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UK PENSIONS UPDATE

There have been a number of important developments this month including a further High Court judgment on RPI/CPI, the publication of some long awaited (potentially helpful) guidance from HMRC on GMP equalisation as well as some further detail on how the Regulator is proposing to raise trustee governance standards. We are giving a brief update this month on the progress of the Pension Schemes Bill, which entered committee stage in the House of Lords on 24 February, but will be giving you further detail in an upcoming edition of our Update.

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HMRC publishes GMP equalisation tax guidance

Following the 2018 High Court decision in *Lloyds* (please see our October 2018 Update for more information) and the publication of other industry guidance, HMRC has published tax guidance on Guaranteed Minimum Pension (GMP) equalisation, in the form of a newsletter (the Guidance).

The Guidance confirms HMRC's views in relation to various tax matters that may be relevant when schemes equalise for the effect of GMPs. Importantly, however, the Guidance applies only to GMP *equalisation* (i.e., an approach where dual record keeping is required - Methods B, C1 and C2 in the *Lloyds* judgment), and not to GMP *conversion* (where GMPs are converted into "standard" scheme benefits - referred to as Method D2 in the *Lloyds* judgment), or any adjustment of other benefits which is not strictly required for equalisation purposes. HMRC notes in the Guidance that it is continuing to consider other pension taxation issues relating to GMP equalisation, including the treatment of lump sum and death benefit payments, as well as GMP conversion.

The Guidance is helpful as it confirms the general principle that any increase to benefits as a result of

GMP equalisation should not be tested for annual allowance purposes in the past, or prejudice applicable lifetime allowance protections. This is on the basis that the increase results from pension built up in the period between 17 May 1990 and 5 April 1997. However, HMRC notes that adjustments may be required in relation to future annual allowance calculations, and will have an impact on the amount of any previous and future benefit crystallisation events for lifetime allowance purposes. Further notifications to HMRC from both trustees and members may be required, as well as tax payments where the lifetime allowance is exceeded.

In terms of what this means for pension schemes in practice as they look to comply with the Lloyds judgment, the Guidance is particularly helpful for schemes that have decided to use Methods B or C as, once the High Court has given its decision on the issue of historic transfers in the next instalment of the Lloyds litigation, there are unlikely to be any further major impediments to proceeding with the equalisation process. However, for trustees and employers that are interested in pursuing GMP conversion, they may wish to wait for further specific HMRC guidance on this method.

Brief update on the Pensions Schemes Bill

We have reported previously on the Pension Schemes Bill, which contains provisions addressing, amongst other matters, the Regulator's powers, pension dashboards and collective defined contribution arrangements. A number of further amendments are currently being considered, including, in particular, a new provision introduced by the Department for Work and Pensions (DWP) relating to climate change risk.

The stated intention of the new provision, which would be added to the Pensions Act 1995, is to require that trustees effectively govern their scheme's exposure to the effects of climate change. The DWP has confirmed that this provision is designed to reflect recommendations made by the industry-led Taskforce on Climate-related Financial Disclosures created by the Financial Stability Board (established to develop a set of recommendations for consistent climate-related financial risk disclosures in mainstream reporting). Whilst the DWP has also confirmed that the changes are "not intended to direct pension schemes as to how they should invest", the new requirements, as currently drafted, may well impose further obligations on trustees.

Whilst no immediate action is required, trustees should stay abreast of developments in this area. It is not yet known when such a provision, if enacted, would come into effect.

Regulator publishes response to future of trusteeship and governance consultation

The Pensions Regulator (the Regulator) has published its Response to the Consultation that it issued in July 2019 in relation to the future of trusteeship and governance. Please see our July 2019 Update for more information on the Consultation.

In the Consultation, the Regulator sought feedback in three main areas: (i) trustee knowledge and understanding (TKU), skills and ongoing learning; (ii) scheme governance structures for effective decision-making; and (iii) driving DC consolidation. The Regulator also made various suggestions as to how improvements could be made in each of these areas. However, the Regulator confirmed in the Response that it is not proceeding with several of its original proposals, including a requirement to have a professional trustee on every board, minimum qualifications for trustees and mandatory board diversity reporting requirements.

The main proposed next steps for the Regulator coming out of the Response were that it will:

- Review and update TKU expectations in a code of practice, related guidance and the trustee toolkit. A consultation is expected in the early part of 2021.
- Establish and lead an industry working group to develop guidance and practical tools to support schemes to improve diversity and inclusion on boards; and
- Continue to monitor DC consolidation activity and work with both industry and the DWP to find solutions to overcome barriers to further consolidation.

The Response also confirmed that, in the "*first half of this year*", the Regulator will be consulting on the single Code of Practice that will combine many of its existing Codes of Practice and will address the changes required under the Pensions Act 2004 (as amended in 2019) for pension schemes to establish and operate an effective system of governance.

Further RPI/ CPI case - employer fails to switch to CPI

The High Court has rejected the arguments by the principal employer of an Atos pension scheme that the correct index for pension increases is an index other than RPI.

