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Briefing note

May 2016

1. New corporate law disclosure requirements apply from 6 April

New requirements came into force on 6 April which mean that most UK incorporated companies and LLPs will need to keep a register of people and legal entities that own or control them.

Key issues

1. New corporate law disclosure requirements
2. "Brexit"
3. EIOPA drops plans for solvency-based funding regime
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Who is subject to these requirements?

- All UK incorporated companies (apart from exempt companies) and LLPs incorporated under the Limited Liability Partnerships Act 2000.
- The exemptions broadly cover publicly listed companies (e.g. those listed on the LSE or AIM) on the basis that they are already subject to disclosure / transparency requirements equivalent to those imposed by the new regime.
- There are no specific exemptions for trustee companies, dormant companies or wholly-owned subsidiaries. Pension schemes with UK incorporated corporate trustees will therefore be affected and must comply with the new requirements

What are the requirements?

The requirement is to maintain a register which lists both "persons with significant control" (or '**PSCs**') and "relevant legal entities" (or '**RLEs**').

Very broadly:

- A PSC of a company covers an individual who holds (directly or indirectly) more than 25% of the company's shares or voting rights; or holds the right (directly or indirectly) to appoint or remove a majority of the company's directors; or has the right to exercise/actually exercises significant influence or control over the company. A PSC is always an individual.
- A RLE is a legal entity which would be a PSC if it were an individual and is subject to its own disclosure requirements (either because it is itself required to keep a PSC register or is subject to equivalent disclosure/transparency obligations).

Not all PSCs and RLEs have to be listed on the register. The requirements are quite complex, but, broadly, they mean that in practice, subsidiary companies will not usually have to register entities above their immediate parent company in the chain, assuming that parent company itself keeps a PSC register (or is exempt from the requirements).

What's the timeframe for compliance?

- The requirement to maintain a PSC register came into force on 6 April. There is no set format for this register (other than that it must contain the prescribed information). The PSC register is kept internally but must be made available for inspection upon request.
- **A PSC register must never be empty**:
  - If an entity subject to the requirements has no PSCs

or RLEs, this must be stated on the register.

- For those who were not in a position to enter details in a PSC register on 6 April (e.g. because investigations were still ongoing to determine who needs to be registered), it is permissible to insert holding wording in the register. This must follow prescribed wording.

- The information on the PSC register must also be filed with Companies House as part of the annual confirmation statement (which will replace the annual return) from 30 June 2016 onwards.

Non-compliance with these requirements is a criminal offence.

Action needed

UK incorporated corporate trustees of pension schemes need to maintain a PSC register from 6 April.

The new requirements are not particularly onerous (and for most corporate trustees, it's likely the register only needs to list the trustee's immediate parent company).

In practice, pension trustee companies are often subsidiaries within a wider corporate group (typically that of the employer), in which case it's likely the wider group has already identified those group companies subject to the PSC requirements (including the corporate trustee) and put in place the necessary registers.

However, corporate trustees should be aware of the new requirements and check with the wider group to ensure their PSC register is in place.

For more detailed information about the new PSC requirements, please see our briefing paper accessible at the following link: http://www.cliffordchance.com/briefings/2016/03/the_psc_registerrequirementsapracticalguid0.html

2. What would a "Brexit" mean for UK pensions?

On 23 June, a referendum will take place concerning the UK's continued membership of the EU.

If the UK were to leave the EU ("**Brexit**"), what would the impact be for UK pensions? Whilst not possible to answer this question with any real certainty, many in the industry have been speculating over what the consequences could be.

Whilst much of current pensions legislation and case law is domestic in origination, some of it does have EU roots. For example, law on discrimination and equal treatment, scheme funding and the Transfer of Undertakings – Protection of Employment (TUPE); which although now enshrined in UK law, originally derived from Europe.

In theory, following a "Brexit", it would follow that the UK would be free to depart from these aspects of pensions law if no longer bound by EU law. However, this would require the relevant UK legislation to be repealed first – something which is perhaps unlikely, particularly given that much of this law provides protection for pension scheme members.

Notwithstanding this, it is certainly possible that, over time, some aspects of UK pensions legislation and practices which flow from EU law could move away from the EU position following a Brexit. For example, the proposed requirement to equalise GMPs (which comes from the European Court of Justice case, ***Barber***[1]) might be dropped, as might any additional governance and disclosure requirements imposed by a revised IORP Directive (see further below).

