Technical Connection

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7 Staple Inn, London, WC1V 7QH.
Tel: 020 7405 1600 Fax: 020 7405 1601
E-mail: enquiries@technicalconnection.co.uk
www.techlink.co.uk

FINANCE BILL 2012 MISCELLANY

- Legislation will be included in the Finance Bill 2012 so that for the tax year commencing 6 April 2015 and subsequent years the automatic increase in the nil rate band (NRB) will be based on changes in the Consumer Prices Index (CPI) over the year to the previous September. The result of this automatic calculation will be rounded up to the nearest £1,000.

  Automatic indexation by reference to the CPI will start from tax year 2015/16 (based on the increase in the CPI for the 12 months to September 2014).

  Automatic indexation of the NRB may still be overridden for a tax year if Parliament sets a different figure. In the meantime, the NRB will remain frozen at its current rate of £325,000 up to and including 2014/15.

- From 6 April 2012 interest or similar amounts payable by building societies, banks and other deposit-takers on investments that are qualifying time deposits (basically non-transferable fixed deposits of £50,000 or more which are repayable at the end of a specified period of not more than five years) will be paid net of basic rate tax rather than gross.

  Those not liable for tax will still be able to make a declaration and receive gross interest. Companies will continue to receive their interest gross as the deduction at source rules do not apply to them.

- Legislation will be introduced in Finance Bill 2012 to allow for the capital gains tax annual exempt amount to rise in line with the Consumer Prices Index (CPI) instead of the Retail Prices Index from 2013/14. Automatic indexation of the annual exempt amount using the CPI will still be subject to override if Parliament determines a different amount should apply. The legislation will also set the annual exempt amount for 2012/13, keeping it at the 2011/12 level of £10,600.

HMRC TIGHTENS THE QROPS RULES

The Government has announced its intention to introduce new legislation, effective from 6 April 2012, that will strengthen the information and reporting requirements for QROPS to ensure better compliance with the pension tax regime and deter misuse.

HMRC says in an explanatory note to the draft legislation that "QROPS were designed to allow those who are leaving the UK to take their pension savings with them to their new country of residence and provide an income in retirement there. It was intended to be a way of continuing pension saving rather than a method of converting existing pension saving into a lump sum or of escaping taxation on pension savings."

The Government has found that "QROPS are being marketed extensively as a way of paying amounts or enabling the payment of amounts that are not allowed under UK rules (in particular 100% lump sums) once the UK tax rules no longer apply". HMRC states that this "is contrary to the policy rationale for allowing transfers of UK tax-relieved pension savings to be made free of UK tax to QROPS".

As a result, the draft regulations amend a number of the existing regulations on the operation of QROPS. The draft regulations seek "to tackle attempts to manipulate the rules, while maintaining a workable system of transfers for those who are using the system as intended."

One very significant change is in the conditions that a pension scheme must meet to be an 'overseas pension scheme', which is the first step in a scheme satisfying the conditions to be a QROPS. This now provides that for a scheme to be regarded as an 'overseas pension scheme' that where an exemption from tax in respect of benefits paid from the scheme is available to a member of a scheme who is not resident in the country/territory in which the scheme is established, the same exemption must also be available to a member who is resident in the country/territory. This new requirement is imposed as exemptions in such schemes had 'been used to promote transfers for tax rather than pension saving purposes'.
Subsequently, HMRC issued detailed guidance on:

- The requirements to be regarded as an 'overseas pension scheme'
- The requirements to be regarded as a 'recognised overseas pension scheme'
- The requirements to be a QROPS
- The way in which a scheme can submit a QROPS notification to HMRC
- The production of the list of QROPS schemes and the inclusion, removal or suspension of schemes from that list.
- The process of transferring from a registered pension scheme to a QROPS

- The information that a QROPS must provide to HMRC and the further information it may be required to provide to HMRC.

TEST-ACHATS AND UNISEX RATES

The Treasury has published a consultation document on the UK response to the Test-Achats case

Just over nine months ago the European Court of Justice (ECJ) handed down its decision in the Test-Achats case on sex discrimination and insurance premiums. The Treasury has now issued a consultation paper and draft regulations making the relevant amendments to the Equality Act 2010.

