

Pensions Legal Update

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Asset-backed pension contributions

Summary: HM Revenue & Customs (HMRC) has published draft legislation about the tax treatment of asset-backed pension contributions (the draft legislation).

Background: An asset-backed contribution (ABC) arrangement usually involves an employer transferring an income-producing asset into a special purpose vehicle (SPV) with the trustees of the pension scheme given an interest in the SPV. The transfer is for a fixed period, for example 15 years, at the end of which the asset reverts to the employer.

On 29 November 2011, the government announced that legislative provisions would be inserted into the Finance Act 2004 to revise the tax treatment of ABC arrangements. The tax treatment of the asset transfer and subsequent payments would be in line with the accounting treatment of ABC structures based on the structured finance arrangements (SFA) legislation in sections 758 to 776 of the Corporation Tax Act 2010. This would allow the value of the asset transferred as a tax deduction, but only any element of interest in the income stream (the finance charge) to be deducted, rather than the whole value of the contributions.

Facts: The draft legislation is to be included in the Finance Bill 2012, and replaces the changes announced in November 2011. It provides that upfront tax relief will not be given unless the structure is an “acceptable structured finance arrangement”. Broadly, this is where the ABC structure satisfies the SFA regime and the following conditions:

- The pension contribution promised upfront under the ABC arrangement must be due to be paid to the pension scheme and is not intended to be held in a subsidiary structure.
- The pension scheme must be the direct lender giving an “advance” (the pension scheme investment) to the employer directly or indirectly through an SPV.
- The advance must be wholly paid out of the promised contribution.
- The contribution must equal both the advance and the financial liability recorded in respect of the advance.
- From the outset, regular payments due to the pension scheme under the arrangement must reduce the financial liability to nil by the earlier of the completion day or 25 years.
- The payments must be of equal amounts due at intervals of no more than one year and must be received by the pension scheme to form part of the sums held for the purposes of the pension scheme.
- The total amount of the payments due to the pension scheme must not be less than the contribution.

The new conditions must be met at the outset of the ABC structure. If the ABC structure does not qualify as an acceptable SFA, then relief will only be available for any future income payments made to the pension scheme under the payment plan. The new tax regime came into effect from 22 February 2012, with transitional provisions applying to payments made between 29 November 2011 and 21 February 2012.

Comment: Employers using, or considering, an ABC structure will need to check the accounting treatment in light of these new changes.

Source: HMRC: Employer Asset-backed Pension Contributions Tax Information and Impact, 22 February 2012, www.hmrc.gov.uk/budget-updates/tiin-draft.pdf; Written Ministerial Statement: Employer asset-backed pension contributions, 22 February 2012. www.hmrc.gov.uk/budget-updates/wms.pdf.

New contracting-out regulations

Summary: The Occupational Pension Schemes (Contracting-out and Modification of Schemes) (Amendment) Regulations 2012 (*SI 2012/542*) (2012 Regulations) have been laid before Parliament.

Background: The government is abolishing the statutory provisions that allow pension schemes to contract out of the state second pension on a defined contribution (DC) basis with effect from 6 April 2012. Currently, both the members of a DC contracted-out occupational pension scheme and their employers pay reduced rates of National Insurance contributions (NICs).

In August 2011, the Department for Work and Pensions (DWP) consulted on a draft version of the 2012 Regulations (the consultation).

“Protected rights” are the part of the member’s pension that derives from the rebates the employer and the member receive on their NICs. Schemes were obliged to include provisions reflecting the protected rights legislation in their rules.

A guaranteed minimum pension (GMP) is the part of a pension built up in a contracted-out defined benefit scheme between 1978 and 1997 which replaces the earnings-related part of the state pension.

Facts: The 2012 Regulations are broadly as proposed in the consultation. The two key changes are:

- Where a scheme revalues GMPs between the member leaving service and retiring using the fixed rate set by the legislation, the rate for early leavers who leave service after 6 April 2012 will be increased from 4.00% to 4.75%.
- Trustees of formerly contracted-out DC occupational pension schemes may remove provisions for protected rights from their scheme rules by resolution under section 68 Pensions Act 1995 (a section 68 resolution).

The section 68 resolution cannot be passed until the 2012 Regulations have come into force on 6 April 2012, but can have retrospective effect. If trustees do not pass such a resolution before 5 April 2018, they will have to make any changes under their own amendment power, which may mean consultation requirements need to be met.

Comment: The increase in the rate of fixed rate of revaluation on GMPs will not be good news for trustees as it will inevitably increase costs. This was expressed in the replies to the consultation, to which the DWP responded that it had not been provided with any evidence suggesting that schemes would have to close because of the increase. However, the ability to pass a section 68 resolution should make life easier for trustees of schemes that would otherwise not be able to remove protected rights provisions from their rules.

Source: 2012 Regulations, 29 February 2012, www.legislation.gov.uk/uk/si/2012/542/contents/made.

Auto-enrolment: consultation on exemption for overseas workers

Summary: The government is consulting on proposals and draft regulations to exempt employers from having to auto-enrol cross-border employees from October 2012 (the consultation).

Background: New laws coming into effect in October 2012 will require all UK employers to automatically enrol “eligible jobholders” into a pension scheme and pay mandatory minimum contributions. A jobholder is defined as an individual “who is working or ordinarily works in Great Britain under the worker’s contract” (*section 1, Pensions Act 2008*).

Employers with UK jobholders working in the EEA also need to consider the Occupational Pension Schemes (Cross-Border Activities) Regulations 2005 (*SI 2005/3381*) (2005 Regulations). This is because an individual who is an eligible job-holder may also be a “qualifying person” under the 2005 Regulations. A “qualifying person” is broadly an individual who is subject to the social and labour laws of a EU member state other than the UK.

The government has the power to pass regulations to exempt employers from automatically enrolling dual-status workers (*section 292A, Pensions Act 2004* (*inserted by section 18, Pensions Act 2011*)) (section 292A).

Facts: If an employer enrolls a UK job-holder who is also a qualifying person (a “dual-status worker”) there are consequences for the pension scheme as it would need to comply with the requirements of the 2005 Regulations. These requirements can be complex and costly.

The government has decided to exercise its power under section 292A and the consultation contains draft regulations which exempt employers from automatically enrolling dual-status workers (Occupational and Personal Pensions Schemes (Automatic Enrolment) (Amendment) (No.2) Regulations 2012) (the draft regulations).

The draft regulations require employers to actively identify dual-status workers and exclude them from auto-enrolment.

Comment: These draft regulations resolve the conflict between the requirements of the auto-enrolment regime and the cross-border regime for workers in the EEA.

Source: Workplace Pension Reform: Automatic Enrolment and European Employers: Consultation on draft regulations, February 2012, www.dwp.gov.uk/docs/auto-enrol-european-employers-consultation.pdf. Comments are requested by 2 April 2012.

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