Bandwagon

The BWCI Group Newsletter

BWCI

Quarter 2 - 2018

Inside this issue:

GDPR is coming!

Rodney Benjamin

In this issue we mark the passing of Rodney Benjamin, who died in February after a long struggle with myeloma. Rodney was a distinguished actuary who, together with Pat Merriman and Stephen Ainsworth, developed the original Bacon & Woodrow practice in the Channel Islands into the BWCI Group that we know today.

Rodney qualified as a Fellow of the Institute of Actuaries in 1977. He trained in the UK with a major life assurance company before moving to a UK pensions consultancy. In 1984 he moved to Guernsey to join the then Guernsey Branch of Bacon & Woodrow. In doing so he became its thirteenth employee, which Rodney regarded as particularly auspicious!

As an experienced actuary he progressed rapidly to partnership and led the client team for a number of our largest clients. In addition to his consultancy work, he was also responsible for business development and worked with Stephen to grow the business to such an extent that staff levels had increased sevenfold by the time of his retirement in 2004.

Rodney also encouraged younger actuaries to develop their careers, acting as an enthusiastic mentor to many. He was also President of the Channel Islands Actuarial Society between 2005 and 2008.

As soon as he arrived in Guernsey, Rodney threw himself into the business life of the Island, particularly with the Institute of Directors, where he served a term as chairman. He also held a number of directorships of captive insurance companies and was much sought after in that role.

Outside work Rodney took a keen interest in music, reflecting his degree course in the unusual combination of mathematics and music; he was heavily involved with St James, where he served on its Council, including a period as its President.

Rodney was a devoted family man and our sympathies go out to Jenny, his wife, and their children and grandchildren. In later years he delighted in his grandchildren, and proudly brought two of them along to the BWCI Camerata Family concert, just a couple of weeks prior to his death.

We will all remember Rodney with great affection. He was well-liked and respected by clients and staff alike. He will be missed by us all and remembered as a "really nice man".

GDPR is coming!

Due to changes in the data protection legislation in May 2018, we need your permission to continue to hold your personal information to keep you informed about relevant news and developments, as well as sending you Bandwagon.

We will not share your information with others.

More information on how we use your data can be found in our privacy policy at:

https://www.bwcigroup.com/privacy-policy/

Many of our readers have already responded. However, if you have not already done so, you will have received a reminder with this issue of Bandwagon.

We wouldn't like this to be goodbye, but unless you give us your permission, we will not be able to "Stay in touch"after 25 May 2018.

The Isle of Man Budget

"a Pension Freedom Scheme was introduced from 6 April 2018"
Michelle Galpin

Further details of the budget changes can be found at:
https://www.gov.im/categories/tax-vat-and-your-money/income-tax-and-national-insurance/budget-2018/

The 2018 Isle of Man Budget, which was published on 20 February, set out a significant number of changes to different aspects of pension provision.

Trivial Commutation

From 6 April 2018 the limit on the size of pension pots that can be commuted on grounds of triviality was doubled from £50,000 to £100,000. This substantial increase comes just two years after the last change, when the limit was increased from £30,000 to £50,000 as part of the 2016 budget. Trivial commutations, which are available from age 55, are treated as income for tax purposes.

As a consequence of the trivial commutation limit changes, the maximum remnant lump sum amount is also increased to £100,000. This means that pension pots of up to £142,587 can be taken in full as cash; this is achieved by first commuting the maximum 30% tax-free lump sum, leaving a residual pension pot of £100,000, which can then be taken as a remnant lump sum.

Pension Contributions

The Isle of Man introduced an Annual Allowance of £300,000 in 2008. It has remained at this level for the last 10 years, but it was cut to £50,000 from 6 April 2018. As a result, the maximum tax relief on pension contributions is now limited to the lower of 100% of earnings and £50,000. In practice, this reduction is not expected to have a material impact since historically very few people have made contributions in excess of £50,000 pa.

National Insurance Changes

The Treasury Minister confirmed in his budget speech that the Isle of Man is still intending to abolish contracting out with effect from 6 April 2019. This will mean that the lower rate National Insurance contributions paid by employers and employees in contracted out employment will also be abolished.

The Minister also confirmed that the Isle of Man was still on track to introduce a new single-tier Manx State Pension in April 2019 and that State Pension Age in the Isle of Man should remain the same as in the UK for the foreseeable future.