Amongst other things, the consultation paper reiterates the Government's legal interpretation that the judgment applies only to new contracts entered into after 21 December 2012, so existing contracts are not affected. The paper notes that 'the usual principles of contract law, as applied by the courts in the field of insurance, will determine when a new contract has been formed'.

PENSION UNLOCKING SCHEME RULED UNLAWFUL

Over the last year or so a number of firms have been promoting 'pension reciprocation' schemes that are designed to enable their members to obtain a loan of up to 50% of the scheme funds before age 55. Many concerns had been raised regarding such arrangements, including a warning from the FSA.

On 31 May 2011 Dalriada Trustees Limited, a professional trustee company, was appointed as a trustee of 13 pension schemes (generally described as the 'Ark Pension Schemes'). It was appointed by the Pensions Regulator following the Regulator's concern over the 'Pension Reciprocation Plan' business model. Although the appointment did not remove the existing trustees, under the appointment Dalriada Trustees Limited is entitled to exercise all the powers of the trustees to the exclusion of the other trustees (Pensions Act 1995 s 8(4)) - effectively it therefore acts as a sole trustee in this matter.
Following its appointment, Dalriada Trustees obtained a freezing order banning the disbursement of scheme funds pending a review of the legality of the pension reciprocation process. It then brought a High Court case regarding 6 of the Ark schemes to determine this.

The High Court, in the Dalriada Trustees Limited case, ruled that the use of 'Maximising Pension Value Arrangements'(MVPA) under the 'Pension Reciprocation Plan'(PRP) under six schemes operated by Ark Business Consulting will result in the members concerned being subject to unauthorised payment charges.

The PRP was conceived as a way of getting members access to their pension capital prior to retirement without breaching HMRC rules. It operates as follows:

1) An individual (Member A) with a pension "pot" in another, unrelated pension scheme is introduced to one of the Schemes (Scheme Y).

2) Member A obtains a transfer of his benefits from his original pension scheme to Scheme Y.

3) A 5% "standard fee" from the transfer sum is paid to the promoters of the PRP, and the remaining 95% of Member A's transfer value is used as follows:

   a) Up to 50% of Member A's funds in Scheme Y is 'lent' to a member (Member B) of one of the other Schemes (Scheme Z) under an MPVA 'loan'.

   b) A reciprocal MPVA 'loan' of equal value is then made by Scheme Z to Member A, using Member B's funds.

   c) The remaining funds of both schemes are then invested in other assets.

The principal question raised was whether those MPVA 'loans' were made pursuant to valid exercises of the schemes' respective powers of investment or whether they were invalidly made and thus void.

The judgement by Mr Justice Bean hinged on the interpretations of sections 164 and 173 of the Finance Act 2004. He believed that section 173 is decisive in confirming that unauthorised member payments will apply and indicates the following:

“Taking the example given above, when Scheme Y (of which A is a member) makes an MPVA payment to B (the member of scheme Z), it does so in the sure and certain hope that a corresponding payment is going to be made by Scheme Z to A; the payment to B "is used to provide" a benefit to A; and, on receiving that benefit in the form of the loan from Scheme Z, A is to be treated as having received an unauthorised payment. The wording "is used to provide" rather than "provides" clearly indicates that indirect causation is sufficient.

I do not accept that any lack of precise matching between the two payments makes a difference. The PRP, as its name suggests, was established for the purpose of reciprocation. As the explanation of the PRP concept exhibited to one witness statement frankly states, "Member A is unable to access cash in existing arrangement due to Finance Act 2004 restrictions. Member A is motivated to make transfer (as advised by the introducer) to enjoy access to an **equivalent reciprocal sum** from Member B MPVA. The same considerations apply to Member B." [emphasis added]

If member A pays an amount of £50,000 (half his total investment of £100,000: see above) into Scheme Y with a view to obtaining an MPVA loan of £50,000, it is of no importance to him whether his £50,000 goes to fund a single loan to B, or is divided between several members of Scheme Z; nor whether the £50,000 which will come to him derives only from B or from several members of Scheme Z. The outcome is the same. His £50,000 is used to provide him, albeit indirectly, with a benefit, namely access to half his pension fund before his retirement, and with no strings attached except an obligation to repay £87,500 in 25 years' time.
The Court found that the person liable to the unauthorised payment charge under s 208(2) is the recipient of the payment.

