the Scheme Reconciliation Service (SRS) query process.

- HMRC confirms that it will apply these provisions consistently across all processes and member types, and that it is considering developing an automated solution to resolve "Not in Scheme" queries for members over State Pension age or deceased.

- Paying State Scheme Premium (SSP) liabilities via Bacs – HMRC reminds schemes to begin their 16 character payee reference with the Scheme Contracted Out Number (SCON) followed by "/SPP", for example, S1111111A/SSP. This will avoid unnecessary delays in having the premium applied.

- Scheme reconciliation and active member queries – closure scan and scheme reconciliation queries will no longer need to be submitted on separate templates, and automated responses will be available for closure scan queries. Further information is also available on the automation of SRS queries.

- SRS to late expressions of interest – having previously announced that it would no longer accept late expressions of interest to register of SRS, HMRC will now accept late expressions of interest in exceptional circumstances.

View the Bulletin.

The Financial Guidance and Claims Bill

As announced in the Queen's Speech and outlined above, the Financial Guidance and Claims Bill was introduced into Parliament and received its first reading in the House of Lords on *June 22, 2017*.

The Bill will establish a single financial guidance body (SFGB) that will replace Pension Wise, TPAS and the MAS (see further below). The Bill will also transfer the regulation of claims management services to the FCA.

The new SFGB will have four functions

- Pensions guidance
- Debt advice
- Money guidance
- Strategic function (primarily, supporting the development of a national strategy to improve financial capability among the public).

The pensions guidance function will be to provide "*information and guidance on matters relating to occupational and personal pensions*". In particular, the SFGB will be expected to "*provide information and guidance for the purposes of helping a member of a pension scheme, or a survivor of a member of a pension scheme, to make decisions about what to do with the flexible benefits that may be provided*".

This wording (together with the associated definitions) matches the wording currently setting out the scope of Pension Wise under the Financial Services and Markets Act 2000 (FSMA), and the relevant parts of FSMA will be repealed by the Bill from a date to be appointed in regulations.

The remainder of the Bill will put in place the framework for setting up the SFGB. In practice, it may delegate any of its functions other than the strategic function to a "primary delivery partner", which may in turn delegate functions to a "secondary delivery partner" (which may itself further delegate with the consent of the SFGB. The SFGB will be funded by industry levies and must set FCA-approved standards to be complied with by any person providing information or guidance under its pensions, debt or money guidance functions, and it must monitor compliance with these standards.

The Bill's second reading was on *July 5, 2017*.

Government's response to consultation on the SFGB

On *July 5, 2017*, HM Treasury and the DWP published the response to their consultation on creating a SFGB (see item on the Financial Guidance and Claims Bill above).

The new body will replace the Money Advice Service (MAS) the Pensions Advisory Service (TPAS) and the DWP's 'pension wise' guidance.

Other proposals set out in the response include:

- The SFGB will have the following four core functions
  - Provision of debt advice in England
  - Provision of money guidance across the UK
  - Provision of pensions guidance across the UK
  - To work with others in the financial services industry, the devolved administrations, and the public and voluntary sectors to support the co-ordination and development of a national strategy to improve people's financial capability and debt management ability and to provide financial education to children and young people.

The SFGB will be funded by levies on the financial services industry and pension schemes. It will be a non-departmental public body sponsored by DWP and will be accountable to Parliament. The proposal is to review it at least once every Parliament to ensure it remains fit for purpose, is well-governed and is properly accountable for what it does.

Summer Finance Bill to include reduction in money purchase annual allowance

In a written statement to the House of Commons, the Government has confirmed that it will reintroduce provisions it had previously withdrawn from the Finance Bill 2017, as it was fast-tracked through the legislative process shortly before the June general election. These provisions, which include the reduction in the MPAA, will be contained in a new Bill to be published "as soon as possible after the summer recess", which ends on *September 4, 2017*.