Workplace Pensions

The Treasury intends to consider and consult on the possibility of introducing some form of workplace pension arrangements from 2020. However, no further details are currently available.

New type of Pension Scheme

Following on from a consultation about the potential introduction of "Pension Freedoms" last summer, a new type of pension arrangement, a Pension Freedom Scheme ("PFS") was introduced from 6 April 2018.

A PFS must go through the same approval process as other approved pension arrangements; it will first need to be authorised by the Financial Services Authority and then approved by the Income Tax Authority.

Changes from initial proposals

We summarised the initial proposals in the Quarter 4 2017 edition of Bandwagon. However there have been some changes. Only one PFS is available to a person at any one time. The annual contribution limit to a PFS is £50,000, rather than £5,000. In addition, the income tax relief on the contributions is available at a person's marginal rate, up to a maximum of 20%.

Some transfers to a PFS from other approved arrangements in the Isle of Man are permitted, but transfers from occupational defined benefit schemes or statutory schemes will not be allowed.

While there is no limit to the amount that can be transferred into a PFS, each transfer is subject to a 10% pension transfer fee. The Treasury has emphasised that this fee is not a charge to income tax.

Key Features of Pension Freedom Scheme

- a minimum retirement age of 55
- no maximum retirement age
- tax relief on contributions:
  - up to an annual contribution limit of £50,000; and
  - allowed at the member's normal rate of income tax
- pension growth builds up tax-free
- full access on reaching the scheme retirement age, including the ability to take the whole of the pension pot in one withdrawal or to take smaller withdrawals as required
- 40% tax-free lump sum
- remainder of funds are subject to income tax at the member's normal rate
- no tax on death
- 10% transfer-in fee

Reviewing Investment Management Charges

"Do these charges represent value for money?"
Carl Stanford

Background

It is important for pension scheme trustees to monitor whether the fees charged by their investment manager are reasonable. This is particularly important in defined contribution schemes, where charges are generally borne by the member and could potentially have a significant impact on their final retirement savings.

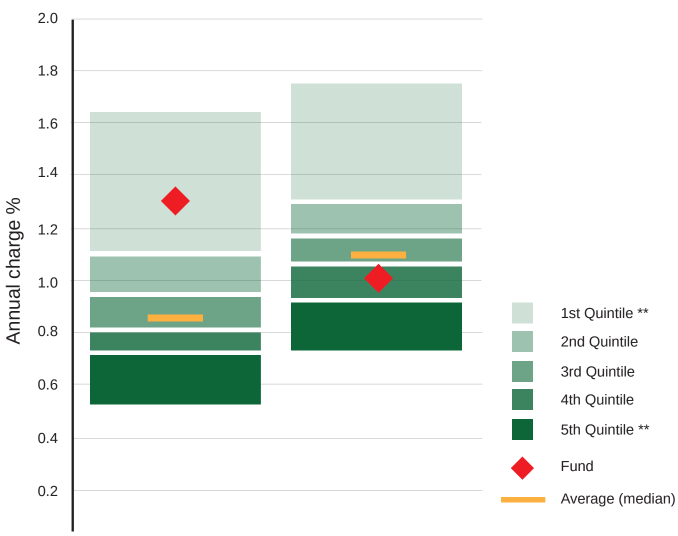
Guernsey's new pensions regulatory framework requires charges deducted from members' accounts to be reasonable and transparent*. Scheme members must to be notified where fees are deemed to be unusual or outside current market practice. However a stronger test is do these charges represent value for money?

Value for Money

A value for money assessment considers the level of the charges in conjunction with the quality and scope of the services provided, comparing them with other options in the market.

For example, a fund may not have delivered value for money even if its charges were average but it had suffered from poor performance. Equally, a fund with modest outperformance but well above average charges might also be considered to be poor value for money.

Trustees of UK pension schemes must check charges borne by members annually to see if they represent value for members. This assessment covers all member borne charges, including administration, governance and investment management charges.



Data source: Morningstar: Schemes qualifying for institutional share classes

Enforcement action on "Closet Trackers"

A recent investigation by the Financial Conduct Authority (FCA) into UK domiciled funds resulted in compensation of £34m being paid to investors who have overpaid for "Closet Tracker" funds. These funds provided index tracking performance but charged active management (higher) fees.

