Technical Connection

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HMRC ONLINE TRUSTS REGISTRATION SERVICE DELAYED

HMRC has announced that its online Trusts Registration Service will not be ready for launch this June as originally intended. The online Trusts Registration Service replaces the paper 41G(Trust) form and the ad hoc process for trustees to notify changes in their circumstances, and will be relevant to any trust that generates 'tax consequences'.

The launch was intended to coincide with the beneficial owner registration requirements of the EU's Fourth Money Laundering Directive (4MLD) - transposed into UK law at the end of June.

The Register will allow HMRC to collect and hold adequate and up-to-date trust information centrally in line with the specific requirements of the 4MLD, and will require any new or existing trust that generates a 'tax consequence' to provide information on the identity of the settlor, the trustee(s), the protector (if any), the beneficiaries (or class of beneficiaries if the trust is a discretionary trust) and any other persons exercising control over the trust; as well as a detailed picture of the assets held. This imposes a more onerous reporting obligation on many trustees who have until now been exempted from the requirement to complete a form 41G(Trust) if there was 'no income arising, and no likelihood of income or gains in the future'. In contrast, the new requirement to register or update trust details online applies in any year that the trust generates a UK tax consequence of

any kind - this could be an income tax, CGT, IHT or SDLT implication.

Trusts that hold collectives will have needed to register under the previous system and for these trusts little more will change other than when and how the information is provided. For trusts that hold no assets other than onshore and/or offshore single premium investment bonds, the new rules will presumably mean that online registration will not be required unless either a chargeable event occurs or a chargeable occasion for IHT occurs. However, the position is not yet entirely clear.

The requirement to register will apply to both onshore and offshore trusts. However, bare trusts, where any tax liability generally arises to the beneficiary rather than to the trust, are excluded from reporting.

Until the Trusts Registration Service is available, HMRC has asked customers to delay notification of new trusts. In the meantime, those completing Trust and Estate Tax Returns have been instructed by HMRC to leave blank the box that asks for confirmation that 'changes to the trust have been updated on the Trust Register', with a view to ensuring that correct details are recorded on the register when it is up and running. Once the Service is operational, trustees will have until October 5 this year to register new taxable trusts, and until January 31 2018 to provide information on existing trusts.

FCA CONSULTATION PAPER: DB TRANSFERS

The FCA has issued a consultation paper proposing changes to how advice is provided on pension transfers involving defined benefit schemes and other safeguarded rights.

Page 33 of "Freedom and choice in pensions", the original consultation paper that accompanied George Osborne's surprise announcement on pension flexibility on 19 March 2014, stated as follows:

"the government recognises that the attractiveness of transferring from defined benefit to defined contribution may increase as a result of the changes to the tax framework for how defined contribution pension savings can be accessed."

The remark has proved something of an understatement, with Mercer estimating that £50bn has been transferred out of final salary pension schemes by 210,000 members since April 2015, when full flexibility came into being.

The Pensions Regulator has given credence to Mercer's figures, saying in response to a Freedom of Information request that "For the period of 1 April 2016 to 31 March 2017 defined benefit pension schemes have, in total, reported 67,700 transfers out of the scheme. However, not all of these schemes have reported how many transfers they carried out. Our estimate is that there were around 80,000 transfers made."

Now, just over three and a quarter years after Mr Osborne's bombshell and the subsequent transfer market boom, the FCA has issued a consultation paper (CP17/16) entitled "Advising on Pension Transfers". The proposals represent a significant overhaul of the current regime, which has its roots in the compulsory Transfer Value Analysis System (TVAS) introduced on 1 January 1995 by LAUTRO as a response to the pensions mis-selling saga.

The FCA's suggested reforms are taking aim at two separate areas:

1. Giving advice and assessing suitability

- The FCA wants "all advice on the transfer and conversion of safeguarded benefits to include a personal recommendation", including a safeguarded right which is a guaranteed annuity rate. The Regulator says it has seen only a "few cases" of advisers claiming they are not giving a personal recommendation. In those instances, the FCA discovered "the advice did not comply with the existing analysis requirements and in many cases is *(sic)* actually a personal recommendation". The main reason for the insistence on a personal recommendation is to stop the Finance Advice Market Review applying to safeguarded transfers.

