As we have covered in a couple of previous Aries Insights, one of the valuable services that we offer our Members is the Aries Help Desk. Aries Members can ask us any technical queries that they may have and we will do any research needed and provide a response.

We also capture all of these queries into an ever-growing database for the benefit of all Aries members. (All queries are, of course, suitably anonymised.)

For this Aries Insight, we will look at some of the interesting queries that have been raised with us recently.

What to do with Surplus AVCs?

Our first case concerns a Defined Benefit scheme which allowed members to transfer in benefits from other schemes to secure additional pensionable service under the scheme and also allowed for the payment of 'added years' AVCs. (These are AVCs which purchase an additional period of pensionable service for the member under the scheme.)

In this particular case, the member had:

- 29 years of service due to their membership of the scheme, plus
- 18 years of extra pensionable service arising from a transfer in, plus
- 2 years of extra service arising from the payment of 'added years' AVCs.

So, in total, 49 years of pensionable service.

The problem here, however, is that the Scheme Rules (which have not been updated since 2001) limit the maximum period of pensionable service that can be taken into account to 40 years, in line with the usual pre A-Day limits. Those Rules also included provisions relating to the possible refund of 'surplus AVCs', again in line with the pre A-Day provisions.

As our enquirer correctly pointed out, under the A-Day tax regime, there is no maximum benefit, so no 'surplus' can arise and if any refund were to be paid it would unauthorised.

The question, then, is *what – if anything – can be done about the 'excessive' period of pensionable service, in particular the added years that the member paid for via AVCs? Will the member simply have to forego any benefit in respect of that excessive period of pensionable service?*

In terms of the added years secured by the payment of AVCs, it will not be possible to return the AVCs to the member as an authorised payment.

As explained in the PTM, a return / refund of contributions will only be an authorised payment where it qualifies as either a short service refund lump sum (generally referred to as a 'return of contributions' to an early leaver) or a refund of excess contributions lump sum (which can only arise where the member's contributions to the scheme in a tax year exceeded their relevant UK earnings for the tax year).

There is, in fact, actually a third possibility here, which arises when contributions are incorrectly paid to a scheme. As a simple example, suppose that the correct member contribution rate is 5% of earnings but the employer accidentally deducts 15% and passes this across to the scheme: the scheme was never entitled to the extra 10%, so that extra amount was incorrectly paid to the scheme. The scheme can return the extra 10% back to the employer, who will pass it on to the member. This sort of possibility is considered in the PTM, however it is unlikely to be of any help in this case.

It is, of course, possible that the Scheme Rules include a provision saying that members are not able to purchase 'added years' via AVCs where the total pensionable service period would exceed 40 years, in which case it would appear that the added years AVCs were paid in contravention of the Rules, meaning that the scheme was never entitled to receive them. Unfortunately, we doubt that such a Scheme Rule will exist because, at the point a member joins a scheme, nobody knows how long their period of pensionable service will be (or if any other benefits will be transferred in to secure extra service etc).

We actually doubt that the Scheme Rules would be structured in this way, simply because, pre A-Day, there were provisions allowing the return of 'surplus AVCs', so there was no real need to have a separate Scheme Rule prohibiting 'excessive' AVCs being paid in.

What other solutions might there be to this case?

Firstly, many Scheme Rules actually include a provision that allows the Trustees to pay 'alternative' benefits (that is, a benefit of a different amount or in a different form) from those usually available under the Scheme Rules – with the usual caveat that the alternative benefits offered must be of at least equal value to the normal 'Scheme Rules' benefit.

If such a Trustee discretion does exist, it may be possible for the scheme to pay out a pension based on more than the usual maximum service period of 40 years, despite the standard benefits being restricted to only 40 years. If so, this would mean that the member might actually be able to receive benefits based on the full 49 years of pensionable service.

There might be other possible work-arounds here, depending on the actual provisions of the Scheme Rules and just how far the scheme / Trustees wish to go in resolving the issue for the member. It is theoretically possible for the member to take a partial transfer out now (representing the 'excessive' 9 years of service) to bring the total period of pensionable service in the scheme down to the maximum of 40.

Such a transfer would be a non-statutory transfer, because only part of the member's defined benefits would be being transferred, and so would be subject to the Scheme Rules permitting non-statutory partial transfers. There would also be a cost to the scheme in terms of working out the cash equivalent value of the 'excessive' period of service that is being transferred out: this is likely to be a rather non-standard calculation and so may well need input from the Scheme Actuary.

Bespoke member communications might also be required and, if the transfer would be made to a money purchase arrangement, the 'appropriate independent advice requirement' might apply, noting that this can apply where the ***total*** value of the member's safeguarded benefits under the transferring scheme exceeds £30,000, not just the amount being transferred.

Other alternatives might also be possible, which again depend on the provisions of the Scheme Rules and just how far the scheme / Trustees wish to help. The member might, for example, be able to exchange the 'excessive' period of service to provide for a larger rate of survivor's pension and / or higher than usual increases on the pension in payment.

The *Pensions Act 1995* includes rules against the assignment / surrender of a member's occupational pension benefits, however certain such transactions are permitted, such as those mentioned here.