Normally when considering poor value for an active fund, attention is drawn to a high level of charges or poor performance. However in these cases neither of these may have applied; the funds involved were providing poor value for money, compared to the cost of index tracking funds, which would have very much lower fees. The FCA looked into 84 potential closet tracker funds and demanded changes to the marketing material of 64 of them to improve transparency for their clients.

The FCA has estimated that there is about £109bn sitting in "partly active" funds which are charging fully active fees. While these funds may be adequately disclosing how they invest, they may still be providing poor value for money.

Charges Review

To avoid similar issues, trustees may wish to carry out a review of charges. This includes an assessment of whether the existing investment management charges represent good value, as well as considering some or all of the following:

- total charges including, where possible, transaction costs
- performance delivered net of fees
- level and quality of services provided
- cost of equivalent funds

The chart illustrates the results of a charges review for two different funds. It shows the actual fees on each fund, relative to the range of fees available within that market sector. The funds are ranked by their charges; a position higher up the chart reflects higher charges.

In this example the US Equities Fund's charges were above the sector average and in the top 20% most expensive funds. However, the Emerging Markets Equity Fund had below average charges. This information, taken together with the performance and level of service provided, would determine if the fund represented value for money.

A charges review also provides an opportunity to consider whether any scale discounts would be available on charges. In view of the growth in investments, better terms may now be available.

* Sections 10.1 and 10.12.1 of the GFSC's Scheme Rules (No 2) 2017

** The top and bottom 5% of funds have been removed

Over-optimistic life expectancy projections?

"the rate of improvement appears to be slowing"
Stacey Wilen

Background

Until relatively recently, the media has regularly reported that people are living longer than previously anticipated, as mortality rates continued to fall; to put it another way, average life expectancy has been continuing to increase.

Evidence is now emerging which suggests that the rate of improvement in mortality rates is slowing down. Initially it was dismissed as a "blip". However, what is turning out to be quite a long blip, is making many ask:
"Are we seeing the start of a new trend?"

The Continuous Mortality Investigation (CMI)

The CMI (a body supported by the Institute and Faculty of Actuaries) carries out ongoing analysis of death data in the UK. The results feed through to the regular publication of updated mortality rates, and future improvement projections. The CMI's latest projection model, which was published in March 2018, is referred to as "CMI 2017". This showed that the mortality rates observed in 2017 were higher than predicted by the previous version of the projection model, CMI 2016. CMI 2016, in turn, showed that mortality rates in 2016 were higher than suggested by CMI 2015.

Reduction in mortality improvements

Over the period from 2000 to 2011, the rate of improvement in UK mortality rates was fairly stable from year to year, averaging around 2.7% pa for males and 2.2% pa for females. However, since 2011, the rate of improvement has been significantly lower than this, at around 0.5% pa for males and 0.1% pa for females.

What does this mean in practice?

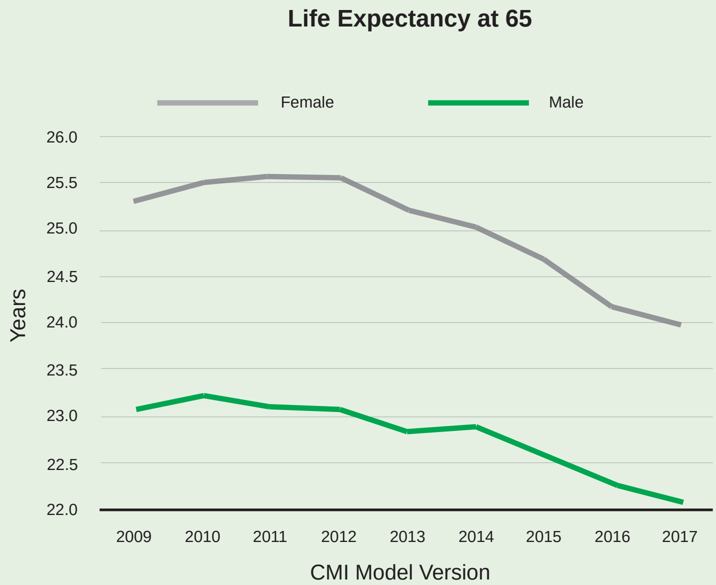
Changes in projected mortality rates can best be illustrated by considering the impact on implied future life expectancies – that is how long, on average, someone of a particular age and gender is expected to live. The chart illustrates life expectancies at age 65 implied by the various versions of the CMI projection model.