- The current FCA guidance is that an adviser should start from the assumption that a transfer will be unsuitable. Pension flexibility and rising transfer values has made this stance look increasingly outdated and the FCA is now suggesting that it be replaced with "a statement in the Handbook that for most people retaining safeguarded benefits will likely be in their best interests and guidance that advisers should have regard to this". This wording echoes that of TPR in its Regulatory Guidance: DB to DC transfers and conversions.

- Alongside this watering down of the default view, the Regulator is proposing to strengthen the assessment process by making it clear in making a personal recommendation an adviser

  "should consider the following elements:

  - the client's income needs and expectations and how these can be achieved, the role safeguarded benefits play in providing this income and the impact and risk if a conversion or transfer is made;

  - the specific receiving scheme being recommended following the transfer and the investments being recommended within that scheme to ensure that it is appropriate for the risk profile of the client;

  - the way in which the funds will be accessed, either immediately or in the future, including follow-on arrangements;

  - alternative ways of achieving the client's objectives. For example, there may be ways for a client to provide death benefits which can be funded from income rather than by a lump sum funded by a pension transfer, and which does not carry so much risk; and

  - the relevant wider circumstances of the individual."

  This final point is a piece of back covering, which the FCA says is individual-dependent, but will incorporate such issues as tax, death benefits, state of health and interaction with means-tested benefits.

- Where the adviser does not fulfil the role of the pension transfer specialist and instead uses internal or external support, the responsibilities of that third party are also being more sharply defined. The FCA wants the specialist to be more than a mere TVAS number-checker. It proposes that the specialist must review the reasonableness of the personal recommendation made by the adviser, implying "an independent assessment of the

soundness of the basis for the advice". This would "take into account the client's wider circumstances, including their appetite and capacity for risk and the nature of the scheme being transferred to". The greater scrutiny by the pensions specialist will not move the ultimate responsibility for advice from the adviser dealing with the client, although it potentially increases the liability of the specialist to the adviser.

Where an external pension transfer specialist firm takes on the complete role of giving transfer advice to the client and the referring adviser's firm focuses on investment of the transferred funds, the FCA says both firms must be able to demonstrate the advice they give is suitable for the client.

2. Transfer value analysis (TVA)

- The FCA acknowledges that "The current form of TVA has essentially stayed unchanged since additional requirements for pension transfers were introduced". The Regulator also accepts several of the criticisms that have long been made about TVAs, such as the annuity focus, the unsuitability for those close to retirement and the poor public understanding of the critical yield concept, despite its existence for more than 20 years.

  The proposed solution starts by rebranding TVA as APTA – appropriate pension transfer analysis.

- The APTA will include, "*as a minimum*:

  - an assessment of the client's outgoings and therefore potential income needs throughout retirement;

  - the role of the ceding and receiving scheme in meeting those income needs, in addition to any other means available to the client – effectively obtaining an understanding of the client's potential cashflows;

  - consideration of death benefits on a fair basis, for example where the death benefit in the receiving scheme will take the form of a lump sum, then the death benefits in the ceding scheme should also be assessed on a capitalised basis, and both should take account of expected differences over time; and

  - 'the prescribed comparator'."

  Except for the prescribed comparator (see below), many existing TVAS systems already produce a detailed analysis which would more than satisfy the FCA's proposed minimum requirements. It is virtually impossible otherwise to demonstrate and compare the use of pensions flexibility.

  The FCA wants the APTA to take account of the client's risk appetite and ability to manage investments when assessing the possible benefits from a potentially suitable receiving scheme. This is to include scenarios where the plan is to withdraw transferred funds for reinvestment outside the pension environment.

- The prescribed comparator is likely to prove the most controversial part of the FCA's proposals. It starts by following the current TVAS approach in valuing the transferring scheme's projected benefits at the chosen retirement date on an annuity basis. However, whereas the TVA uses an interest rate that is averaged over 12 months, the APTA will take a

current rate. The removal of the 12 month averaging will mean sharp index-linked gilt market movements have an immediate effect, rather than get smothered, as happened in the second half of last year.