The Court also found that the MVPA loans were not ‘investments’ but instead characterised them as ‘disinvestment’. The MPVA loans were accordingly outside the scope of the power of investment in the Schemes.

Although this judgement is specific to the Ark Schemes, it is likely to severely curtail the amount of money being transferred to other similar pension unlocking arrangements.

While HMRC declined to be a party in this case it could consider using its powers to de-register such schemes where the unauthorised payment charges exceed 25% of the market value of the scheme's assets.

THE SEED ENTERPRISE INVESTMENT SCHEME

The press made much of the Seed Enterprise Investment Scheme (SEIS), which was announced by George Osborne in the Autumn Statement. We now have the draft Finance Bill 2012 clauses, together with a Tax Information and Impact Note about the scheme.

- The maximum total individual investment in SEIS will be £100,000 per tax year with 50% income tax relief given by way of a reduction in the tax otherwise payable by the investor. Relief is available for shares issued between 6 April 2012 and 5 April 2017.

- An eligible SEIS company must:

  - Be no more than two years old;
  - Have 25 or fewer full-time equivalent employees;
  - Have gross assets of not more than £200,000; and
  - May raise no more than £150,000 in total (*not* per tax year).

- A capital gains tax exemption will be available for 2012/13 for individuals who realise gains that are re-invested, wholly or in part, in a SEIS. This is an outright exemption which means that relief of up to 78% (50% + 28%) is potentially available during the scheme's first year. The exemption from CGT is attractive but it could prove difficult to make the necessary reinvestment – time will tell.

COMMENT

Anyone considering investment in a SEIS needs to be aware that the level of tax relief on offer is commensurate with the risk involved in such an investment.

GOVERNMENT CONSULTS ON AUTO ENROLMENT THRESHOLDS

With auto-enrolment due to start in less than 10 months' time, you might have thought that by now all the earnings thresholds for contributions would be in place. Alas for payroll system programmers everywhere, that is not the case.

A review of auto-enrolment commissioned by the incoming coalition government and published in October 2010 recommended that auto-enrolment should not occur until earnings matched the personal allowance, but that once this threshold was passed contributions should be based on earnings between the Primary (employee) NIC threshold (PCT) (£5,715 in 2010/11) and £38,185 (the 2006/07 UEL revalued in line with earnings). The government said it accepted all the points in the review, while at virtually the same time announcing a jump in the PCT. However, it did legislate for an earnings trigger of £7,475 (in 2011/12 terms) in the Pensions Act 2011.

The Pensions Act 2011 requires the Government to review the automatic enrolment earnings trigger and the lower and upper limits of the qualifying earnings band each tax year.

The DWP has now published a consultation paper on these earnings thresholds. It has looked at adopting PAYE thresholds, indexing the old numbers in line with earnings or revaluing them in line with prices (based on the CPI), and is seeking views on the following proposed thresholds for 2012/13:

- £8,105 for the automatic enrolment earnings trigger, aligning it with the PAYE threshold;
- £5,564 for the lower limit of the qualifying earnings band, aligning it with the NICs Lower Earnings Limit; and
- £39,853 for the upper limit of the qualifying earnings band, which is the Pensions Act 2008 figure of £33,540 revalued in line with earnings.

These thresholds produce a theoretical minimum contribution of £203 a year ([£8,105-£5,564] x 8%), although during the protracted first part of the phasing period the minimum will be only £51 given the 2% overall contribution requirement. The maximum theoretical contribution is £2,743.

COMMENT

These numbers have been a long time coming. Now they are here, it seems unlikely the consultation will meet with much opposition.

CHANGES TO THE SCOTTISH SUCCESSION RULES

The prior right of the spouse to the matrimonial home is to increase from £300,000 to £473,000 from February 2012

Under Scots law when a person dies intestate the surviving spouse or civil partner has "prior rights" to the estate, the most important of which is the right to the deceased's interest in the matrimonial home up to the value of £300,000. If the value of the house exceeds £300,000 the surviving spouse/civil partner is entitled to a lump sum of £300,000 in place of the house.

