LCP INSIGHT CLARITY ADVICE

LCP CORPORATE PENSIONS FOCUS: JULY 2015

Political impacts on pensions – the Budget implications and investment considerations of the potential Greece exit from the Eurozone

In this edition of LCP's Corporate Pensions Focus we consider:

- The Chancellor's emergency Budget last week could mark the end of senior executive pensions, we look at what you need to review this summer.
- As we go to press, brinkmanship regarding Greece has turned to crisis, but what could the different possible outcomes mean for investment markets?

Key UK pension assumptions and statistics*

	30 June 2015	31 December 2014	30 June 2014
IAS19 discount rate	3.6-4.1%	3.2-3.9%	4.1-4.5%
Assumed RPI inflation	3.1-3.5%	2.8-3.3%	3.2-3.6%
Assumed CPI inflation	1.8-2.8%	1.5-2.6%	1.9-2.9%
Long term gilt yield	2.6%	2.4%	3.4%
FTSE 100 Index	6,521	6,566	6,744

* The figures shown are indicative ranges, different figures may be appropriate depending upon the individual circumstances.

IN THIS ISSUE

Executive Pensions Survey

LCP will be launching the annual FTSE 100 Executive Pensions Survey very soon.

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Senior Executive Pensions – the end of the road

On 8 July, George Osborne effectively announced the end of the road for tax-effective pension saving for senior executives. Anyone with total taxable earnings over £110,000 will need to re-consider whether the new rules impact on them; and anyone with taxable earnings in excess of £210,000 will effectively be limited to contributions at around the current "Auto-enrolment" level of 2% (a maximum of £10,000 pa). It is too early to say what the full ramifications of this change might be, but one concern will be how interested senior executives are in the quality of the pension provision, beyond the Auto-enrolment requirements, now that they are effectively excluded from them.

Assessing who is impacted?

The first challenge for companies will be to establish who is impacted by the new rules. As the taper relates to an individual total taxable income, not just that from the employer, there is no guarantee that any pension payment over £10,000 is within the new Annual Allowance from April 2016. However, the first test will be whether a member's income (including all taxable elements, and elements of income gained outside of employment) exceeds £110,000.

Curiously, those individuals who just breach the £110,000 may find that the most effective way to bring their assessed income below £110,000 is to make a pension contribution!

Of course, pensions teams will not have details of income outside of the company's employment, and indeed there may be internal barriers to obtaining detailed data on total remuneration that is provided by the company. As such, the best that can be done is to identify the "most at risk" category of members. Beyond this, it may make most sense for the employer to provide access to an online pensions tax modeller that enables individuals to establish their own position.

We have found this approach to be very effective under previous tax changes that impacted the most highly paid individuals.

Pensions for employees beyond £210,000 pa

In many organisations the most senior individuals do receive annual remuneration above £210,000. For this group, the Annual Allowance for tax effective pension saving will become £10,000 – which equates to 5%, at most. This is coupled with a reduction in the Lifetime Allowance to £1m, including investment roll up.

It is likely therefore that the most tax effective option will be for the most senior individuals to be removed from their existing pension arrangements. So as to remain competitive overall, some form of "Pension Supplement" will need to replace this lost benefit, and no doubt there will be a need for most organisations to urgently consider this issue over the summer.

The Government has also announced a complete review of the way in which pension savings are taxed, with one possibility being complete integration with the ISA savings vehicle. It will be very interesting to see how the industry moves in the coming years ahead.

Where next?

In summary, the July 2015 Budget has again brought significant change to the pensions world. There will be a need to communicate to members, and perhaps provide assistance to them regarding their position to avoid unintended tax consequences down the line. Further, the pension provision for all senior executives will need to be reviewed, and potentially stopped, ahead of April 2016.

LCP Pensions Tax Modeller

Helping employees understand current and future tax consequences of their pension savings.

Click here to find out more

Greek fudge may not taste so sweet

Although dramatic, the resounding "no" vote in the Greek referendum changed few facts on the ground. What did change however was that what was once mere brinkmanship and a series of lapsed deadlines took on a sense of true crisis.

It is a fast moving drama; by the time you read this it is likely that things will have moved again. Perhaps Greece is on a rapid journey to expulsion from the Euro. Perhaps its hitherto defiant politicians could not dare to leave the Euro, and so capitulated and have secured a further bail-out package. Or have all European parties once more demonstrated their penchant for fudge?

What is clear is that the rules of the game have changed; the admission that there is a plan for Greek expulsion from the Euro has laid bare the assumption that membership of the single currency is a one-way street. It has again stimulated the debate as to whether monetary union alone can succeed. As a consequence, the EU will have to decide whether or not the only way to avoid others following Greece's example is to speed up significantly its fiscal and political integration plans, which may have important implications for the UK's negotiations over the terms of its membership.

As far as markets are concerned, a fudged outcome would provide near-term relief but little comfort that the crisis will not persist. Absent events elsewhere (particularly China's equity market gyrations), a more definitive resolution to this long running issue would provide a much firmer foundation for markets longer term; that is, so long as peripheral Eurozone contagion can be managed.

At all times, but especially now, pension schemes require a diversified and risk managed approach to investment strategy, enabling them to navigate their way through periods of potential volatility such as this. And, if markets do turn out to be choppy, then the silver lining to this particular cloud may well be the investment opportunities thrown up for long-term investors. We will therefore be monitoring markets with a view to assisting you if we see any that we believe are of particular interest.

Proposed changes to IAS19 threaten companies with extra balance sheet liabilities

In June an exposure draft proposing changes to international pensions accounting standards was published, setting out two key changes:

1. Changes to complex IFRIC14 rules, which require companies to recognise large extra liabilities over and above their IAS19 deficit in certain circumstances. While we expect most companies to be unaffected, a minority could see huge extra liabilities. **Action: Companies with funding obligations should review their legal and actuarial advice to find out if they may be threatened with these large extra liabilities.**

2. Changes to the rules on accounting for special events under IAS19, such as closures to accrual, buyout, and benefit changes. **Action: Companies planning changes to their pension schemes should take into account possible changes in the calculation of costs when budgeting.**

Any questions?

If you would like any assistance or further information on the issues raised, please contact Alex Waite, Alex Whitley or the partner who normally advises you at LCP via telephone on +44 (0)20 7439 2266 or by email to enquiries@lcp.uk.com.

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Clarity out of uncertainty - Making sense of the pensions world in 2015 and beyond
16 September 2015
The LCP Annual Pensions Conference 2015 will help you navigate your way around the changing pensions landscape with a clear strategy for 2016 and beyond.

For full details of all events and to register, please visit www.lcp.uk.com/events

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