GODDARD PERRY
CONSULTING

Hot topics in Pensions

Spring 2014

1. Pensions Act 2014

After a lengthy passage through Parliament the Pensions Act 2014 ("the Act") finally received Royal Assent on 14 May 2014. This landmark Act makes radical changes to the private and state pension's landscape in the UK. The key provisions are:

- **State pension reform (single-tier state pension)**

The Act includes provisions to introduce a new single-tier flat rate state pension from 6 April 2016. The new state pension replaces the current Basic State Pension and State Second Pension. The full new state pension will be no less than £148.40 per week. The actual amount will be set in autumn 2015.

- **Increase in State Pension Age**

State pension age will rise from age 66 to age 67 for men and women between 2026 and 2028. The Government will be required to review state pension age at least once every 6 years to take account changes to life expectancy.

- **End of DB contracting-out - statutory amendment power**

Contracting-out on a defined benefit basis will end in 2016 when the new state pension is introduced. The Act contains a power for private sector employers to increase member contributions and/or reduce future benefit accrual, to offset the increase in National Insurance contributions which employers will face.

Before this power can be exercised, an actuary will be required to certify that the saving arising out of any amendments does not exceed the increase in the employer's National Insurance contributions. The Government is currently consulting on draft regulations which will provide important detail on the operation of the employer override power.

- **Regulator's new statutory objective**

The Act introduces a new statutory objective for the Pensions Regulator requiring it to minimise any adverse impact on the sustainable growth of sponsoring employers when exercising its functions relating to scheme funding. The new objective comes into force on 14 July 2014. The Pensions Regulator has already consulted on a revised Code of Practice on Scheme Funding prompted by this new objective. The consultation ended in February and a new Code is expected to be published on 10 June.

- **Automatic transfer of small pots – “pot follows member”**

The Act enables a system to be put in place so that an individual's defined contribution pension will be automatically transferred to their new pension scheme when they change jobs. A formal consultation on draft regulations setting out the details is now expected with new regulations anticipated to come into effect before the 2015 general election.

- **Cap on charges**

The Government has previously said that it intends to introduce a cap on charges of 0.75% of funds under management on qualifying schemes from April 2015. The Act gives the Government the power to now do this.

- **Abolition of short service refunds from money purchase plans**

At a date yet to be announced, members of occupational money purchase schemes who leave pensionable service between 30 days and 2 years from starting will no longer be entitled to a refund of their contributions. This is designed to ensure that members retain savings within a pension scheme.

- **PPF compensation cap**

The PPF compensation cap has been increased for members with more than 20 years’ service. All those receiving PPF compensation will have their payments reassessed and uplifted as necessary for compensation due from April 2015.

2. Same sex marriages

Further to the Marriage (Same Sex Couples) Act 2013, the first marriages of same sex couples took place on 29 March 2014. For the purposes of occupational and state pensions, same sex couples will be treated in the same way as civil partners are currently. This means that, on the death of a defined benefit (DB) scheme member after 29 March 2014, a surviving same sex spouse will be entitled, as a minimum, to the same non-contracted-out benefits as an opposite sex surviving spouse for pensionable service accrued since 5 December 2005. However, in respect of any contracted-out rights, a same sex spouse will be entitled to 50% of the contracted-out rights accrued by the member since 6 April 1988.

If trustees make no changes to their rules, a same sex spouse will only be entitled to the same minimum level of benefits paid to civil partners. If Trustees wish to provide benefits in excess of this minimum they may need to amend their rules in which case legal advice should be sought,

It is worth noting that the 5 December 2005 limit is currently under review as it has been challenged as being in breach of European Union law. The outcome of the review is expected by July 2014.

Trustees should seek advice from their professional advisers regarding possible amendments to their scheme rules to accommodate the new legislation. Trustees should also consider communicating the change to the pension scheme membership.

3. Budget 2014

This year's shock budget has transformed the landscape of UK pension provision with the Chancellor claiming to make the most far reaching pension reforms of the last century. Details of these radical reforms are contained in the Government's consultation paper "Freedom and choice in pensions". The key changes, some with immediate effect, are set out below.