Once the annuitised value of benefits has been calculated, this must be discounted back to the present day if the retirement date is 12 months or more distant. The current TVAS effectively calculates a discount rate using the Cash Equivalent Transfer Value (CETV), and that rate becomes the critical yield. Under APTA the calculation becomes reversed and the adviser "must determine an appropriate discount rate to value the amount needed to reproduce the safeguarded benefits, after appropriate charges". The FCA wants this rate to be appropriate to the client, "based on their attitude to risk, irrespective of whether the proposed receiving scheme will involve flexi-access drawdown or an annuity". There is a clear guidance that the FCA does not expect the rate (before charges) to exceed the intermediate rate of growth shown on a corresponding KFI for the receiving scheme (normally 5%).

The difference between the calculated value using the adviser-selected discount rate and the actual transfer value must be shown in a prescribed format with a block graph and a framed statement:

> It could cost you £X to obtain a comparable level of income on the open market.
>
> This means the same retirement income could cost you £(X – CETV) more by transferring.

In CP17/16 an example is given where X is £140,000 and the CETV is £120,000, implying a £20,000 shortfall. This is not unrealistic given the differing assumptions that will apply between the largely gilt-driven FCA calculation basis and the "best estimate" CETV principle required by SI 2006/33.

Under the heading of "Areas for discussion", the FCA also address overseas transfers, although it does not make specific proposals. It notes that the APTA requirements "are likely to result in a more complex analysis having to be undertaken for an overseas transfer than for a transfer to a UK DC arrangement". For example, the FCA says that "…firms must ensure that the APTA contains sufficient information in order to be able to compare financial and tax regimes in two countries", a requirement which may result in the involvement of advisers in each country concerned or even two stage transfers (ie DB to PPP, then PPP to QROPS).

The consultation period will run for three months, with the FCA currently saying final rules will emerge "by early 2018".

COMMENT

In many respects, the FCA's proposals are no more than bringing the regulatory environment in line with what the market is already largely doing. Advisers that already have a robust transfer process in place will generally have no major concerns about the FCA proposals. The one key initiative that will have greater ramifications for all advisers is the transfer comparator. Explaining the shortfall between discounted value and transfer value will be a challenge.

THE QUEEN'S SPEECH AND BEYOND – CONSOLIDATED LATEST POSITION

The Queen's Speech was significant as much for what it did *not* contain as for its predictable (and weighty) Brexit content.

The Queen's Speech, delivered on 21 June, was not the grand event that might have been expected. To quote the Parliament website, the State Opening of Parliament took place with 'reduced ceremonial elements…due to the unique circumstances of the general election'.

The Speech lasted just nine minutes, yet was designed to cover the next two years of legislation – if the government survives that long. The doubled (theoretical) length of the parliamentary session is a direct consequence of the raft of Brexit-related legislation that needs to be in force by 29 March 2019 (EU exit date). Meeting this timetable promises to be extremely challenging.

As far as legislation relevant to the financial services industry is concerned, you will hunt in vain in the Queen's Speech for any of the proposals contained in the Conservative Manifesto:

- The word 'pension' did not pass the Queen's lips, so we can assume the Triple Lock and Winter Fuel Allowance stay in place. There was no mention of (BHS-inspired) legislation protecting pensions during company sales or mergers.

- The statement that the government "will seek to enhance rights and protections in the modern workplace" is little more than an acknowledgement that there will be a response to the Taylor report. However, press reports suggest its publication has been put on hold while the government considers its position.

- On social care, the Speech offered only a promise to "bring forward proposals for consultation." As the Dilnot capped regime for care costs is not due to begin until April 2020, there is still time for it to be culled.

There was no comment about Budget timing in the Speech, although the Chancellor had used the Andrew Marr Show to confirm that there will be no Summer Budget. Mr Hammond said "…there's not going to be a sort of summer budget or anything like that, there will be a regular budget in November as we had always planned, and in that budget we will set out our future plans for public spending, for taxation, for fiscal balance and everything else that needs to be clear."