The Scottish Government plans to raise the threshold from £300,000 to £473,000 from February 2012 to reflect the increase in property values since it was last increased in 2005. This will be done by an amendment to the Succession (Scotland) Act 1964.

Another proposed change will allow more people to deal with small estates without incurring heavy legal costs. A sheriff clerk will be able to prepare an inventory and declaration to finalise an estate when it is worth less than £36,000 – up from the current figure of £30,000.

COMMENT

Of course, the prior rights only come into play in the event of intestacy and so the importance of making a Will should, as always, be emphasised. It should also be remembered that certain fixed rights of spouses and children exist under Scots law regardless of whether there is a valid Will or not – these are the "legal rights" that apply to movable property.

ABI CONSULTS ON ANNUITY CODE OF CONDUCT

The ABI is consulting on a proposed compulsory Code of Conduct for its members, which is designed to further encourage the take up of the open market option. This new Code of Conduct will apply where ABI members are writing to members of money purchase schemes who are approaching their retirement date. This is designed to encourage more retiring members of such schemes to take advantage of the open market option (OMO).

ABI figures show that increasing numbers of consumers are buying an annuity from a provider which is not their pension provider (44.4% in the second quarter of 2011, compared to 35.9% in the same quarter of 2009), and about 70% of people shop around, that is, consider switching provider.

The ABI identified customer inertia as one of the key reasons why people fail to shop around. It indicated that "many consumers currently receive an application form for an annuity from their existing provider as part of the communication pack posted to them in the run-up to their retirement date. Many simply complete and sign the application form and send it back to their existing provider, rather than shop around for a better deal."

It was as a result of this that the ABI announced it would introduce, in the first quarter of 2012, a compulsory Code of Conduct binding all ABI members. Under the Code, ABI members will remove the annuity application form from the communications they send to their customers. This will stop consumers from automatically rolling over their pension savings to an annuity with their current provider. The new Code will also ensure that customers receive all the information they need to shop around in one easily accessible place.

The ABI has now issued a consultation on a draft Code of Conduct that goes beyond its earlier announcement in the following three respects:

- All communications by providers, whether written, on-line or over the telephone, must take consumers through a clear customer journey covering the three key steps of understanding retirement, understanding the different ways of taking retirement income and understanding how to buy. Written communications must also include a standardised heading on the first page about the benefits of shopping around.

- Illustrations provided by the provider which have not been requested by the customer must follow rigorous rules to ensure the options are comparable, and include a clear statement about the higher income available from enhanced annuities based on lifestyle or medical conditions, where providers do not offer or illustrate them.

- Providers' sales processes must take customers through the key questions they should consider in order to buy the appropriate product, and alert them where they are not offering an enhanced annuity.

In view of the many changes to communications and processes that will be required by the Code, ABI members will be given one year from the publication of the finalised Code to make the necessary changes.

SHORT SERVICE REFUNDS TO BE ABOLISHED AND CONSULTATION ON TRANSFERRING SMALL PENSION POTS

The Government has announced its intention to bring in legislation to abolish refunds of member contributions where a member leaves a DC occupational scheme having completed less than two years' pensionable service. The short service refund rules for DB schemes, the largest provider of which in terms of active members is the Government, will remain unchanged.

The preservation legislation in the Pensions Act 1993 will be amended so that a member of a DC occupational scheme will have automatic vested rights from the date that contributions are first paid to the scheme. However, this change will not override the right to a refund arising from a worker's right to opt out of an automatic enrolment scheme.

The Government has felt the need to make this change to ensure that employers are not influenced by the current preservation rules in choosing their qualifying scheme for automatic enrolment purposes.

It is anticipated that this change will be effective from 2014, provided an accompanying solution for the transfer of small pension pots can be introduced at the same time. Accordingly, the Government has also issued a consultation on the following three possible options to enable individuals to more effectively transfer and keep track of their small pension pots:

- relatively minor changes to the current system to help make member-initiated transfers easier and less expensive;
- an automatic transfer system where small, dormant pension pots can be easily consolidated into an aggregator scheme or schemes with minimal involvement of individuals or employers; and
- a system where small pension pots follow individuals from job to job.

INCOME WITHDRAWAL RATE FOR JANUARY 2012

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in January 2012 is 2.5%.