PENSION SCAMS - GOVERNMENT UNVEILS NEW MEASURES IN THE FIGHT AGAINST FRAUD

We offer a perspective on the Government's recent response to the pension scams consultation.

COLIN CLARK

Colin's career in pensions spans over 30 years. In his current role as Proposition Development Manager he oversees a broad spectrum of closed pension products, focusing on delivering against Lloyds Banking Group's commitment to maintain its proposition and fair treatment for longstanding customers.

HM Treasury and Department for Work and Pensions have published their joint response to the pension scams consultation. Unfortunately whilst the package announced in August contains some welcome initiatives, important details and timelines still need to be agreed and doubts remain on its overall effectiveness.

The consultation was launched in December 2016 but the issue of pension scams has been a major concern since at least February 2013 when The Pension Regulators' 'Scorpion' campaign was launched. Since then we've seen Project Bloom (the cross-Government multi-agency task force set up to tackle pension fraud) and the FCA's own ScamSmart initiative. In 2015 an industry code of good practice was published, aimed at strengthening trustee/administrator due diligence for pension transfers and outlining good practice for customer communications, warnings and discharge of liability.

Despite this, tangible progress towards protecting vulnerable pension customers has not been as rapid as many would have liked. And scams continue to be a blot on the pension landscape and wreck people's retirement plans.

THE RESPONSE TO THE DECEMBER 2016 CONSULTATION

First off the Government wanted to agree on a clear definition for pension scams to assist identification, record-keeping and prevention. It has achieved this objective.

AGREED PENSION SCAMS DEFINITION:

The marketing of products and arrangements and successful or unsuccessful attempts by a party (the 'scammer') to:

- release funds from an HMRC-registered pension scheme, often resulting in a tax charge that is not anticipated by the member
- persuade individuals over the normal minimum pension age to flexibly access their pension savings in order to invest in inappropriate investments
- persuade individuals to transfer their pension savings in order to invest in inappropriate investments
- where the scammer has misled the individual about the nature of, or risks attached to, the purported investment(s), or their appropriateness for that individual investor.

Now let's look at a quick summary of what was announced to combat pension scams. We can see three key proposals:

1

Banning cold calling in relation to pensions

A number of different types of phone conversation are proposed to fall within the scope of the ban including:

- offers of a 'free pension review', or other free financial advice or guidance
- assessments of the performance of the individual's current pension funds
- inducements to hold certain investments within a pensions tax wrapper including overseas investments
- promotions of retirement income products such as drawdown and annuity products
- inducements to release pension funds early
- inducements to release funds from a pension and transfer them into a bank account
- inducements to transfer a pension fund
- introductions to a firm dealing in pensions investments
- offers to assess charges on the pension
- offers to trace lost pension pots
- offers to consolidate pension pots

The ban will cover electronic communication – texts and emails.

There will be no ban imposed in relation to the cold calling on all investment products.

The ban will not be limited to transfers between pension schemes – it will also cover scenarios where consumers are encouraged to release funds from a pension – perhaps using the new pension freedoms options – and transfer this to a bank account, before investing in an inappropriate product.

There will be limited exemptions to the ban where:

- a consumer has expressly requested information from a firm
- an existing client relationship exists.

The ban will not prevent firms from issuing pensions-related marketing material to the public via traditional or social media.

The Information Commissioners Office (ICO) will enforce the ban.

There will be no criminal sanctions and custodial sentences applied as part of this legislation and ICO cannot take action against overseas firms, unless the calls are made on behalf of a UK company.

The Government will work with ICO to ensure consumers can easily report cold calls.

There will be further activity to inform consumers about the ban and the need to be wary of fraudsters.

Next steps

The Government will work on the final details of the ban during the course of 2017 and will bring forward legislation when Parliamentary time allows.

OUR VIEW

The cold-calling ban grabbed the most headlines when the response was published but is arguably the least effective of the measures announced and the one with the most detail still to come 'when parliamentary time allows'.

There was widespread support for this during the consultation because everyone recognises the damage that pension scams do and few consider that pensions cold-calling offers positive benefits.

However the real value of any 'ban' is more likely to attach to an effective consumer awareness campaign and the deterrence or disruption of scamming activity rather than any realistic hope of prevention or punitive enforcement, particularly in the absence of criminal sanctions or the threat of a prison sentence.

Determined scammers may view the threat of a fine with equanimity or simply move operations offshore to escape the reach of the ICO.

SUGGESTED ACTIONS

We will wait with interest for further details to emerge. Of particular concern will be how the Government can deliver on its stated intention of 'future proofing' the legislation so that it addresses the potential development of scam activity designed to circumvent the ban, whilst at the same time not disrupting legitimate activity and business development. Making the reporting of scams easy – and worthwhile – may also be a challenge.

Readers may also be interested to consider an alternative view on this from Aries Insight's Ian Neale. This can be accessed here: http://www.ariesinsight.co.uk/webfront/vlogpod.htm

2

Limiting the statutory right to transfer

The statutory right to transfer will be limited to:

- transfers in to personal pension schemes operated by firms authorised by the Financial Conduct Authority (FCA)
- transfers in to authorised Master Trust schemes
- transfers where a genuine employment link to the receiving occupational pension scheme could be evidenced.

Scheme members will be primarily responsible for providing evidence of earnings demonstrating an employment link.

Next steps

The Government will actively engage with industry, consumer groups and other stakeholders on how best to implement the employment link and also add overseas transfers to QROPS to the statutory transfer criteria. It will also consider whether 'due diligence' for scheme trustees/managers should be enshrined in legislation; and, in an apparent contradiction to the policy objective, whether trustees or managers should have the power to amend their scheme rules in order to accommodate legitimate non-statutory transfers where there is no such power already.

