AMPS Pinsent Masons

Scheme Pension

Paragraph 2(4)(b) Schedule 28, Finance Act 2004

We have been asked to provide a note to the Association of Member Directed Pension Schemes in relation to an issue which has arisen concerning HMRC's interpretation of paragraph 2(4)(b) Schedule 28, Finance Act 2004 and guidance relating to that provision contained in the Registered Pension Schemes Manual (RPSM).

Paragraph 2(4)(b) reads as follows:-

> *"2(4) None of the following prevent the pension satisfying the condition in sub-paragraph (3) – (b)a reduction in the rate of the pension which applies to all the scheme pensions being paid to or in respect of members of a pension scheme."*

The question specifically relates to the interpretation of the words: *"all the scheme pensions being paid to or in respect of members"*.

HMRC have confirmed that they interpret this provision as excluding the case of a single member scheme and/or a scheme with only one scheme pension in payment. They also suggest that if the provision did include single member pension schemes, it would open up "obvious avoidance opportunities". A copy of the correspondence with the HMRC Pension Scheme Helpdesk is contained in the Appendix to this note.

In our view this is not the correct interpretation of this provision. It is not in accordance with statutory rules of interpretation or common law rules of interpretation. We suggest that HMRC should be asked to consider obtaining further legal advice from the Treasury solicitor regarding its interpretation of this provision.

We set out below our reasoning as to why HMRC's interpretation cannot, in our view, be correct:-

1. STATUTORY LAW - THE INTERPRETATION ACT 1978

Section 6 of the Interpretation Act 1978 reads as follows:-

> *"6. In any Act, unless the contrary intention appears,- (c)words in the singular include the plural and words in the plural include the singular."*

In Paragraph 2(4)(b), no "contrary intention" appears.

Therefore, section 6 of the Interpretation Act requires that "scheme pensions" in the plural would include "scheme pension" in the singular. Therefore Paragraph 2(4)(b) allows the reduction of a scheme pension in a scheme where there is only one member and/or only one member in scheme pension.

2. COMMON LAW

There is a presumption in English law that the legal meaning of an enactment is that which corresponds to the literal meaning.[1]

2.1 The Literal Meaning Rule

It is a rule of law that where an enactment is grammatically capable of one meaning only and on an informed interpretation of that enactment the interpretative criteria raise no real doubt as to whether that grammatical meaning is the one intended by the legislator, the legal meaning of the enactment corresponds to that grammatical meaning.[2]

Applying this rule means that the literal meaning must be given where there is nothing to modify, alter or qualify it. This rule determines the operation of nearly every enactment, because nearly every enactment has a straightforward and clear meaning with no counter-indications. The interpretation must be the meaning the provision bears when, as a piece of English prose, it is construed, without reference to any other text, according to the rules and usages of grammar, syntax and punctuation.[3]

Applying this to Paragraph 2(4)(b), it is clear that it is indeed only capable of one meaning. The plural use of "scheme pensions" merely indicates the fact that the reduction has to be applied to all "scheme pensions" which are being paid by a pension scheme, not that there must be more than one scheme pension in order for the reduction envisaged under this provision to be allowed. The words "scheme pensions" are used in order that the sentence is grammatically correct, not to determine that there must be more than one scheme pension in payment.

Similarly, the reference to "members" is a generic reference to the members of the scheme and would apply equally to one member or many members.

Paragraph 2(4)(b) does not mention anything about single member schemes and/or schemes with only one scheme pension in payment being excluded from the provision. We therefore consider that there are no modifications or counter-indications contained in the provision.

2.2 Other methods of interpretation

Even if a court saw fit not to apply the literal interpretation to the provision, we do not consider that any other method of interpretation would comfortably lead to the interpretation set out in the HMRC Pension Scheme Helpdesk's email.

- **Common Sense Rule of Interpretation**

  This requires that common sense must be applied in construing statutes.[4] Under a common sense interpretation if Paragraph 2(4)(b) was meant to apply only where there was more than one scheme pension in payment this would have been expressly set out. In our view, the common sense approach is that the provision was drafted in the way it was in order to make grammatical sense and that "all the scheme pensions" necessarily includes a single scheme pension.