As well as the reduction in the MPAA from £10,000 to £4,000, the withdrawn provisions include an exemption from income tax for up to £500 worth of employer-arranged pensions advice in any tax year. The Government's statement confirms that where measures have previously been announced as applying from the start of the 2017–18 tax year or another date before the introduction of the Bill, those dates will take effect as originally announced.

The original Finance Bill provisions reducing the MPAA were stated to apply from *April 6, 2017*. A list published by HM Treasury and HMRC confirms that the pensions advice provisions and the reduction in the MPAA will apply from the start of the 2017/18 tax year.

Comment

Those who had hoped that the reduction in the MPAA would be dropped after this year's election will be disappointed. The reduction, largely seen as an unnecessary measure in the first place, will no doubt be viewed as particularly unacceptable now that it is to be backdated. Those retirees who have already accessed some of their pension fund under the pension freedoms have had their hopes dashed that the original £10,000 MPAA would be retained.

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the New Regulations) came into force on *June 26, 2017*, the deadline for transposition into UK law of the EU Fourth Money Laundering Directive.

The Money Laundering Regulations 2007 (the 2007 Regulations) require trust or company service providers to register with HMRC if they are not authorised by the FCA (or certain other specified professional bodies) and where they are in the business of offering services as a trustee or director of a trustee company.

The New Regulations define trust or company service providers in the same way as the 2007 Regulations, and thus registration will continue to apply to those acting as trustees by way of a business. However, HMRC's current guidance classifies occupational pension schemes as low risk trusts, meaning professional trustees of those schemes are not required to register with HMRC.

New reporting requirements

Under regulations 41-44 of the New Regulations, trustees of "relevant taxable trusts" (whether or not they are trust or company service providers) must keep adequate, accurate and up-to-date information on the beneficial ownership of their trust, and must also make this information available to law enforcement agencies and the UK Financial Intelligence Unit.

The extent of the work required by trustees and administrators will depend on whether HMRC modifies the definition of "beneficiary" for schemes, although there is currently no indication that it intends to do so. The regulations therefore appear to require trustees to keep accurate data on trustees, employers, other persons who exercise control over the plan and all identifiable beneficiaries – active members, pensioners, and deferred members. Where there is a class of beneficiaries not all of whom have been determined (e.g. potential recipients of survivors' benefits) then trustees need only maintain a description of the class.

Data to be recorded includes the name, date of birth, NI number (or residential address if there is no NI number) and unique taxpayer reference (if any) of all "beneficial owners" of the trust. Where the individual has no UK address, passport details must be obtained. The information will need to be provided to HMRC annually and also any changes notified, with the first deadline being *April 6, 2018* (or the end of the tax year in which they first become liable to pay income tax, CGT, inheritance tax, stamp duty land tax or stamp duty reserve tax). Failure to comply with the New Regulations will be a criminal offence, potentially resulting in a fine and/or up to 2 years' imprisonment.

The New Regulations do not currently include an exemption for pension scheme trustees from these requirements. Neither has HMRC indicated that any guidance it publishes will provide exemptions for occupational pension schemes. However, some assurance has been provided by HMRC in correspondence that it will "take a pragmatic approach to minimise burdens" on schemes and that it will provide guidance to the pensions industry on how the regulations will work in practice. We will provide an update once the new guidance is available.

The Occupational Pension Schemes (Charges and Governance) (Amendment) Regulations 2017 – DWP confirms restrictions on early exit charges and ban on member-borne commission

The above Regulations have now been finalised and they restrict the early exit charges that can be applied to the funds of members of occupational pension schemes using the DC pension freedoms. The consultation response also confirms the extension to the prohibition on charges being applied to members to recoup commission payments made by service providers to advisers. Such charges are a way of levying a cost on members to recover commission payments from the service provider to advisers.

The Government's response confirms that the regulations will come into force with few amendments, relating mainly to "minor and technical points". However, a provision relating to circumstances where a member could have been subject to multiple early exit charges has been withdrawn, as no specific examples of such occurrences could be identified.

