



THE CHEVIOT TRUST

Pensions for the legal sector

PENSIONS UPDATE – FEBRUARY 2011

1. DWP consults on impact of switch to Consumer Prices Index (CPI)

In July 2010 the Government announced its intention to replace the Retail Prices Index (RPI) with CPI as the measure for determining increases for all occupational pensions, not only public sector schemes.

On 8 December 2010, the Department for Work and Pensions (DWP) published a consultation paper on the impact of using the CPI as the measure of price increases on private-sector pension schemes. The main points of the consultation are:

- **No statutory override.** The Government does not propose to introduce legislation to override the rules of occupational schemes in order to impose CPI.
- **No modification power.** Neither does the Government intend to introduce a modification power to allow schemes to amend their rules to reflect CPI as the basis for revaluation and indexation of members' benefits.
- **No CPI underpin for schemes with RPI.** The Government intends to legislate to prevent schemes being required to pay pension increases at the higher of CPI or RPI if, in future, RPI is lower than CPI.
- **Changes to rules on indexation and revaluation to require consultation.** Currently, changes to scheme rules on indexation and revaluation are not "listed changes". The Government intends to amend the regulations to require employers to consult on changes to scheme rules on indexation or revaluation where the change is "less generous" to members.

The consultation ends on 2 March 2011 and the next annual revaluation order will use the CPI as the measure of inflation for the year to 30 September 2010. The Order came into force on 1 January 2011.

View the [consultation paper](#).

Cheviot comment – many in the pensions industry are disappointed that, after months of speculation, the Government has stated that it intends to introduce neither a statutory override to impose CPI nor a modification power to enable schemes to make the switch. The extent to which schemes can adopt CPI will now depend on the way their rules are drafted. We are currently reviewing all schemes affected.

2. HM Treasury publishes consultation on options to meet pensions tax charges

On 2 December, HM Treasury published a discussion document, "Options to meet high annual allowance charges from pension benefits", following the coalition Government's announcement that:

- from April 2011, the annual allowance (AA) for tax-privileged pension saving will be reduced from the current level of £255,000 to £50,000; and
- the lifetime allowance (LTA) will also be reduced, from its current level of £1.8 million to £1.5 million

It has been recognised that some individuals who have pension contributions which exceed the AA in a single year may face a tax charge. In such situations, the Government has agreed to consult on options to enable individuals to meet the charge out of their pension benefits, rather than current income.

Responses were invited by 7 January 2011.

Cheviot comment – This lengthy document shows how complex the proposals are. It is too early to comment and we will keep a watching brief.

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3. HMRC publishes clarification on reduced annual allowances (AA)

HMRC has published guidance in relation to the reduced AA that will apply from 6 April 2011.

The guidance also states that schemes which have not previously nominated a pension input period (PIP) may make a retrospective nomination to ensure that their PIP is aligned with the tax year.

View the [guidance note](#).

Cheviot comment – We shall update the website with the guidance for members. Cheviot's PIP is 1 January to 31 December and was notified to members in April 2006.

4. HMRC publishes lifetime allowance (LTA) guidance

HMRC has now also published draft guidance on the changes to the LTA, which will be reduced from £1.8 million to £1.5 million from 6 April 2012. The draft guidance is based on the draft legislation published on 9 December 2010, and is subject to any changes which may be made before the legislation is finalised.

View the [draft guidance](#).

Cheviot comment – The draft guidance is based on the draft legislation published on 9 December 2010, and is subject to changes which may be made before the legislation is final. We will keep a watching brief.

5. DWP consults on guidance for offering default option for defined contribution automatic enrolment schemes

This consultation document seeks views on offering a default option for defined contribution automatic enrolment pension schemes. Automatic enrolment will see millions of individuals newly saving for retirement. It is likely that many of these individuals will not make an active investment choice. For this reason, the Government has developed guidance to provide what it hopes will be helpful information on the design, governance, communication and review of default investment options. The deadline for responses is 7 March 2011.

View the [consultation paper](#).

Cheviot comment – We are currently reviewing the Money Purchase Scheme to ensure it meets the criteria for a Qualifying Workplace Pension Scheme, alternative to NEST and will keep you informed of future developments.

6. NEST announces details of charges and consultation on rule amendments

The National Employment Savings Trust (NEST) has published a briefing note setting out how its combination charge will meet its charging objective. This follows the announcement last month that a combination charging structure will apply to NEST members. Broadly, this will consist of an annual management charge of 0.3 per cent on the total value of the member's fund and a contribution charge of 1.8 per cent on contributions to the scheme. The contribution charge will fall away once the costs of establishing NEST have been met.

View the [briefing](#).

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NEST has consulted on two amendments to the NEST scheme rules. The consultation period finished on 24 December 2010.

The first amendment would enable an employer formally to cease participation in NEST. By giving 28 days notice, the employer would be allowed to end their participation and be classed as former participating employers. They would then have no further legal obligations or liability to the scheme in respect of that period of participation. Employers could participate in NEST again in the future.

NEST has also consulted on an amendment so that a member's benefit age (that is, the age at which the member intends to take his benefits) may be adjusted automatically if the member decides not to take his benefits at a pre-arranged date.

View the [consultation paper](#).

Cheviot comment - In line with our previous comment we will keep a watching brief.

7. HM Treasury publishes call for evidence on early access to pensions savings

On 13 December, HM Treasury published a call for evidence to explore whether allowing early access to private pensions could encourage higher levels of saving. The Government is seeking views on the potential benefits and risks of the proposal, how it could be offered and to what extent early access would be welcomed by pension schemes, providers and individuals.

