



Deloitte Finance Club
The community for Financial
Controllers and senior financial
executives

Wednesday, 22nd October 2014



Deloitte Finance Club

A few facts

- Established in **May 1997** as the *Financial Controllers' Club*, and renamed **Deloitte Finance Club** in 2013
- Provides an **annual programme of technical updates and hot topic briefings**
- Connects our members to relevant experts as well as over **2,200 members** across the country

Deloitte Finance Club

Upcoming programme

- **Key trends and developments in the UK insurance market**
Wednesday, 19 November 2014 – 5:30pm-7:00pm (arrivals from 5pm)

- **Holiday finance checklist 2014**
Wednesday, 10 December 2014 – 8:30am-10:30am (arrivals from 8am)

Managing pensions risks & costs and Tax update

Agenda

- **Bill Dodwell** – Tax update
- **Amanda Swaffield** – Annual report insights 2014
- **Paul Geeson & Neil Campbell** – Managing pensions risks & costs



Deloitte Finance Club Tax update

Bill Dodwell



Tax update

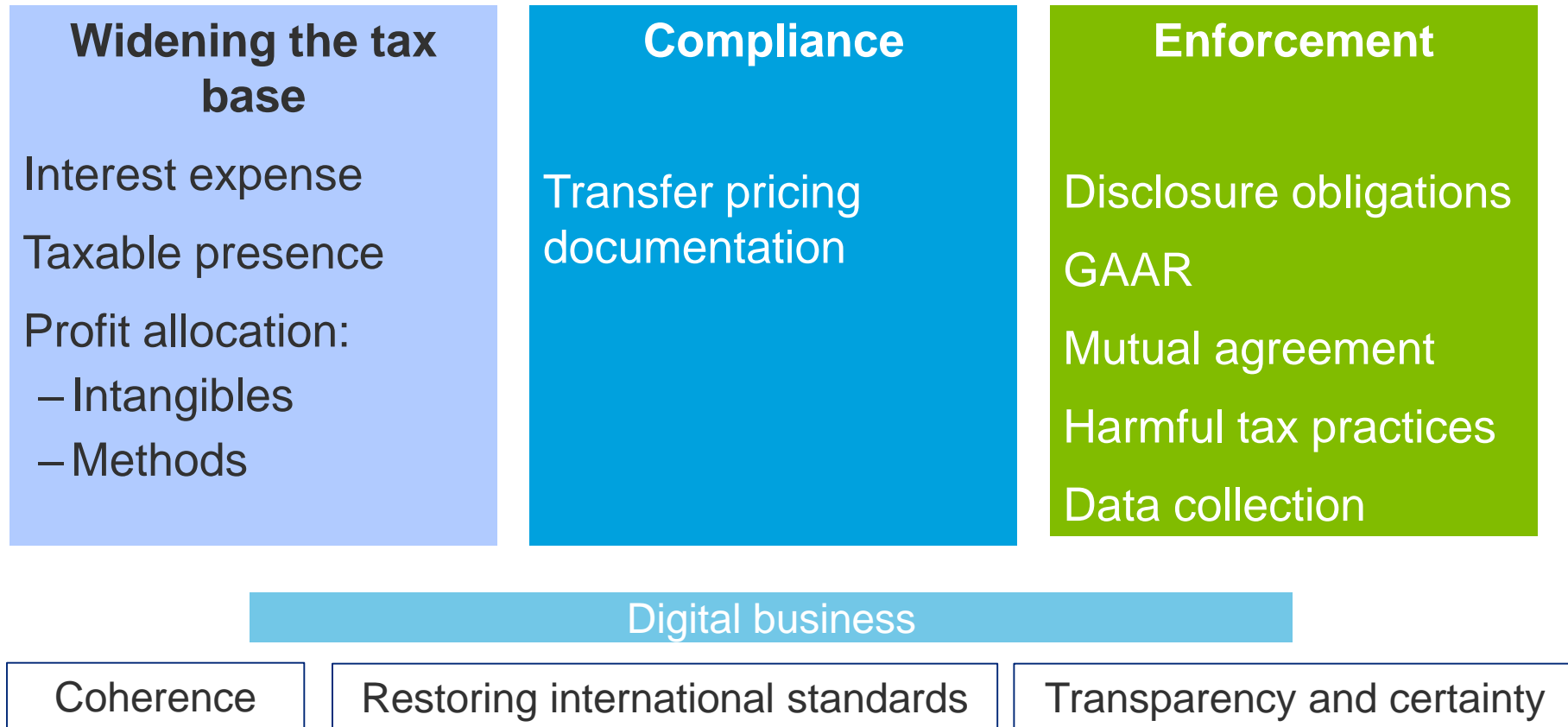
Agenda

- Base Erosion and Profit Shifting: update
- General Election 2015: Party policies
- Devolution