Another relevant consideration on a potential Brexit for defined benefit ("**DB**") schemes would be the impact on the employer's covenant (i.e. the sponsor's ability and willingness to fund its pension scheme), which trustees are required to monitor. If a Brexit were to significantly improve or weaken the employer's covenant, trustees would need to consider whether changes would be needed to the scheme's existing security and funding arrangements. The impact of a potential Brexit on investments would also be important in considering a scheme's investment strategy.

3. EIOPA drops plans for solvency-based funding regime "at this point in time"

The European Insurance and Occupational Pensions Authority ("EIOPA"; the EU pensions regulator) has recently announced that it is ending its work on developing a solvency-based funding regime for pension schemes.

The idea of a solvency-based funding regime is something which has been bubbling along in the background for some time now. The regime would have been based on the Solvency II regime which applies to insurers and would have likely imposed onerous capital adequacy requirements on DB schemes.

In an opinion published on 14 April, EIOPA has concluded that the

introduction of a "one-size-fits-all" solvency regime would not be appropriate and has decided to refrain from introducing harmonised funding or capital requirements at EU level "at this point in time".

The news is likely to be welcomed by many as reports have suggested that a solvency-based funding regime would significantly increase deficits for DB schemes and cause disruption to investments. (Although EIOPA's reference to "at this point in time" should be taken as a cautionary indication that a resurrection of the proposals at some point in the future may not be out of the question).

However, whilst any plans to introduce a solvency-based funding regime have, for now, been dropped, EIOPA has instead recommended the introduction of a European framework for risk assessment and transparency for schemes based on common valuation rules and a standardised risk assessment. The idea is that schemes would need to produce a market-consistent balance sheet (based on the "holistic balance sheet" proposals) and a risk-assessment using a common funding methodology (but schemes would not need to be funded on this basis).

Concerns have already been expressed that this kind of reporting system could lead, at the very least, to confusion, additional (and unnecessary) complexity and increased administration costs and the UK pensions industry may seek to push for a watering down of the proposed requirements.

4. Progress on "IORP II"

In other European pensions news, the revised draft IORP Directive ("IORP II") continues to be considered by the various European institutions and the text will now be debated in "Trilogue" negotiations involving the Council of the European Union, MEPs and the European Commission.

There are still a number of key issues to be resolved, including:

- **Transfers** – proposals that member consent should be required for all pension transfers (both cross-border and domestic), which could essentially prohibit without-consent bulk transfers currently permitted in the UK.
- **Funding** – proposals that the requirement for cross-border schemes to be fully funded at all times be replaced with a requirement for full funding "at the moment" the IORP "starts operating a new or additional scheme".
- **"Fit and proper" requirements** – the European Commission originally proposed that those running an IORP must have professional qualifications. Amendments have been proposed to remove the need for professional qualifications and instead for experience to be "collectively adequate".
- **Pension benefit statements** – a proposal that the Directive set out guiding principles on the information to be included in the annual benefit statement, rather than a prescriptive set of rules.

Subject to the outcome of the UK's referendum on continued EU membership in June (see above), IORP II may cause some problems for UK schemes if the above issues are not resolved. Although, practically speaking, any difficulties caused are likely to be a way off yet – the final text is expected in June, following which member states are expected to have 18 – 24 months to implement the Directive into national law.

5. ESMA publishes list of UK pension arrangements which benefit from derivatives clearing exemption

As reported in the last edition of UK: Pensions Update the European Securities and Markets Authority ("**ESMA**") recently published a number of opinions on the application of the exemption from the derivatives clearing obligation to different types of UK-based pension arrangement. (The obligation derives from The European Market Infrastructure Regulation (648/2012) ("**EMIR**"), which came into force in August 2012 and requires over the counter derivatives to be cleared).

Certain pension scheme arrangements benefit from a transitional exemption (in force until August 2017) which means they do not have to comply with the clearing obligation. While some arrangements automatically benefit from the exemption, others [2] need to obtain prior authorisation. In the UK, this requires a request to be made to the Financial Conduct Authority ("**FCA**"). The FCA must obtain the opinion of the ESMA before making a decision.

As previously reported, on 2 February, the ESMA published a document setting out the opinions it provided to the FCA on the application of the exemption to 16 different types of UK-based pension arrangement. In each case, the ESMA expressed the view that the availability of the exemption is justified. However, at that time, it remained up to the FCA to make the final decision (the FCA is not bound to follow the ESMA's opinion). It seems the FCA has subsequently granted

the exemption in all 16 cases as on 18 February, the ESMA published a list of those arrangements that will benefit from the exemption (covering all those listed in the original opinions).