It demonstrates that, all else being equal, more recent versions of the projection model result in lower assumed life expectancies for both males and females. In particular, comparing CMI 2017 with CMI 2014, projected future life expectancy has reduced by 10 months for males and by 12 months for females.

Will this trend continue?

There is a lot of debate as to the cause of the recent reduction in mortality improvements; it is difficult to say whether the trend is likely to continue. However, there is some evidence to suggest that medium or long-term influences could be the reason. The general view among experts tends to be that mortality rates will continue to reduce, albeit at a slower rate than previously envisaged.

In other words, it is beginning to look like historical projections of future improvements in life expectancy may have been over optimistic. Life expectancy is not reducing currently, but the rate of improvement appears to be slowing considerably.



Source: CMI March 2018 Briefing note on CMI 2017

IAS19 Changes

"new volatility and extra complexity"
Matt Stanbury

Summary of changes

The International Accounting Standards Board ("the IASB") recently issued amendments to IAS 19 Employee Benefits, which will affect the accounting treatment of certain "Special Events" (amendments, settlements and curtailments) in defined benefit pension plans.

The amendments relate to the assumptions used to quantify the impact of a Special Event itself, together with the interaction of the impact of the Special Event with the asset ceiling requirements.

Background

Currently under IAS 19, if a Special Event occurs, entities should not adjust the assumptions used to calculate the current service cost and net interest during the remainder of the relevant reporting period, even if an entity remeasures the net defined benefit liability/asset as a result of that Special Event. However the IASB has now concluded that this approach is inappropriate.

Determining current service cost and net interest

At present the current service cost and net interest are calculated using actuarial assumptions determined at the start of the annual reporting period. However, in future when a Special Event occurs, an entity will need to:

- Determine the current service cost, for the remainder of the period after the Special Event, using the actuarial assumptions used to remeasure the net defined benefit liability asset after the Special Event

- Determine the net interest for the remainder of the period after the Special Event using:

  (i) the net defined benefit liability/asset reflecting the benefits offered under the plan and the plan assets after that Special Event; and

  (ii) the discount rate used to remeasure that net defined benefit liability/asset

The IASB expects that using updated assumptions will provide useful information to users of financial statements.

Effect on asset ceiling requirements

Where the defined benefit plan has a surplus, the net defined benefit asset is measured as the lower of the surplus and the asset ceiling.

Accounting for a Special Event may reduce or eliminate any surplus, which may then cause the effect of the asset ceiling to change.

The IAS 19 amendments clarify that any past service cost, or a gain or loss on settlement, should be determined first without considering the effect of the asset ceiling. This amount is recognised in profit or loss.

The effect of the asset ceiling after the Special Event should then be determined. Any change in that effect (excluding amounts included in net interest) is recognised in Other Comprehensive Income ("OCI"). This means that entities might have to recognise a past service cost, or loss on settlement, which reduces a surplus that was not previously recognised. This could lead to some unusual situations, such as the position illustrated in the following example.

Example

Consider a company with a defined benefit plan, with assets of 100 and a defined benefit obligation (DBO) of 90. Due to the impact of the asset ceiling the company is not able to recognise the surplus of 10.

The company then settles the plan. However, the amount of plan assets it transfers to settle its DBO is 100.

As a result, the company would need to record a loss of 10 on settlement in the profit or loss account. The assessment of the asset ceiling is then carried out as a separate step from the calculation of the settlement loss. The company reverses the effect of the asset ceiling separately through the OCI.

Effect on Company Accounts

These changes have the potential to introduce new volatility and extra complexity to company accounts. Even small changes to a pension plan could trigger a major knock-on effect on the profit and loss account. The effect on profit could be positive or negative and will depend on market conditions at the time the Special Event occurs, making results unpredictable.

Transition and effective date

The IAS 19 changes must be applied prospectively to Special Events occurring on or after the beginning of the first annual reporting period commencing on or after 1 January 2019. While earlier application is permitted, companies do not need to take any action until next year. However, where a Special Event may be on the horizon sometime over the next year, it would be worth considering if it would be preferable, from an accounting perspective, if it were to occur before or after 1 January 2019.

Jargon Buster

Current service cost
The increase in the present value of the defined benefit obligation resulting from employee service in the current period

Curtailment
A significant reduction by the entity in the number of employees covered by a plan

Defined Benefit Obligation (DBO)
The present value of the accrued scheme liabilities at the measurement date

Net Interest Cost
The change during the period in the net defined benefit liability/asset that arises from the passage of time

Past service cost
The change in the present value of the defined benefit obligation for employee service in prior periods, resulting from a Special Event

Settlement
A transaction that eliminates all further legal or constructive obligations for part or all of the benefits provided under a defined benefit plan, other than a payment of benefits to, or on behalf of, employees that is set out in the terms of the plan and included in the actuarial assumptions.