- **Mischief Rule of Interpretation**

  The mischief rule of interpretation requires that a court should look to apply a provision in a way to suppress a mischief which the provision was intended to

[1] *Bennion on Statutory Interpretation*, 5th edition, Part XVIII, Section 285
[2] Ibid, Part XI, Section 195
[3] *Halsbury's Laws of England*, Vol 44(1), para 1470
[4] *Bennion on Statutory Interpretation*, Part XI, Section 197

suppress.[5] HMRC's Pension Scheme Helpdesk hint at this approach when it states "*Another reason we do not provide for a single member scheme pension to be reduced, is because of the obvious avoidance opportunities that would be opened up.*" However, we do not believe that this is a good argument, particularly as Paragraphs 2 and 2A of Schedule 28, Finance Act 2004 make express provision for dealing with "avoidance arrangements" (see paragraph 2A(2)). Any mischief which the provision is intended to address can be dealt with under these provisions without requiring the strained interpretation of the meaning of "all the scheme pensions".

- **Purposive Rule of Interpretation**

A purposive construction is one which (a) follows the literal meaning where that meaning is in accordance with the legislative purpose; or (b) applies a strained meaning where the literal meaning is not in accordance with the legislative purpose.[6]

The purposive rule of interpretation would also not, in our view, support HMRC Pension Helpdesk's interpretation. We do not believe that the purpose of Paragraph 2(4)(b) was to restrict the ability to make a reduction in scheme pensions to schemes where there is more than one scheme pension in payment. Rather, we believe the purpose of Paragraph 2(4)(b) is to afford some flexibility to schemes where it is found that the initial actuarial assumptions applied in calculating the level of scheme pension which a scheme could afford are not being borne out in practice.

A scheme pension is intended to be a pension for life. As such there may (especially in the money purchase arena) be circumstances where a scheme pension fund cannot continue to sustain the current level of scheme pension being paid. We believe Paragraph 2(4)(b) was therefore intended to allow the reduction of all scheme pensions being paid by a scheme in order to ensure that the scheme pensions were indeed a pension for life and to ensure they did not have to stop due to insufficient funds being available to pay them. This principal applies equally if there are one or 100 scheme pensions being paid from a scheme. Therefore the literal interpretation, that "scheme pensions" includes a single scheme pension, is in accordance with this purpose and so a strained interpretation should not be applied.

3. OTHER FINANCE ACT 2004 PROVISIONS

Other provisions also show that, if the drafting in Paragraph 2(4)(b) intended to exclude single member schemes and/or schemes with only one scheme pension in payment, the drafting would have specified this.

For example, section 191(3)(c) dealing with relief on contributions states:-

> "*(3) Subject to subsection (7), relief in respect of contributions under a pension scheme made by a member of the pension scheme may (instead of being given in accordance with section 192) be given in accordance with section 193 (relief under net pay arrangements) if- (c) relief in respect of contributions made under the pension scheme* ***by all of the other members*** *of the pension scheme who are employees of the sponsoring employer is given in accordance with that section.*"
>
> (my emphasis)

[5] Ibid, Part XIX, Section 289
[6] Ibid, Part XX, Section 304

Clearly this provision would apply if there was only one member. Therefore the reference to "other members" must include a single member scheme as well as multiple 'other members'.

Further, inclusion of the wording in bold shows that if the drafting of Paragraph 2(4)(b) was intended to exclude single member schemes and/or schemes with only one scheme pension in payment, it could easily have been made to do so with wording such as:

> "*a reduction in the rate of the pension which applies to all the* ***other*** *scheme pensions being paid to or in respect of members of a pension scheme.*"

A further example is contained in paragraph 22(6) of schedule 36 which states:-

> "*(6) A transfer is a block transfer if- (a) it involves the transfer in a single transaction of all the sums and assets held for the purposes of, or representing accrued rights under, the arrangements under the pension scheme from which the transfer is made* ***which relate to the member and at least one other member*** *of that pension scheme...*"
>
> (my emphasis)

Again, this shows that if the intention was that Paragraph 2(4)(b) only applied where there was more than one scheme pension, this would have been expressly set out.

In light of this, as mentioned above, we recommend HMRC are asked to consider obtaining further legal advice from the Treasury solicitor regarding its interpretation of this provision. It should then be asked to confirm the advice given to the AMPs board.

Pinsent Masons LLP.

Pinsent Masons LLP
20 May 2010

APPENDIX 1

ORIGINAL EMAIL CORRESPONDENCE WITH HMRC'S PENSION SCHEMES HELPDESK

-----Original Message-----
From: Pension Schemes Helpdesk [mailto:pensionschemes@hmrc.gov.uk]
Sent: 17 March 2010 14:59
To: Andy Strawbridge
Subject: Re: Scheme Pension under a Money Purchase Scheme (KMM8899838V37718L0KM)

Dear Mr Strawbridge,

Thank you for your email enquiry of 24th February 2010.