6. Trustee liability insurance – what's the scope of your cover?

Background: when could insurance be relevant?

If there is a breach of trust, negligence or maladministration, this may give rise to a claim by a member or beneficiary to the Pensions Ombudsman and/or an additional liability for the scheme. In some circumstances, the pension scheme trustees could become personally liable.

Employers and trustees may look to insure against these risks, but may wish to consider exactly what such insurance covers. Most policies will cover trustee personal liability, but such liability is extremely rare due to the various trustee protections available (see below) and some sponsors and trustees may wish to consider whether further cover would be preferable.

What protections are there for trustees and trustee directors?

- **Protections under the scheme trust deed and rules**: typically these comprise exoneration and indemnity clauses.
  - Exoneration clauses effectively prevent liability to members and beneficiaries from arising (although they cannot exclude trustee liability to third parties and are also subject to limits e.g. will usually not protect against fraud, dishonesty or deliberate breaches of trust, nor can they cover fines, penalties or liabilities from negligence in making investment decisions).
  - Indemnities protect from the financial consequences of liability rather than from liability itself. Usually they offer protection where the trustees have liability to third parties (e.g. in respect of professional advisers' fees).
- **The corporate veil**: corporate trustees benefit from a layer of protection afforded by the "corporate veil". This is because it is the trustee company which directly owes duties to scheme members and would be liable for a breach of trust – the individual directors do not owe a direct duty to members. This is far from complete protection, but is generally considered to offer some additional comfort.
- **Statutory protection**: a court can excuse a trustee from liability where they have acted honestly and reasonably. However, this is very limited and as a result, many schemes provide some form of express protection for their trustees.

Scope of Insurance

As noted above, personal liability is rare, but some insurance terms will go further than this and cover additional amounts payable due to a breach, whether the trustees are personally liable or not. Clearly, whether employers and trustees see significant value in this will vary from scheme to scheme, but they may wish to check the exact terms of any cover in place.

7. Ban on member-borne commission effective from 6 April

As reported in our December edition of UK: Pensions Update, the Department for Work and Pensions ("**DWP**") previously consulted on a proposal to ban member-borne commission payments in occupational schemes which provide money purchase benefits and which are being used as qualifying schemes for auto-enrolment (so-called "specified schemes").

The consultation closed in November and the DWP has since published its response and consulted on regulations to implement the ban. The regulations *(the Occupational Pension Schemes (Charges and Governance) (Amendment) Regulations 2016*)) came into force on 6 April 2016.

The ban operates to prevent a charge being imposed on a member of a specified scheme that is used directly or indirectly to pay an "adviser", or to reimburse the "service provider" for a payment the service provider has made to an adviser.

- **"service provider"** is defined as a person who provides an administration service directly to the trustees of a specified scheme.
- **"adviser"** is defined as a person who provides advice/services[3] to the member's employer/former employer or to a member.

The new regulations allow members to opt-in to advice/services and have the cost met by their fund, but they must enter into an agreement with the service provider and this must meet certain conditions. Namely, the agreement must:

- be in writing;

- describe the advice/service being provided;
- state the cost of the advice/service;
- make clear that entering into the agreement is not a condition of scheme membership;
- be entered into before the charge is applied to the member's fund.

A signed copy must also be given to the service provider and the trustees.

Both trustees and service providers will have a role – the service provider has the main duty of ensuring compliance with the ban, but trustees are required to notify the service provider that the scheme is subject to the ban.

The ban currently only applies to new commission arrangements entered into on or after 6 April 2016 (or old arrangements which are varied or renewed after this). However, as originally envisaged, the DWP is going to consult later in the year on regulations to extend the ban to existing arrangements.

8. Statutory modification power introduced to help with GMP revaluation issue on abolition of contracting-out

Scheme trustees and employers will be well aware of the abolition of contracting-out, which has been looming for some time and finally took place on 6 April 2016.

Preparations for the end of contracting-out had thrown up a number of issues along the way, including a technical issue on GMP revaluation.

Very broadly, prior to the abolition of contracting-out, GMPs had been revalued until the date a member leaves *contracted-out service* in accordance with the section 148 method. On leaving contracted-out service, a scheme could (if its rules permit) then choose whether to switch to fixed rate revaluation. Whilst clear that the Government's intention was not to trigger this switch for those ceasing contracted-out service on 6 April (with any switch for these members intended to happen when subsequently leaving pensionable service), the new legislation is not overriding and most scheme rules provide for the switch to happen when leaving contracted-out service (reflecting the pre-6 April 2016 statutory position). For more detail on this issue, please see the last edition of UK: Pensions Update.