The Regulations will

- Limit exit charges for *pre-1 October 2017* members to one per cent of the benefits being taken, converted or transferred, or such amount as was provided for under the scheme rules as at *October 1, 2017*. Trustees cannot increase charges and new early exit charges cannot be imposed.

- Ban early exit charges for new joiners once the regulations are in force on *October 1, 2017*. The Government's intention is to remove a possible disincentive to those seeking to access their pension savings. Similar provisions already apply to contract-based schemes under amendments to FCA rules that came into effect on *March 31, 2017*.

- Extend the existing prohibition on member-borne commission payments to agreements entered into before *April 6, 2016* by members of occupational pension schemes used for automatic enrolment. However, the ban will not apply to payments made before *October 1, 2017*. Service providers will have up to six months to make any necessary modifications to their processes in order to comply, effectively extending the deadline for compliance to *April 1, 2018*.

The Contracting-out (Transfer and Transfer Payment) (Amendment) Regulations 2017

These regulations came into force on *July 3, 2017*, and concern changes to enable transfers of pensioner members, with consent, from formerly contracted-out (defined benefit) occupational pension schemes to schemes that have never been contracted-out in certain circumstances

Whilst transfers of deferred contracted-out schemes pension rights with member consent are permitted to a scheme that has never been contracted-out, this isn't possible for transfers of pensioners' rights. The DWP is aware that certain schemes would like to perform these transfers, but are prevented from doing so by the legislation.

If these transfers do not take place, because of the financial position of some of the schemes, pensioner members may have to transfer to the PPF; the benefits members receive may then be less than if a transfer could be made to a newly established scheme. The newly permitted transfers will be restricted to circumstances where the scheme is undergoing a PPF assessment or where a regulated apportionment arrangement has been entered into.

DWP publishes consultation response on two new sets of draft amending regulations concerning GAR valuation and the advice requirement

These proposed regulations are relevant for schemes with "safeguarded flexible benefits". Such benefits are DC in nature, but also offer some form of guaranteed level of pension income, such as via a guaranteed annuity rate (GAR). The DWP has now published its consultation response, which deals with simplifications to the valuation process for safeguarded flexible benefits containing GARs, for the purpose of ascertaining whether the statutory threshold of £30,000 for the "advice requirement" applies. New consumer protections are also included, and these are intended to protect members who wish to transfer out such benefits and thereby risk losing potentially valuable guarantees.

The original implementation date was to be *October 1, 2017*, but this has now been put back to *April 6, 2018*.

The consultation response confirms that the Government intends to proceed with the proposed changes subject to "some relatively minor changes". These include separating the original proposals into two statutory instruments

- The Pension Schemes Act 2015 (transitional Provisions and Appropriate Independent Advice) (Amendment No.2) Regulations 2017 (the Valuation Regulations).
- The Pension Schemes Act 2015 (transitional Provisions and Appropriate Independent Advice) (Amendment) Regulations 2017 (the Risk Warning Regulations).

The new regulations will

- Simplify the process for assessing if a member is subject to the requirement to obtain appropriate independent advice.
- Introduce a new valuation procedure for member's safeguarded benefits containing GARs to mirror that used for calculating a member's cash-equivalent transfer value.
- Clarify when a personal risk warning needs to be sent and changes to the timings involved.
- Require the risk warning to tell the member that unless they tell their scheme otherwise, the transfer will go ahead.
- Provide greater flexibility for schemes in meeting the "projected income illustration" element of personalised risk warnings by allowing providers to use assumptions aligned with the FCA's rules for benefit projections.

View the consultation response.

R (Palestine Solidarity Campaign Limited and another) v Secretary of State for Communities and Local Government [2017] – High Court upholds challenge to LGPS statutory investment guidance

On June 22, 2017, the High Court issued its decision in R (*Palestine Solidarity Campaign Ltd and another) v Secretary of State for Communities and Local Government [2017*], holding that statutory guidance governing the investment strategy for the Local Government Pension Scheme (LGPS) was outside the minister's statutory powers.