Again, there would be a cost to the scheme here, in terms of either calculating the higher rate of survivor's pension or the extra increases on the pension in payment, as well as the added administrative complexity of actually paying those non-standard benefits.

Another solution might be, again subject to Scheme Rules and the Trustees' stance on the matter, to convert the 'excessive' service period into money purchase benefits within the scheme, which the member could then take as an Uncrystallised Funds Pension Lump Sum. This would, of course, trigger the Money Purchase Annual Allowance for the member and might again require the member to take 'appropriate independent advice'.

Ultimately, it may well be a case of establishing how much flexibility there is (if any) under the Scheme Rules and the extent (if any) to which the Trustees are prepared to allow a non-standard solution to the issue.

Aries comment

This is a rather unusual case, where the problem really arises because the Scheme Rules have not been updated to reflect the A-Day position. It does, however, show that, where issues arise, it is sometimes necessary to try to 'think outside the box' and come up with creative solutions that work for both the member and the scheme.

'Scheme Pays' problems

Our next query concerns issues with Scheme Pays (the process under which a member can require a scheme to settle part or all of their Annual Allowance charge with HMRC).

In this case, our enquirer was aware that there are some changes coming in concerning Scheme Pays which might be helpful for their case.

The case in question concerned a member who had recently discovered that he had been subject to the Tapered Annual Allowance for the 2021/22 tax year as well as for 'some previous tax years too'.

Do the changes to the Scheme Pays requirements help here and, if not, what can be done to help the member?

To start here, [Section 9](#) of the *Finance Act 2022* has introduced some modifications to the mandatory Scheme Pays notice deadline. Previously, the standard deadline for the notice was 31 July in the year following the end of the tax year to which the notice relates.

This deadline is now modified by the *Finance Act 2022* to cover cases where the scheme is required to provide the member with amended information in connection with a change to the individual's Pension Input Amount under the scheme for a tax year.

In a little more detail, from 24 February 2022, where during a period beginning on 2 May after the end of a tax year and ending six years after the end of that tax year, a scheme administrator is required to provide the member with information in connection with a change to the individual's Pension Input Amount for the tax year, the member must provide the mandatory Scheme Pays notice to the scheme by the earlier of:

(a) three months after the date on which the scheme administrator provided the member with the amended Pension Input Amount information; and

(b) six years after the end of the tax year to which the amended Pension Input Amount information relates.

[*FA 2004 s.237BA as inserted, with effect from 24 February 2022, by FA 2022 s.9 (3)*]

This change in the deadline is also supported by new Regulations (The Registered Pension Schemes (Miscellaneous Amendments) Regulations 2022 [SI 2022 / 392]) which impose new requirements on scheme administrators and employers where there is, in effect, a retrospective change to a member's Pension Input Amount under a scheme, whether because of 'new information' or as a result of a change in the Scheme Rules.

Briefly here, the employer is required to provide the scheme with any 'new information' that affects the member's Pension Input Amount under the scheme for a tax year and the scheme has new duties to provide the member with an amended Pension Savings Statement for the tax year.

Unfortunately, for this query, it does not appear that any of the changes detailed above will help at all. In this case, the member has discovered that he is subject to the Tapered Annual Allowance for the 2021/22 tax year and some previous tax years. Where a member is subject to the Tapered Annual Allowance, this reduces their Annual Allowance for the tax year, meaning that it is more likely that an Annual Allowance charge will arise.

Being subject to the Tapered Annual Allowance, however, does ***not*** change what the individual's Pension Input Amount under the scheme for a tax year actually is. All of the new changes explained above relate to situations where the Pension Input Amount under the scheme retrospectively changes, and that is not the case here (it is just the amount of the Annual Allowance charge that is due that changes).

As such, we are back to a mandatory Scheme Pays notice deadline of 31 July following the end of the tax year to which the notice relates. For the 2021/22 tax year (deadline 31 July 2023) and the 2020/21 tax year (deadline 31 July 2022), the member can still submit a mandatory Scheme Pays notice; however for earlier tax years, the mandatory Scheme Pays notice deadline has already expired.

The scheme could, however, offer voluntary Scheme Pays for these earlier tax years instead. The difficulty here is that, in these cases, the deadline for the member reporting the tax liability and for the scheme to settle the charge is the standard self-assessment deadline of 31 January following the end of the tax year in question. This point is touched on in the PTM in the text:

If the scheme agrees to pay an amount of a member's annual allowance charge liability on a voluntary basis, the scheme would not have joint and several liability for the tax charge and the liability for the annual allowance charge would remain with the member. The payment made by the scheme on a voluntary basis should therefore be paid to the member's normal Self Assessment deadline.

It is also worth noting the guidance in the PTM in the text:

If a member does not meet the conditions for 'Scheme Pays' to apply, their pension scheme may agree to pay their annual allowance charge liability on a voluntary basis. If they do this, the liability for the annual allowance charge will remain with the member until the charge is paid. This means that if, for any reason, the scheme does not pay this within the required time limits, the member will still be liable for the payment of the charge and may incur interest and penalties.