The Chancellor's promise that there would not be "anything like that" was subsequently contradicted by a few lines in the 82 pages of background notes issued by No 10 to accompany the two pages of Queen's Speech. Hidden on page 16 of these copious notes under the heading of "Other Measures" is the following:

'The [two-year parliamentary] programme will also include *three* [our italics] Finance Bills to implement budget decisions. Summer Finance Bill 2017 will include a range of tax measures including those to tackle avoidance.'

The prospect of a Summer Finance Bill raises two questions:

1. When does Summer end? Governments are prone to elasticate seasons to suit their circumstances - witness the timings of some Autumn Statements. The parliamentary timetable announced before the House of Commons was dissolved has the [genuinely seasonal] Summer recess running from 20 July to 5 September 2017. In past years the post-Summer sitting has lasted only ten calendar days before the House shuts up shop for nearly four weeks because Conference Season has arrived. In 2016, that meant the House rose on 15 September and business did not resume until 10 October.

   On the face of it a new Summer Finance Bill, introduced before the Summer recess, would have very limited time to debate if the aim was for it to attain Royal Assent by 20 July. Thanks to the recesses, it would not have much more debating time if the Royal Assent goal was mid-October.

2. What would be in the Summer Finance Bill? The material culled from the Finance (No. 2) Bill 2017 was the contentious content. In theory, a Summer Finance Bill could run to over 600 pages, based on the difference between the Finance (No. 2) Bill 2017 (776 pages) and the eventual Finance Act 2017 (155 pages). Would the government try to reinstate all the abandoned legislation and, if Royal Assent by July 20 is the goal, rush it through? In the current political climate trying to push through Making Tax Digital (to mention just one of the dropped items) without detailed parliamentary scrutiny might well be difficult.

COMMENT

The legislative situation remains unclear on the "lost" Finance Bill measures. Alas, the promise of a Summer Finance Bill does little to clarify matters for now.

THE FCA CONSIDERS TURNING OFF PRE-RDR TRAIL COMMISSION

The Financial Conduct Authority (FCA) is considering whether it is possible to turn off all trail commission paid to advisers from legacy products.

Although the retail distribution review (RDR) banned the payment of trail commission on new products when the changes came into effect at the end of 2012, if a client invested in a fund before that deadline advisers can still receive trail commission.

In a consultation paper published alongside its asset management study the FCA said it was looking at whether it was possible to 'switch off' trail commission for legacy products.

The interim report found that the 21 asset management firms surveyed paid £1.4 billion in commission in 2014 and the Regulator said the interim report of its asset management study found that some people were paying more to invest because they were in pre-RDR products.

The FCA has therefore asked advisers about the impact of banning all trail commission over a period of time. It added it would look at legacy trail commission paid on personal pension and life assurance products as well.

THE FCA PUSHES BACK ON THE RETAIL DISTRIBUTION REVIEW

FCA has pushed back a review of the impact of the retail distribution review (RDR) from 2017 to 2019. The RDR was due to be the second part of the Regulator's research into reforms introduced at the end of 2012.

In a paper published on 30 June the Regulator said it would now delay this review and combine it with a planned analysis of the Financial Advice Market Review (FAMR) in 2019.

The FCA said the delay will allow the market time to react to the regulatory change from both FAMR and MiFID II, and will allow the FCA to use its resources more efficiently and minimise the reporting burden on firms. It added a 2019 review will allow the FCA to draw on five years of evidence.

The first review of RDR was published in 2014. Its main finding was that there was little evidence of an 'advice gap' caused by the new rules.

Following this initial review the Regulator said it would undertake another intermediate stage review in 2017 to understand any further impacts of RDR. However, this has now been delayed to 2019.

As part of the 2019 review the FCA will consider the impact of FAMR changes as well as the RDR. It has identified accessibility, affordability and quality of advice as the three themes it will track annually to measure the development and strength of the advice market.

To reach these baseline findings the FCA asked 13,000 people in the UK about their attitude to financial advice. The baseline findings will be used as a benchmark to assess the outcomes of FAMR when conducting the review in 2019.

INCOME WITHDRAWAL RATE FOR JULY 2017

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 July 2017 is 1.5%.