Under regulations made in September 2016, the investment strategy for LGPS funds must be formulated within the statutory guidance and one of the criteria included is how policies on social, environmental and corporate governance considerations impact on the selection, non-selection, retention and realisation of specific investments. The guidance stated that administering authorities under the LGPS must not

- Use pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries except where the Government has put in place formal legal sanctions, embargoes and restrictions.
- Pursue policies that are contrary to UK foreign policy or UK defence policy.

The claimants, the Palestine Solidarity Campaign (a pressure group lobbying local and central government to support its campaign for an end to Israel's occupation of the West Bank and Gaza and advocating boycott, divestment and sanctions against Israel) and one of its pension scheme members challenged the statutory guidance by way of judicial review on the following grounds

- The prohibition on boycotts, divestments and sanctions was outside the minister's statutory powers (ground one).
- The foreign/defence part of the guidance lacked clarity and certainty and was therefore unlawful (ground two).
- The guidance breached EU law which prohibits local investment decisions being subject to "any kind of prior approval or systematic notification requirements" (ground three).

The Court ruled in favour of the claimants on the first ground and accepted that this paragraph of the guidance (and the summary of requirements) fell outside the proper scope of the Secretary of State's statutory powers. The Court held that the requirements were issued not in the interests of the proper administration and management of the LGPS from a pensions perspective but were a reflection of broader political considerations, including a desire to advance UK foreign and defence policy, to protect UK defence industries and to ensure community cohesion.

In rejecting the other two grounds of challenge, the Court

- Held that there is no binding principle that ministerial guidance or policy is unlawful because it is materially unclear or ambiguous, or silent as to important circumstances. In order for the guidance to be unlawful, it had to be positively misleading or erroneous in law, not simply imprecise.
- Rejected the claimants' assertion that the prohibition in the guidance amounted to a system of prior approval. The requirement in the directive for prior approval involved individual scrutiny of investment decisions which is not what the ban in the guidance envisaged.

However, on July 17, 2017, it was announced that revised guidance has now been issued, with the removal of the paragraph in the original guidance which stated: " ... *the Government has made clear that using pension policies to pursue boycotts, divestment and sanctions against foreign nations and UK defence industries are [sic] inappropriate, other than where formal legal sanctions, embargoes and restrictions have been put in place by the Government*".

Comment

It is unclear whether this decision will result in local authorities changing the strategy under which they make decisions before investing LGPS funds but they will need to ensure that their investments are made taking into account appropriate factors, both financial and non-financial. There is both legal precedent and DB investment guidance from TPR recognising that trustees may take non-financial considerations into account when making investment decisions. Whether trustees in occupational schemes will pay greater heed in future to political factors when making investment decisions regarding scheme funds remains to be seen but they may find their decisions challenged if they do.

Williams v The Trustees of Swansea University Pension & Assurance Scheme and another [2017] – discrimination arising from disability – Court of Appeal decides that advantageous treatment was not unfavourable

In *Williams v The Trustees of Swansea University Pension & Assurance Scheme and another*, the Court of Appeal (CA) considered whether advantageous treatment of a member, which could have been more advantageous, could constitute unfavourable treatment within the meaning of section 15 of the Equality Act 2010.

Legal background

Under section 15(1) of the Equality Act 2010 (the Act), "discrimination arising from disability" in the pensions context occurs where both

- An employer treats a scheme member unfavourably because of something arising in consequence of the member's disability.
- The employer cannot show that the treatment is a proportionate means of achieving a legitimate aim.

Until the employment appeal tribunal (EAT) decision in this case, there was no authority on the meaning of unfavourable treatment in this context. Nevertheless, tribunals have tended to treat it in a similar way to the concept of detriment, as understood in the context of the Act.