Base Erosion and Profit Shifting update

OECD BEPS Action Plan

Key themes



Timetable

September 2014

September 2015

December 2015

- **Digital economy**
- **Hybrid mismatches**
- **Treaty abuse**
- **Transfer pricing documentation**
- **Transfer pricing of intangibles**
- **Harmful tax practices**
- **Multilateral instrument**

- Permanent establishments
- Transfer pricing of intangibles, risks and capital, other
- CFC
- Disclosure of aggressive tax planning
- Dispute resolution
- Interest restrictions
- Data collection and analysis

- Interest (pricing)
- Harmful tax practices
- Multilateral instrument

Thinking about BEPS




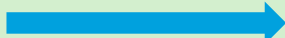
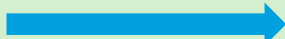
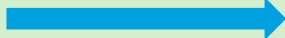
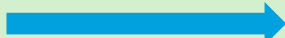
Transfer Pricing documentation

- Three-tiered global standard for transfer pricing documentation:
 - a **master file** containing high level standardised information relevant for all members of a multinational enterprise
 - a **local file** providing more detailed information relating specifically to material transactions of the local taxpayer
 - a **country-by-country report** for risk analysis
 - Turnover – related party/third party
 - Profit before tax
 - Tax
 - Employees, Tangible assets, Shareholders' funds
 - List of companies with activity codes
 - UK announces will introduce provisions

Hybrid Mismatches

- Report proposes removing beneficial impact of hybrids
 - Deduction, no income
 - Double deduction
- Commentary to enable domestic adoption will be issued no later than September 2015 and include examples, transitional rules if there are differing dates of implementation
- Work will continue on outstanding substantive points
- UK announces domestic consultation to be released 3 December

BEPS: next steps

October 2014 – April 2015		Discussion drafts
September 2015		Release 2015 Actions
Autumn 2015		International conference starts
December 2015		Final Actions
2016		OECD releases Model Treaty, Transfer Pricing guidelines
Countries implement measures		