There may just, however, be a possible way out of this problem. If, for the earlier tax years, the member did provide a mandatory Scheme Pays notice by the required 31 July deadline, the member can change the amount specified in that notice by giving the scheme an amended Scheme Pays notice. The deadline for providing an amended notice is currently 31 July following the end of a period of four years beginning with the last day of the tax year to which the original notice related. This 'four years' is, however amended to six years with effect from 6 April 2022. Amended Scheme Pays notices are considered in the PTM.

Unfortunately, however, this amended notice route is unlikely to help in practice. This is because, where mandatory Scheme Pays is involved, there is a maximum amount that the member can require the scheme to pay and this maximum is based on the Annual Allowance charge arising on the member's Pension Input Amount in excess of the ***standard*** Annual Allowance (i.e. currently £40,000). This point is addressed in the PTM in the text:

There is a maximum amount that a member can ask their scheme administrator to pay under these circumstances based on the pension input amount in the scheme which exceeds the annual allowance (for example, for tax year 2016-17, this means exceeded £40,000 - note - the tapered annual allowance and/or money purchase annual allowance is ignored).

If the member has previously provided a mandatory Scheme Pays notice for the tax years in question and the member required the scheme to pay all of the Annual Allowance charge arising (based on the assumption that they were subject to the standard Annual Allowance rather than the Tapered Annual Allowance), then they could ***not*** submit an amended mandatory Scheme Pays notice requiring the scheme to pay any further charge arising because they are subject to the Tapered Annual Allowance instead.

Aries comment

This query is interesting because it concerns some very recent changes to the legislation in this area, even though those changes do not actually help solve the problem in this instance.

The query is, however, a useful reminder that the maximum amount a member can require a scheme to pay under the mandatory Scheme Pays process is based on the Annual Allowance charge arising on the member's Pension Input Amount in excess of the ***standard*** Annual Allowance, even where the member is subject to the Tapered Annual Allowance or the Money Purchase Annual Allowance.

The recent legislative changes mentioned above are very much driven by the McCloud judgment and the solution being introduced to resolve this. As such, they are unlikely to have any significant impact on schemes that are not public service schemes.

The new 'Conditions for Transfers' Regulations

We know that many schemes are still getting to grips with the new 'Conditions for Transfers' Regulations. The Occupational and Personal Pension Schemes (Conditions for Transfers) Regulations 2021)[SI 2021/1237], as they are officially known, came into force from 30 November 2021.

One issue that came up recently was exactly how these Regulations apply where pension credits (benefits awarded to an ex-spouse or ex-civil partner under a Pension Sharing Order) are involved.

Do the new Regulations apply in this situation?

To explain this, we need to make a very clear distinction between two different situations.

When a Pension Sharing Order is served against the Trustees or managers of a scheme, the Order will award the ex-spouse / civil partner a **pension credit** and the Trustees or managers are required to discharge their liability for that **pension credit** either by way of an internal transfer (creating **pension credit rights** for the ex-spouse / civil partner within the scheme) or by way of an external transfer (transferring the pension credit to another arrangement to create **pension credit rights** for the ex-spouse / civil partner within that external arrangement).

Now, the new 'Conditions for Transfers' Regulations apply where a **pension credit member** is making an application to transfer their **pension credit rights** under a scheme to another arrangement.

When the Trustees or managers of a scheme are implementing a Sharing Order by way of an external transfer, the ex-spouse / civil partner is not a member of the scheme and has no **pension credit rights** under the scheme, so the new Regulations do not apply.

Conversely, if the Trustees or managers of a scheme discharge their liability for a **pension credit** by way of an internal transfer, the ex-spouse / civil partner will become a pension credit member of the scheme and will have **pension credit rights** under the scheme. If such a member wanted, at a later date, to transfer those **pension credit rights** to another arrangement, then the new Regulations will apply. The same would be true if the Trustees or managers of a scheme discharge their liability for a **pension credit** by way of an external transfer and the ex-spouse / civil partner later wants to transfer their **pension credit rights** under the arrangement that received the **pension credit** onto another arrangement.

> ***Aries comment***
> The distinction between a **pension credit** (awarded to an ex-spouse / civil partner under a Pension Sharing Order) and **pension credit rights** (created for the ex-spouse / civil partner when that Pension Sharing Order is actually implemented) is a common source of confusion. It may be helpful to remember that, until the Sharing Order is actually implemented, the ex-spouse / civil partner does not have any actual benefits in respect of that Order.

Did you find this Aries Insight useful?

If so, please share it with your colleagues and let them know that more information is available from the *Aries Pensions System*.

If you have any suggestions for topics that you would like to see covered in a future Aries Insight, then please let us know.

Aries Insight produces these 'Insights' for Aries Members to highlight key legislative changes and other topics of interest. ***As they are only short articles, they cannot always cover every aspect of the topic being discussed and must not be considered as legal or financial advice.***

All Aries Insights are intended to reflect the position as at the date the Insight was issued. Please consider the possibility that the relevant legislation may have changed since an Insight was issued.