I can confirm that in our view the legislation(paragraph 2(4)(b) Schedule 28, Finance Act 2004) is constructed in terms of "pensions" without covering the case of a single member scheme pension. RPSM09101530 reflects this. Another reason we do not provide for a single member scheme pension to be reduced , is because of the obvious avoidance opportunities that would be opened up.

I can also confirm that this view will apply to the example you put forward in your email, with the resultant unauthorised payments, as you suggest.

We may have removed personal details from this reply to protect confidentiality

Yours sincerely

Colin Robinson
Pension Scheme Services Website: www.hmrc.gov.uk/pensionschemes

Helpline:
Great Britain: 0845 600 2622

If you are phoning from outside Great Britain ++44 115 9741600 Opening hours Monday to Friday 9.00 to 17.00

Original Message Follows:

I would be grateful if you would clarify a technical point on Scheme Pension under a Money Purchase Scheme.

We operate a portfolio of Small Self Administered Schemes. We are considering whether to make Scheme Pension available as a member option. I have therefore read through RPSM to review the necessary requirements. One of our professional contacts has advised me that HMRC may interpret the following section of RPSM differently to the apparent industry understanding.

RPSM09101530 - Technical Pages: Member benefits: A secured pension: Scheme pension: Stopping or reducing scheme pension: Scheme wide reduction Where a scheme wide reduction is applied
[Para 2(4)(b), Sch 28]

This exemption is intended to cover situations where, for example, the scheme has to reduce pensions payable over the previous years level on the basis of actuarial advice. In this case, the scheme pensions can be reduced provided the reduction was applied to all the scheme pensions currently being paid from the scheme. This does not include dependants scheme pensions. This reduction may be applied on a pro-rata basis or a flat rate basis. If a scheme pension is reduced in accordance with this relaxation, and the reduction is part of what the legislation calls avoidance arrangements, the member will become liable to an additional unauthorised payments charge on a defined appropriate amount.

RPSM09101600 explains what the legislation means by avoidance arrangements and the appropriate amount. I understand that in the case of a Money Purchase scheme where only one member is receiving Scheme Pension, HMRC may hold that the above exemption does not apply, as the legislation refers to a reduction in the scheme pensions - i.e. implying more than one member within a scheme. Therefore, on review by an actuary, if it was determined that the level of Scheme Pension should be reduced, the resulting income payments would become Unauthorised Payments, as the payments would no longer meet the criteria for a Scheme Pension.

If the scheme is supported by an employer, the employer could make a contribution to cover the shortfall, to maintain the Scheme Pension at its original level and thereby avoid an Unauthorised Payment. Furthermore, if the reduction in Scheme Pension was significant, an additional tax charge would apply to the amount of any pension commencement lump sum that had been paid as a result of the member going into Scheme Pension.

I would be grateful if you would confirm if this understanding is correct as many of the industry providers seem to be relying on the Scheme Wide Reduction Exemption as a safety mechanism if the Money Purchase fund is depleted too rapidly, irrespective of whether only one member is in receipt of Scheme Pension.

We have a particular client who is interested in Scheme Pension. The SSAS has two members a younger member has uncrystallised funds, the other is over 75 and is in Alternatively Secured Pension.

The older member is considering Scheme Pension. This member drew his benefits before A Day and used the SSAS annuity deferral option. He has not been subject to the BCE regime, nor has he drawn any pension commencement lump sum under the current regime. No contrivance of increasing a pension commencement lump sum is involved the member is interested in the 10 year guarantee under Scheme Pension, and the higher level of income that can be supported in comparison with ASP. We have taken initial actuarial advice, and the proposed Scheme Pension figure is prudent approximately 10% higher than the ASP maximum. The SSAS assets are invested conservatively and the member is in fair health.

We would propose to engage the actuary to undertake triennial reviews of the Scheme Pension. However, if the actuary recommends that Scheme Pension should be reduced, will the subsequent payments become Unauthorised Payments, unless the employer covers any shortfall in the fund? The younger member is only aged 53 and unlikely to draw benefits using Scheme Pension during the lifetime of the older member.

I look forward to hearing from you.

Andy Strawbridge

AssociateDirector

Smith WilliamsonFinancial Services