The master trust authorisation regime won't be fully rolled out in 2019. Legislation to cover the new statutory right will need to align with the roll out of the authorisation regime.

An appropriately drafted statutory right to transfer is a sensible move.

OUR VIEW

Strengthening pensions legislation alongside the other measures proposed is useful in terms of supporting the principle of freedom and choice for consumers.

We agree that an appropriately drafted statutory right to transfer is a sensible move. It restores the position that was widely understood before February 2016's High Court judgment on Hughes vs Royal London overturned this so in theory should be relatively simple to reinstate into due diligence activity.

Once again though the devil is in the detail and how effective this measure is will depend on the exact requirements for providing evidence of an employment link.

Our experience shows that determined scammers will seek and often find ways to circumvent legislation. Reliance on legislation to prevent scams also places an onerous burden for 'policing and prevention' on pension scheme trustees/managers; this has proved to be inefficient and/or ineffective despite best efforts.

It delays the transfer process, which nevertheless remains subject to the standard statutory timescales (unless exceptionally an extension is granted), and causes an increased volume of complaints. Overall it requires diversion of significant technical and legal resource, ultimately to the detriment of the majority of consumers and shareholders.

Plans to extend the new statutory rights to include QROPS are welcome. Without this all transfers to QROPS would also be subject to the full rigours of lengthy due diligence which would be impractical. There are suggestions that some QROPS are used for pension scam activity and this may be a particular problem for schemes/customers based in the EU, where the HMRC criteria are less stringent and there is no overseas transfer tax charge. Brexit may change all that; meanwhile we expect to continue viewing all overseas transfers, regardless of residence or destination, as worthy of additional warnings, including the risks of pension scams.

SUGGESTED ACTIONS

Again there is little alternative but to wait for further details to emerge. Meanwhile signposting delays in making changes to strengthen legislation are never ideal as this can encourage the very kind of activity that the amendments seek to prevent.

3

Making it harder to open fraudulent schemes

Changes to scheme registrations

All new occupational pension scheme registrations are to be made through an active company. HMRC will be given discretion to register legitimate schemes with a dormant sponsoring employer. There will be a right of appeal for rejected scheme registrations.

This will extend to existing pension schemes registered with a dormant sponsoring employer, with the same discretion so that HMRC can decide not to de-register a legitimate dormant employer scheme.

Draft legislation for this has been published and it will appear in the 'Winter' Finance Bill in 2017.

Consent of the sponsoring employer

Sponsoring employers will need to consent to the opening of a new occupational scheme with their support.

SSASs

For SSASs, the Government will not pursue the option to require pensioneer trustees.

OUR VIEW

Stronger powers in relation to the 'dormant employer' are welcome but a determined scammer could find ways to circumvent this.

It is also unclear the extent to which HMRC will be able to exercise its new (de)registration powers in relation to dormant employers – whether for new or existing schemes. In practice this may be another measure intended more as a deterrent because there are sure to be a number of genuine schemes that have dormant employers and HMRC will need to be very clear on grounds for deregistration in particular or face challenge.

Furthermore the penalties for deregistration – the removal of tax reliefs and imposition of a deregistration charge – fall on the victim rather than the perpetrator and there must be some doubt as to the likelihood of any or all of this money being recoverable where a scam has been perpetrated.

This could also complicate due diligence processes. Where there are doubts about the employer status HMRC may be less likely to confirm that the scheme is registered and revert to the non-committal stance of 'neither confirming nor denying' that the scheme is registered.

> The real value of any 'ban' is more likely to attach to an effective consumer awareness campaign

SSAS

Perhaps the most disappointing aspect of the response concerns SSAS. Whilst we don't support the nuclear option of banning SSAS, we think stronger measures could and should have been taken against rogue schemes.

It's widely accepted that single member SSAS have been the vehicle of choice for scammers and many industry commentators have called for governance and regulatory oversight to be strengthened in this area – remember single member schemes don't even have to register with The Pensions Regulator.

It's strange that the Government resolutely refuses to require additional safeguards for SSAS at a time when we see increased governance and oversight requirements elsewhere.

The Government says this is because scheme members should be free to choose their own investments. But they can also do this with SIPPs which are subject to stronger FCA regulation and oversight. Most would agree that this is suitable in terms of protecting customers and strengthens consumer confidence.

To leave SSAS free of any comparable oversight is tantamount to saying that the Government believes scheme members should be able to choose to circumvent measures designed for their own protection and leaves them more exposed to scams.

It's true that HMRC introduced the 'Fit and Proper' test for scheme administrators with effect from 1 September 2014. Since then the number of new scheme registrations has fallen by 12% (2016/17) according to HMRC's own statistics but fraudulent schemes persist.

SUGGESTED ACTIONS

We don't expect HMRC to deregister swathes of existing dormant employer schemes from 6 April 2018 and legitimate schemes should be safe. However advisers might want to consider reviewing existing schemes. Where such schemes are dormant, could be wound up and/or benefits transferred or otherwise secured for the members, now might be a good opportunity to explore options.

CONCLUSION

There is clear consensus that action needs to be taken now to combat pension scams.

As I write the Work and Pensions Committee has announced an inquiry into Pension Freedoms and one of its areas of focus will be how freedom and choice to cash in pensions has played into the hands of scammers, determined to find new ways to liberate pension savers of their retirement savings.

We think more could be done to combat scams, especially in the SSAS space and current timescales are not sufficiently urgent. And the onus should be less on pension providers and scheme trustees as pension transfer gatekeepers.

A sustained programme of consumer engagement, information and awareness should be pursued. More attention should be given to highlighting the risks for UK resident customers of unregulated offshore advice and use of pension vehicles such as QROPS and the potential for poor outcomes and tax penalties arising from high risk or fraudulent offshore investments.