Defined Contribution ("DC") flexibility form April 2015

The core change is significantly increased flexibility for individuals reaching retirement with DC savings. From April 2015, it will be possible for an individual, from the age of 55, to take their entire pension pot as a lump sum. Amounts above the tax free limit will incur tax at the member's marginal income rate. There will no longer be a requirement for members to purchase an annuity. Income drawdown will no longer be subject to a cap or the requirement to have a minimum amount of guaranteed pension income before selecting income withdrawal.

To help people understand these choices, individuals with DC pension pots, approaching retirement, will be offered free and impartial face-to-face guidance. The Financial Conduct Authority, working closely with a number of parties, will develop the framework for this. A £20 million development fund has been made available.

We are likely to see an increase in transfer requests from DB to DC pension plans from members wishing to take advantage of the additional DC flexibilities. The Government intends to ban transfers from public service pension schemes to DC plans and are also considering whether there should be restrictions from private sector DB plans to DC plans.

Immediate changes from 27 March 2014.

There are also a number of immediate changes.

Increases to small lump sums

- For DB and DC schemes, an increase in the trivial commutation limit from £18,000 to £30,000.
- An increase in the limit on the value of small pensions which can be taken as a lump sum (regardless of pension savings elsewhere) from £2,000 to £10,000.
- For personal pensions, an increase in the number of small pension pots that can be taken as a lump sum from 2 to 3.

Drawdown

- An increase in the maximum amount that can be taken out each year from a capped income drawdown arrangement from 120% to 150% of an equivalent annuity
- A reduction in the amount of guaranteed income needed in retirement to access flexible drawdown from £20,000 per year to £12,000 per year.

3. GMP reconciliations – HMRC's new Scheme Reconciliation Service

The end of contracting out in April 2016 will trigger the requirement for all schemes currently contracted-out to reconcile Guaranteed Minimum Pensions ("GMPs"). In order to reduce the large number of schemes all attempting to reconcile GMPs simultaneously, HMRC have introduced a new "Scheme Reconciliation Service" to try and make the process easier. This service enables schemes to beat the rush and reconcile membership and GMP reconciliation data in advance of 2016.

4. Pension Protection Fund

Assumptions - The Pension Protection Fund (PPF) has updated its guidance on the assumptions to be used for PPF levy (known as section 179) and PPF entry (section 143) valuations. The changes are exactly as proposed in the recent consultation. The revised assumptions are intended to more closely reflect pricing in the bulk annuity market. The new assumptions apply for valuations with an effective date on or after 1 May 2014.

PPF levies – Experian was chosen as the PPF's new insolvency risk score provider last July. Following Experian's appointment, the PPF has been working with Experian and an industry steering group to develop a new model for calculating insolvency risk. In March 2014 the PPF confirmed that the new model would be a bespoke model tailored to its own universe of employers and the specific risks they pose to the PPF. The PPF is due to issue a consultation on the model at the end of May 2014. The new risk scores will not be used by Experian until 1 October 2015 and so will impact on next year's PPF levies will be based on a six month averaging period to 31 March 2016 (rather than the usual 12 month period).

5. Money purchase definition

The new statutory definition of money purchase benefits is expected to come into force in July 2014. Under the new definition benefits will only be money purchase where assets are equal to liabilities and a funding deficit cannot arise. Pension schemes which are currently treated as money purchase, but have Consultation concluded 6 May 2014.

6. Disclosure of information amendments

Updated with effect from 6 April 2014.

Investment report - the annual investment report for defined benefit schemes will need to include a statement of any policy adopted by the trustees concerning rights (including voting rights) attaching to investments as well as the extent to which social, environmental or ethical considerations are taken into account in investment decisions.

Timing for notification of 'material alterations' - where a 'material alteration' is made to any of the basic scheme information provided to a member, this must now be communicated 'before or as soon as possible after' the date the change takes effect. Previously, the requirement was to provide information before the change took effect 'where practicable'.

Benefit statements (defined benefit): these can now use an assumed retirement date which does not have to be the scheme's normal retirement age.

Transfers out: the required information is simplified but must state that more detailed information is

Where can I get further information?

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

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available on request.