"Detriment" is not defined in the Act and tribunals have looked to the meaning of detriment established by case law. In *Shamoon v Chief Constable of the Royal Ulster Constabulary* [2003], the House of Lords held that a worker suffers a detriment if a reasonable worker would or might take the view that they had been disadvantaged in the circumstances in which they had to work. An "unjustified sense of grievance" is not enough.

Facts of the case

Mr Williams suffered from Tourette's Syndrome, obsessive compulsive disorder, depression and other psychological problems. He worked for Swansea University for approximately 13 years, the first ten of which were full-time. In the last three he reduced his hours by half, as a result of reasonable adjustments agreed by the University. Eventually, his medical conditions made him incapable of continuing work and he took ill-health retirement at the age of 38. Under the University's pension scheme rules, he was entitled to an accrued pension, as well as to an enhanced pension based on his final salary at retirement (both without actuarial deduction).

Mr Williams successfully brought a claim for discrimination arising from disability under section 15 of the Act. The employment tribunal held that the failure to base his enhanced pension on the full-time salary he had received prior to his reduction in hours amounted to unfavourable treatment because of something arising in consequence of his disability, and that the treatment was not justified. In reaching this conclusion, the tribunal accepted that the meaning of unfavourable treatment could be equated with that of detriment.

The University successfully appealed to the EAT, which held that unfavourable treatment does not equate to the concept of detriment. The EAT held that treatment which was advantageous could not be said to be unfavourable merely because it could have been even more advantageous. To be treated unfavourably, a person would need to show that he was not in as good a position as others generally would be. The EAT accordingly remitted the case to a freshly constituted. Mr Williams appealed against the EAT's decision.

In the CA, Mr Williams claimed that

- His enhanced pension was based on part-time salary rather than full-time. This was to his disadvantage and so amounted to unfavourable treatment.
- The disadvantage occurred because he had had to reduce his hours. It was agreed that this had arisen in consequence of his disability.
- He had therefore suffered discrimination arising from disability (subject to justification arguments).

Decision
The CA unanimously agreed with the EAT and dismissed Mr Williams' appeal.

The CA commented that only people who are disabled within the meaning of the Act would benefit from the ill-health retirement enhanced pension offered by the University. It followed that Mr Williams' case involved a comparison with other disabled people, whose disabilities had necessitated a sudden retirement, with no intervening period of part-time working.

With this in mind, the CA stated that the critical question was "*whether treatment which confers advantages on a disabled person, but would have conferred greater advantages had his disability arisen more suddenly, amounts to 'unfavourable treatment' within section 15 [of the Act]*?" The CA held that it does not.

In confirming its agreement with the EAT's decision, the CA illustrated what it considered to be the flaws with Mr Williams' case. For example, applying the logic of his case would mean that the following people would also potentially have section 15 claims

- A disabled person who only applied for a part-time role because of their disability (but who would otherwise work full-time if they were not disabled) and received a part-time salary accordingly. In the CA's view, it could not have been Parliament's intention to throw the onus on employers to justify the payment of part-time pay for part-time work in these circumstances.
- A disabled person who took ill-health retirement having initially worked full-time for, say, only six months, but who reduced to part-time because of their disability and then continued to work those part-time hours for, say, the next 13 years. The CA commented that it would be surprising if such a person was entitled to an enhanced pension based on full-time pay.

The only aspect of the EAT's judgment with which the CA disagreed was the decision to remit the case to a tribunal, instead substituting a finding of no discrimination.

Comment
The main practical point of the judgment is that treatment which is advantageous to the member will not amount to unfavourable treatment (under the Act) merely because the individual considers that he could have been treated even better.

This is a significant judgment as it is the first time the CA has considered what is meant by being treated "unfavourably" under section 15 of the Act. Although it does not say so expressly, the CA endorsed the EAT's view that "unfavourably" in the context of section 15 of the Act does not equate to the concept of detriment. But what is the difference between the two?

Under the reasoning in *Shamoon*, disadvantage is considered from the perspective of the reasonable worker, noting that an unjustified sense of grievance is not sufficient. However, it is arguable that many a worker would feel as aggrieved as Mr Williams if they found themselves in a similar situation and it might be difficult to argue that such a worker would be unjustified in feeling that way.