"This is another in a growing list of cases where a sponsoring employer has failed to persuade the court that an index other than RPI should be used. Arguments appealing to a dynamic interpretation of increase rules - essentially that the draftsperson intended the index as shorthand for the main index of consumer prices, rather than RPI which is now published only because the ONS is obliged to do so for index-linked gilts - now seem doomed to fail. As RPI is still published for this narrow purpose, schemes are often stuck with an index which is roundly discredited."

Arron Slocombe
Partner

The Court had to construe "Retail Prices Index", defined as "*the general index of retail prices (all items) published by the Office for National Statistics", or alternatively "any substituted index published by that Office (or its successor) as the Principal Employer and the Trustees may agree…..*") - if one of two "triggers" occurred (where RPI "is not published" or "ceases to exist"). The Court rejected arguments by both the principal employer and the trustee that the two triggers must mean something different and that the second trigger must therefore give "not published" a different meaning from the ONS permanently ceasing to publish RPI (with the trustee and employer then arguing for competing interpretations, effectively for RPI and CPI respectively). The judge also rejected the principal employer's argument that, within the context and purpose of the scheme rules, and the fact RPI is now only published (as the judge accepted) solely because the ONS is obliged against its wishes to do so for index-linked gilts purposes, "the general index of retail prices…" should be interpreted to mean the ONS's main index of consumer inflation which is a national statistic, namely CPI or CPIH.

The Court held that the second trigger must have been added in error, and further held that the relevant index in the rules would remain RPI for so long as RPI is published "*for any purpose*".

PASA launches consultation on DB transfers Code of Good Practice

PASA has issued a Consultation on a new Code of Good Practice in respect of defined benefit transfers. The draft Code has the objectives of:

- improving the overall member transfer experience through faster, safe transfers
- improving communications and transparency in the processing of transfers;
- improving the efficiency for administrators (e.g., by using standard forms and templates).

The draft Code contains guidance in relation to processes that should be followed, as well as template transfer documentation and information on settlement processes. ***Whilst the new Code will not be legally binding, it is anticipated that it will be considered as good industry practice in the future, particularly by the Pensions Ombudsman in the context of transfer complaints.***

It was originally anticipated that the previous guidance issued in July 2019 (please see our July 2019 Update for more detail), which focused on what was defined as a "standard" transfer case, would form the first part of two-part guidance (with the second part covering "non-standard" cases). However, it was subsequently agreed that a Code of Good Practice would be created to cover all DB transfer scenarios and that the industry would be consulted with respect to the draft Code in advance of its publication.

Responses to the Consultation should be made before 30 April 2020, and it is currently expected that the new Code will be effective from 1 September 2020.

Brexit: Regulator issues guidance for trustees on preparing for the end of the transitional period

The Regulator has outlined areas that trustees of occupational DB and DC pension schemes should focus on during the transition period (i.e., the period between the UK's exit from the EU on 31 January and 31 December 2020). Many of the areas highlighted, such as investment, employer covenant, operational/administration and member communications are consistent with previous guidance from the Regulator and will probably have been on trustees' radars for some time. Trustees may, however, wish to check that their planning to date has covered off all the points flagged by the Regulator.

The information can be found here.

Two new professional trustee accreditation systems launched

We reported in our March 2019 Update about the proposed launch of new standards for professional trustees by the Association of Professional Pension Trustees (APPT) and noted that the associated

accreditation framework would be launching later last year. However, the original timing of the launch was delayed. It has now been reported that this will be launched in April this year.

Separately, the Pensions Management Institute (PMI) has confirmed details of its new accreditation programme, which will be called "APTitude". Applications for this programme will be open from 24 February 2020.

Regulator confirms its approach to CVAs

The Regulator has issued its Regulatory intervention report in relation to Arcadia Group Limited (AGL) which sets out what is expected of employers in company voluntary arrangement (CVA) scenarios.

AGL sponsored two defined benefit pension plans, which were creditors in the CVA. The Regulator was involved at an early stage (as it expects to be) in considering the CVA with the employers, trustees and Pension Protection Fund (which obtains a vote in a CVA where a plan is eligible for entry), and the Regulator concludes that a positive outcome for the plans and their members was achieved.

The Regulator confirmed that it will take a principled approach to considering the merits or otherwise of a CVA proposal.The report states that "*the circumstances in which CVAs are proposed may be similar to those where a regulated apportionment arrangement (RAA) may otherwise be sought. In such a case, we will assess the CVA proposal in line with the principles listed in our 2010 statement on RAAs.*"

The RAA criteria are as follows:

- whether insolvency of the employer would be otherwise inevitable
- whether the plan may receive more from an insolvency
- whether a better outcome may be obtained for plan members by other means, including use of the Regulator's powers
- the position of the remainder of the employer group, where there is a group; and
- the outcome of the proposals for other creditors.

The Regulator went on to confirm that it considered this scenario was one where it was appropriate to apply its RAA criteria, even though no RAA was proposed. This is a helpful confirmation of the Regulator's approach for employers or trustees facing a CVA scenario.

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