Special Event
A plan amendment, curtailment or settlement

Guernsey News

Insurance Regulations Update

As an international finance centre, it is important that Guernsey keeps pace with international standards in insurance regulation. These standards, which are issued by the International Association of Insurance Supervisors (IAIS), are set out in the Insurance Core Principles (ICPs).

The Guernsey Financial Services Commission (GFSC) issued a consultation paper on 17 April 2018 putting forward a number of changes to the current regulations. The proposals aim to enhance the transparency of the regulatory regime, as well as providing internationally comparable levels of protection to retail customers of insurance products.

The consultation period runs until 29 May 2018 and discussions between the GFSC and industry (represented by the Guernsey International Insurance Association (GIIA)) are in progress.

Given the diverse nature of the insurance business in Guernsey, it is important that a balance is struck between applying insurance regulation in a proportionate manner, whilst still providing protection to the policyholders and supporting Guernsey's reputation as an international centre for (re)insurance.

The consultation addresses the following specific areas :

- Public disclosure
- Guidance on reinsurance and risk transfer
- Conduct of business rules for insurers
- Own risk and solvency assessment
- Frequency of regulatory reporting
- Guidance on the qualifying criteria for Insurance Category 6
- Majority shareholder controller notification

The full consultation paper is available on the GFSC's website. https://www.gfsc.gg/sites/default/files/20180413%20-%20Insurance%20CP%20-%20FINAL.pdf

We will provide a further update in a future Bandwagon article.

For more info please contact Clair Le Poidevin (clepoidevin@bwcigroup.com)

Tax-free lump sum increase

While up to 30% of the value of benefits from a Guernsey approved pension arrangement can be taken as a retirement lump sum, the amount which is tax-free is subject to a monetary limit. Any excess over this limit is subject to income tax.

It has recently been announced that this limit has been increased from £188,000 to £194,000. The increase will apply retrospectively from 1 January 2018.

For the purposes of applying the monetary limit, the cumulative amount of all lump sums received since 1 January 1998, from approved pension arrangements in Guernsey, need to be considered.

Jersey News

Regulation of Transfers

The Jersey Financial Services Commission (JFSC) is seeking to clarify the current regulatory treatment of pension transfer advice in Jersey, which it believes to be "somewhat unclear and has some gaps".

The JFSC issued a consultation paper on 4 April on the proposed extension of Jersey's Investment Business regime to bring into scope the regulation of advice given in relation to the exercising of a right under a defined benefit scheme to "acquire, dispose of or underwrite or convert such defined benefit scheme".

The consultation document highlights the JFSC's concerns over the suitability of the advice in some cases. In particular, it has highlighted that the risks associated with the transfer may not have been explained adequately.

The consultation period ran for just two weeks and the order to introduce the proposals by an amendment to the Financial Services (Jersey) Law 1988 is expected to come into force shortly. There will be a three month transitional period to give those who are not currently regulated, and who wish to provide investment advice on transfers going forward, the chance to apply to be registered to carry on investment business.

Employers' Disability Charter

Alison Hawkins

We are delighted to be able to announce that BWCI has recently signed up to the Guernsey Employment Trust's Employers' Disability Charter, demonstrating our commitment to offer equal opportunity employment for those with disabilities.

We have worked with Guernsey Employment Trust (GET) on numerous occasions in the past to help support people into work who may not otherwise have had the opportunity to do so due to their disability.

Alison Hawkins, BWCI's Senior HR Manager said, *"We are committed to leading by example to encourage other employers to take up the charter, and to continue to grow our inclusive culture."*

Under the charter we have undertaken to adhere to a range of commitments around our own employment and recruitment practices in relation to disabled people in Guernsey, including signing up to the guaranteed interview scheme, and providing disability awareness training for our staff. In addition, under the charter we have made a commitment to provide assistance to individuals who are registered with GET, if they feel that they need help to understand their employer's pension scheme.

If you would like to know more about the charter, further details can be found at http://www.get.org.gg/employers

Save the date

This year's BWCI Mini Soccer festival will take place on the weekend of 21 and 22 July.

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