The Government has stated that it is committed to encouraging saving and that it wants to give individuals the maximum flexibility and responsibility to save for retirement. The consultation paper identifies four main options:

- A loan model allowing individuals to borrow from their pension fund.
- A permanent withdrawal model, allowing access to funds without repayment obligations - possibly in limited circumstances, such as cases of hardship.
- Early access to the 25 per cent tax-free lump sum currently available from age 55.
- A feeder-fund model, creating a more flexible savings product linking liquid savings products, such as ISAs, and pension savings together into a single account.

Responses should be submitted by 25 February 2011. View the call for evidence document "[Early Access to Pension Savings](#)".

Cheviot comment - We will keep a watching brief.

8. Government proposals to scrap the rule requiring compulsory annuitisation by age 75

HM Treasury has now published its consultation response and has confirmed that the tax rules currently in force, levying charges if individuals do not draw their benefits by age 75, will be removed from 6 April 2011.

The following key points apply in relation to the end of the annuitisation requirements:

- The existing unsecured pension and alternatively secured pension (ASP) regimes will be replaced with a single "drawdown pension". A single annual withdrawal cap will apply.

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- A minimum income requirement (MIR) will mean that to take advantage of the drawdown pension provisions, an individual will need to prove annual income of at least £20,000, including State pension benefits.
- Lump sums such as the pension commencement lump sum and the trivial commutation lump sum will be able to be paid after age 75.
- A 55 per cent tax charge will apply to unused drawdown funds that are paid as lump-sum death benefits in relation to an individual who has died after age 75. Inheritance tax will no longer be levied on unused drawdown pension funds paid after age 75.

Cheviot comment – the proposed scrapping of compulsory annuitisation at 75 has been largely welcomed as good news for savers. However, the changes are likely to benefit mainly the wealthy, as a minimum annual pension income of £20,000 applies.

9. Legislation

Amended Disclosure Regulations published

Regulations amending the disclosure of Information came into force on 1 December 2010.

The amendments permit schemes to use methods of electronic communication (that is, via email and websites) in order to provide information to scheme members. Members will be able to opt out of receiving information by electronic means, in which case the scheme administrators will be required to continue to provide information by post.

Cheviot comment - These changes have generally been welcomed by schemes, as they should help to reduce scheme administration costs. We shall be contacting members to seek their approval.

Draft Finance Bill 2011

HM Treasury has published draft clauses for the Finance Bill 2011, which is due to be published in final form on 31 March 2011. The main pensions related points are:

- **Ending of annuitisation requirements**
- **Reduction of the annual and lifetime allowances** - New clauses will implement the planned reduction in the LTA from £1.8 million to £1.5 million in the 2012/13 tax year. A new “fixed protection” regime will enable individuals to take advantage of the current £1.8 million allowance so long as they accrue no further benefits. Those who claimed primary or enhanced protection in relation to pre-2006 rights will also be able to rely on the £1.8 million LTA.

The maximum amounts for winding-up lump sums and trivial commutation lump sums will be de-coupled from the value of the LTA from the 2012/13 tax year. These limits, currently set at one per cent of the LTA, will be fixed at £18,000.

HMRC has published [draft guidance](#) on the reduction of the LTA (noted above).

- **Anti-avoidance - disguised remuneration** - Provisions are included which target the use of trusts and other arrangements to avoid, defer or reduce tax liabilities.
- **Tax aspects of NEST** - Several provisions to amend the tax rules in relation to the new regime will be implemented.

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Equitable Life (Payments) Act 2010

The Equitable Life (Payments) Act 2010 received Royal Assent on 16 December 2010. This Act will allow the Government to establish and fund the compensation scheme to those who suffered financial loss following the collapse of Equitable Life in 2001.

10. Recent Cases

“No detriment” pension promise transfers to new employer alongside TUPE transfer - Whitney v Monster Worldwide Ltd [2010] EWCA Civ 1312

On a business transfer governed by the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), matters relating to transferring employees’ rights under occupational pension schemes are excluded from the protection of the TUPE regime. However, there is a limited exception to this exclusion in relation to “any provisions of an occupational pension scheme which do not relate to benefits for old age, invalidity or survivors”, which has been applied principally to enhanced pension rights on early retirement following redundancy.

In this case, the Court of Appeal (CA) upheld a High Court decision that assurances given to an employee that he would be no worse off in a new defined contribution pension scheme following closure of the employer’s DB scheme amounted to a binding guarantee. The CA held that it did not matter that the employer’s promises were not recorded in a single document as there was “unanimity of view that there was a contract”. The guarantee, which the CA found also covered increases to pensions in payment in line with the Retail Prices Index, transferred to the new employer by novation alongside the TUPE transfer.

View the [judgment](#).

Cheviot Comment: A key point is that the CA was willing to conclude that a guarantee was given and was legally binding even though it had evolved over time and was not recorded in a single document. The Court held that the “unanimity of view” was sufficient, although the terms were not in writing.

In addition, employers should be aware that historic pension promises can be enforced by the courts many years after they are made. Here the CA concluded that the transferring employer had made a free-standing contractual commitment with its employees and that its pre-transfer assurances should be honoured.

Employers involved in TUPE transfers should ensure that thorough due diligence is undertaken and that adequate warranty protection is obtained.

February 2011

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