Nevertheless, the House of Lords' *Shamoon* decision is binding on both the EAT and the CA. In advancing the view that the unfavourable treatment test under section 15 of the Act is a distinct test (and one which does not involve the views of the reasonable worker) the lower courts are able to sidestep any potential conflict with the House of Lords' view.

We understand that Mr Williams is seeking permission to appeal to the Supreme Court.

View the judgment.

Walker v Innospec Ltd and others [2017] – Supreme Court confirms same-sex partners entitled to equal survivors' pension benefits

In a judgment handed down on *July 12, 2017*, the Supreme Court (SC) has ruled that survivor benefits for same sex partners cannot be restricted to those calculated only on the basis of pensionable service after *December 5, 2005* (the date when the Civil Partnership Act 2004 came into force).

The SC held that

- The partial exemption to the requirement to equalise survivor benefits set out in paragraph 18 of Schedule 9 to the Equality Act 2010 is incompatible with EU law.

- Provided they remain married at the time of Mr Walker's death, Mr Walker's husband would be entitled to a survivor's pension calculated on the basis of the entire pensionable service, not merely that accrued post-5 December 2005.

Mr Walker's claim against his employer, originally begun in 2012, was that any survivor's pension payable to his same-sex spouse should be based on his entire pensionable service, as it would be if he were in an opposite-sex marriage. The financial effect on the pension his spouse would have received was a reduction of £44,000 per annum.
(See our Stop Press from October 2015 for full details of the background to the case).

The SC held that the right to an equal survivor's pension was not "permanently fixed" as the pensionable service it would be based on accrued over time. Instead, it should be assessed at the point that it becomes payable, provided Mr Walker and his partner remained married and his partner does not predecease him. At that point, "d*enial of a pension would amount to discrimination on the ground of sexual orientation*". The SC ruled that the Court of Appeal was wrong to conclude that only service after the Equal Treatment Framework Directive had been implemented should be taken into account for calculation purposes, confirming that Mr Walker had an "*entitlement to a pension calculated on the basis of his years of service before the Directive was transposed*".

Comment

In practice, many schemes have granted civil partners the same rights to receive a full spouse's pension as married partners. However, the decision will have an immediate impact on schemes that have not fully equalised survivor benefits for same-sex partners. Where schemes have relied on the exemption in the Equality Act 2010 and have not equalised benefits, immediate action should be taken to revise both the scheme rules and members communications to reflect the ruling.

The decision may be particularly significant for public-sector pension schemes. A report from the DWP report published in 2014 concluded that equalisation between the sexes, as well as that based on sexual orientation, could cost them around £2.9 billion.

However, it is difficult to reconcile the SC decision in *Walker* with its decision in *O'Brien* (see below) and the Barber decision of 1990. The "no retroactivity" principle applies to EU legislation and the SC acknowledged the difficulty of identifying the time at which the pension entitlement had become fixed – that is, was it at the time of the member's retirement, or at the (future) date of his death when a spouse's pension would be payable?

View the judgment.

O'Brien v Ministry of Justice [2017] – Supreme Court refers case to ECJ

In *O'Brien v Ministry of Justice* [2017], which was heard in the SC along with *Walker v Innospec*, the SC unanimously decided to refer the question of whether the Part-Time Workers Directive (97/81/EC) requires periods of service accrued before the deadline for transposing that Directive to be taken into account when calculating the pension of a part-time judge. The difference between the two periods of service is over 22 years.

In October 2015, the CA held that Mr O'Brien's pension rights were determined by reference to the EU law which applied at the time of the period of service in respect of which those rights were acquired. The effect of this decision was that part-time judges were only entitled to a pension calculated by reference to pensionable service from April 7, 2000, the date on which the UK was required to transpose the Directive into national law.

We will report further once the case has been heard by the ECJ.

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