The pensions industry raised this with the DWP and it was recently confirmed that a new statutory modification power would be introduced. Legislation introducing this power came into force on 6 April.

Broadly speaking, this new power allows trustees to pass a resolution before April 2017 to modify scheme rules to bring them in line with the new legislation. Resolutions can have backdated effect to 6 April 2016 and the new regulations also mean schemes will not be required to consult with employees before making the change.

This power will be useful for schemes which use fixed rate revaluation and without the power would be unable to amend their rules due to restrictive scheme amendment powers.

9. Key announcements from the 2016 Budget – introduction of the LISA

On 16th March, the Budget was delivered and along with it came a number of pensions-related announcements.

Perhaps of most significance was the Government's acknowledgment of its consultation on potential reforms to pensions tax-relief. There had been much speculation about whether the Chancellor would announce a radical change to the current system (either in the form of a move to a taxed-exempt-exempt system, or perhaps a move to a flat rate of tax-relief for all). However, following on from the Budget, it appears that the existing system will continue, at least for now – with the Chancellor noting that over the past year, the Government has consulted widely on whether to make compulsory changes to the pensions tax system "*but it was clear there is no consensus*". (We would note, however, that the Government has not published a formal response to the consultation paper.)

Instead, what has been described as the Chancellor's "different answer" to the problem that people are not saving enough is the new "Lifetime ISA" (or 'LISA') which is intended to be introduced from April 2017.

Key points about the new LISA

Exact details of how the LISA will operate still need to be finalised, but the key principles are as follows:

- Anyone aged between 18 and 40 will be able to open a LISA.
- For every £4 saved, the Government will provide a bonus top-up of £1 (i.e. 25%) with a maximum annual bonus of £1,000 if £4,000 is saved. These bonuses will be paid on any contributions made before age 50 and bonuses will be paid into the LISA at the end of each tax year.

- The savings and the bonus can then be used:
  - towards a deposit on a first home worth up to £450,000 (existing Help to Buy ISAs can be rolled into the new LISA); and/or
  - after age 60 for any purpose (partial withdrawals also allowed).
- If money is withdrawn before age 60 (and not put towards a first home), the Government bonus (and any interest or growth on this) will be lost. There will also be a 5% charge payable.
- Where people are diagnosed with terminal ill health, they will be able to withdraw all of the funds (including the bonus) tax-free regardless of their age.
- The Government is going to consult on whether there should be flexibility to borrow funds from the LISA without incurring a charge if they are fully repaid. It's also going to consider whether there are any other life events on which savers should be able to access the contributions and bonus.
- Further details will be announced after the Government has engaged with the industry and legislation to enact the LISA is being targeted for autumn.

It remains to be seen whether the LISA is truly intended to be an addition to traditional pension saving, or whether it marks the first step in a transition to a wider reform of pensions tax-relief.

It will also be interesting to see how the LISA is intended to interact with auto-enrolment. The DWP recently re-opened an enquiry into auto-enrolment due to concerns that the new LISA risks undermining the regime if workers opt-out of their employer's scheme to save into a LISA without a proper understanding of what this means (in particular, losing out on the employer's contributions, unless these can be redirected to the LISA).

10. Other Budget announcements

Other key pensions announcements from March's Budget include:

- **Salary sacrifice arrangements**: the Government previously expressed concerns about the growing use of salary sacrifice arrangements and their cost to the taxpayer. In last year's Summer Budget, it was confirmed the Government would be "actively monitoring" them. Concerns were expressed once more in the Autumn Statement last November. In March's Budget, the Government said it is considering limiting the range of benefits that attract income tax and National Insurance Contributions ("**NICs**") advantages when they are provided as part of salary sacrifice schemes. However, the intention is pension saving, childcare and health-related benefits should continue to benefit from income tax and NICs relief when provided through salary sacrifice arrangements. It seems that pension arrangements are therefore safe for the time being.
- **Funding financial advice**: there will be an increase in the tax and NICs relief available for employer-arranged pensions advice from £150 to £500 from April 2017. A new pensions advice allowance will also be introduced (during Summer 2016) to allow individuals to withdraw £500 tax-free from their DC savings before the age of 55 to be used for funding financial advice.
- **Pensions dashboard**: to help people clearly see all their retirement savings in one place, the Government will ensure the industry launches a pensions dashboard by 2019.
- **Guidance services**: the Money Advice Service, Pensions Advisory Service and Pension Wise are to be restructured to provide a more streamlined guidance service.
- **Technical amendments to support DC flexibilities** – the Government is going to make some technical amendments to ensure the DC flexibilities are working as intended, including introducing legislation to allow DC pensions already in payment to be paid as a trivial commutation lump sum, where total pension savings would be under £30,000.

11. Pensions Regulator consults on "how to" guides to support DC Code

Following on from last year's consultation on a new DC Code of Practice (which has now closed and is awaiting a formal response), the Regulator has now published six new "how to" guides for consultation, covering the six key areas of the Code.

The guides will not form part of the Code (so that they can be updated more easily from time to time) and are instead designed to support the Code and explain to trustees how they can demonstrate compliance.

The guides set out the standards the Regulator expects trustees to meet (or 'best practice'), but the Regulator is clear that they are not intended to be prescriptive or exhaustive in terms of the ways that the standards in the new Code might be met. The guides fill in the detail where there are gaps in the Code itself. For example, regarding what is expected in assessing whether a scheme offers good value for members.

The new Code had previously been praised for being shorter and more comprehensible than the 2013 version. However, trustees will also now need to consider the six supporting guides alongside the Code itself.

A lot of what the guides say is common sense and the suggestions for best practice are things which existing trustee boards will often already be doing, although some of the suggestions may go beyond this (for example, the suggestion that trustee chairs carry out performance appraisals on trustees and that trustees could spend time with the scheme administrator listening in to calls from members as a way of gaining a better understanding of member needs). However, this is all subject to proportionality and the guides are clear that different approaches may be appropriate for different schemes.

Consultation on the guides closes on 11 May. The new Code is due to be laid before Parliament in May and the Regulator says it will publish a formal response to the consultation on the Code then. The new Code and the guides are then expected to come into force in July.

12. Progress on early exit charges cap

The Government recently published a response to its summer consultation on transfers-out and early exit charges; prompted by concerns that individuals were facing a range of barriers in accessing their pension savings. Of particular concern were early exit charges, a lack of clarity in the transfer process and uncertainty around the provision and need for financial advice on DB transfers.

Key points to note from the consultation response include:

- **Reporting requirements** – a new requirement will be introduced for trust-based schemes to report on an ongoing basis how they are performing in processing transfers, including against possible benchmarks and the new transfer regime. It is intended the Pensions Regulator will work with the pensions industry to bring a package of measures into force this summer.
- **Transfer guidance for schemes** – the Pensions Regulator will issue new guidance for trustees to ensure transfers are processed quickly and accurately. This is designed to support the revised DC Code of Practice (which itself, is expected to come into force in July 2016).
- **Transfer guidance for members** – Pension Wise will develop guidance on transfers to support individuals through the transfer process. This will include providing free and impartial information on schemes' statutory requirements and their responsibilities. The paper does not comment on who will be eligible for this guidance (currently, Pension Wise is available to those aged 50 or over who have flexible benefits) or when the guidance will be made available.
- **Early exit charges cap** – the FCA will have a duty to make rules prohibiting "early exit charges" in contract-based schemes. The Government will mirror these requirements in relation to trust-based schemes. The cap is intended to be implemented in March 2017. Note in particular that:
  - the scope of what will be caught is to be finalised, but the response is clear the scope of the cap will be very wide.
  - the cap will apply to both new and existing contracts.
- **Establishing a "whitelist"**– apparently respondents to the consultation were keen for the creation of a "whitelist" of approved pension providers. However, it looks like this is not going to happen (at least in the short-term). Instead, the Government is considering whether there is a need for increased supervision of master trust providers; stating that this work would form an important foundation for any future whitelist and that the Government will "*continue to develop its thinking in this area over the course of the year*".
- **The advice requirement** – the consultation also considered the requirement to take financial advice on transfers-out (or conversions) of safeguarded benefits worth over £30,000; asking whether this was acting as a barrier to accessing benefits. The response refers to the Government's Financial Advice

Market Review (a joint review by the FCA and HM Treasury) concerned with improving accessibility and affordability of financial advice generally, as well as in relation to pensions. The response states that the Government intends to wait for the outcome of this review before taking any action on the advice requirement issue. (Note that the final report from this review was published in April).

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[1] Barber Guardian Royal Exchange Assurance Group [1991] 1 QB 344.

[2] Namely, the occupational retirement provision businesses of life insurance undertakings and certain other authorised/supervised arrangements operating on a national basis.

[3] Which are to be given their normal meanings and broadly interpreted according to the consultation response.

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