Party policies

Labour Party



Conservative party

Raise the tax-free allowance from £10,500 to £12,500

Raise the 40p income tax rate from £41,000 to £50,000

Be tough on companies avoiding tax

The most competitive corporate taxes in the G20

Liberal Democrats

**New Council Tax
bands for
residential
properties worth
over £2 million**

**Increase CGT, cut
allowance to £2,500**

**Limit tax relief on
pensions to a
pension pot of £1
million**

**Review business
rates**

**Restrict access to
non-domiciled
status**

**Single tax free
threshold for both
income and capital
gains**

**Refocusing the
Entrepreneurs
Relief to ensure it
only helps genuine
entrepreneurs**

**Raise the tax free
personal allowance
to at least £12,500
by the end of the
next parliament**

Devolution

Scottish tax revenues 2013-14

Scotland has 8.5% of UK tax revenues
£41,894 billion

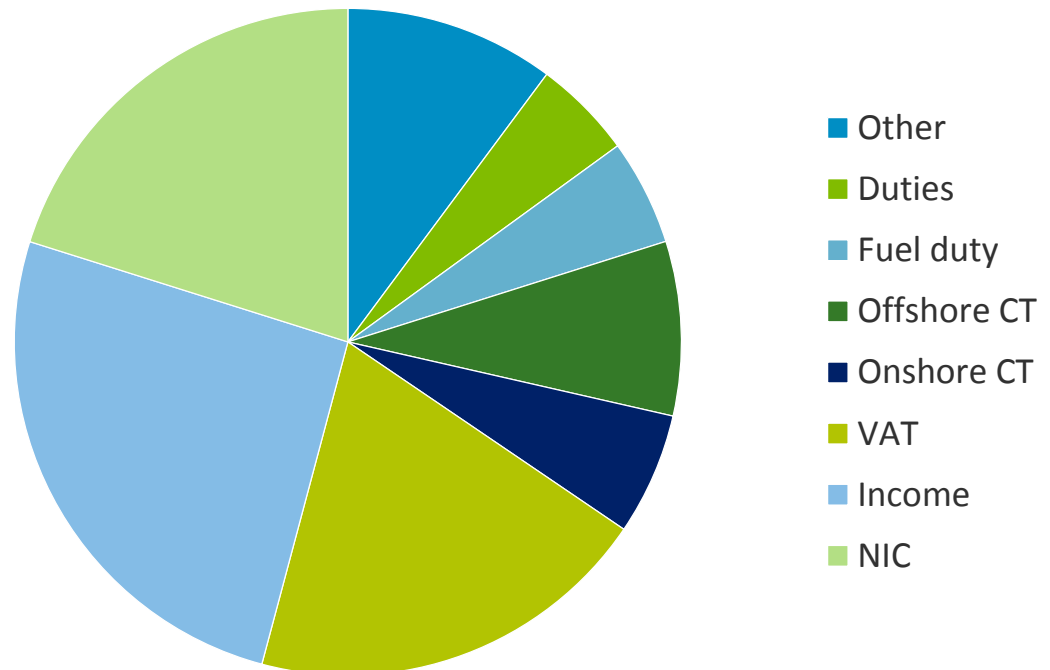


Above average:

- Tobacco
- Spirits
- Offshore CT

Below average:

- IHT
- SDLT
- Stamp duty
- Income tax
- CGT



Devolving tax to Scotland



Income Tax

Rates

Thresholds

Personal allowance

Tax base

NIC

Linked to welfare

VAT

EU law

Assign revenues?

Minor taxes

Air passenger duty?

Corporation tax

Ruled out in Westminster

Devolution of taxes

WALES



- SDLT and landfill tax
- Impact of Business Rates
- Varying income tax rates subject to referendum

NORTHERN IRELAND



- Consultation re devolving CT rate setting powers to NI Assembly in 2011
- Announcement at Autumn Statement?



Annual report insights 2014
Providing a clear steer

Amanda Swaffield



Annual report insights 2014

Providing a clear steer



- Survey of 100 UK listed companies' annual reports
- Examines narrative reporting, corporate governance disclosures and financial statements
- Regulatory overview and best practice examples
- Supporting publication which includes highlights from the full survey and ideas on how you can improve your annual report



www.deloitte.co.uk/annualreportinsights

Narrative reporting

Findings



64%

demonstrated some linkage in their report



80%

discuss value creation in their reports



9

the average number of principal risks presented

Good practice examples

Linkage:
SEGRO

Business model:
Rexam

Risks:
Domino Printing Sciences

How to improve

1

Comply with legal requirements e.g. strategic report approval

2

Clear linkage between strategy, KPIs and risks

3

Cut clutter e.g. performance review duplication

4

Take on board integrated reporting

Corporate governance

Findings



57% reported full compliance with the Code



23% of companies included the FBU statement process



15% of the directors in our sample were women

Good practice examples

Non-compliance explanation:
Johnson Matthey

FBU:
Spectris

Diversity:
M&S

How to improve

1

Include statements of application and compliance

2

Discuss diversity in its broadest sense

3

Focus on the activities of the board and not just processes

4

Early adopt new risk reporting

Financial statements

Findings



68%

used non-GAAP measures on the face of the P&L



44%

included a net debt reconciliation



6/10

Companies with goodwill but no sensitivity analysis had impairment as KSoEU

Good practice examples

Non-GAAP measures:
National Grid

Tax governance:
Weir Group

Key judgements:
Evrax

How to improve

1

Adopt new IFRSs, including package of 5

2

Clearly identify critical judgements and KSoEU that are consistent with other disclosures

3

Consider restructuring accounting policies

4

Volunteer a net debt reconciliation or tax governance info

A clear steer for your annual report

To help you ensure your annual report meets the needs of investors and other stakeholders



In order to reflect the differing appetites as to how far preparers want to go in improving their reports our tips are split into four levels:

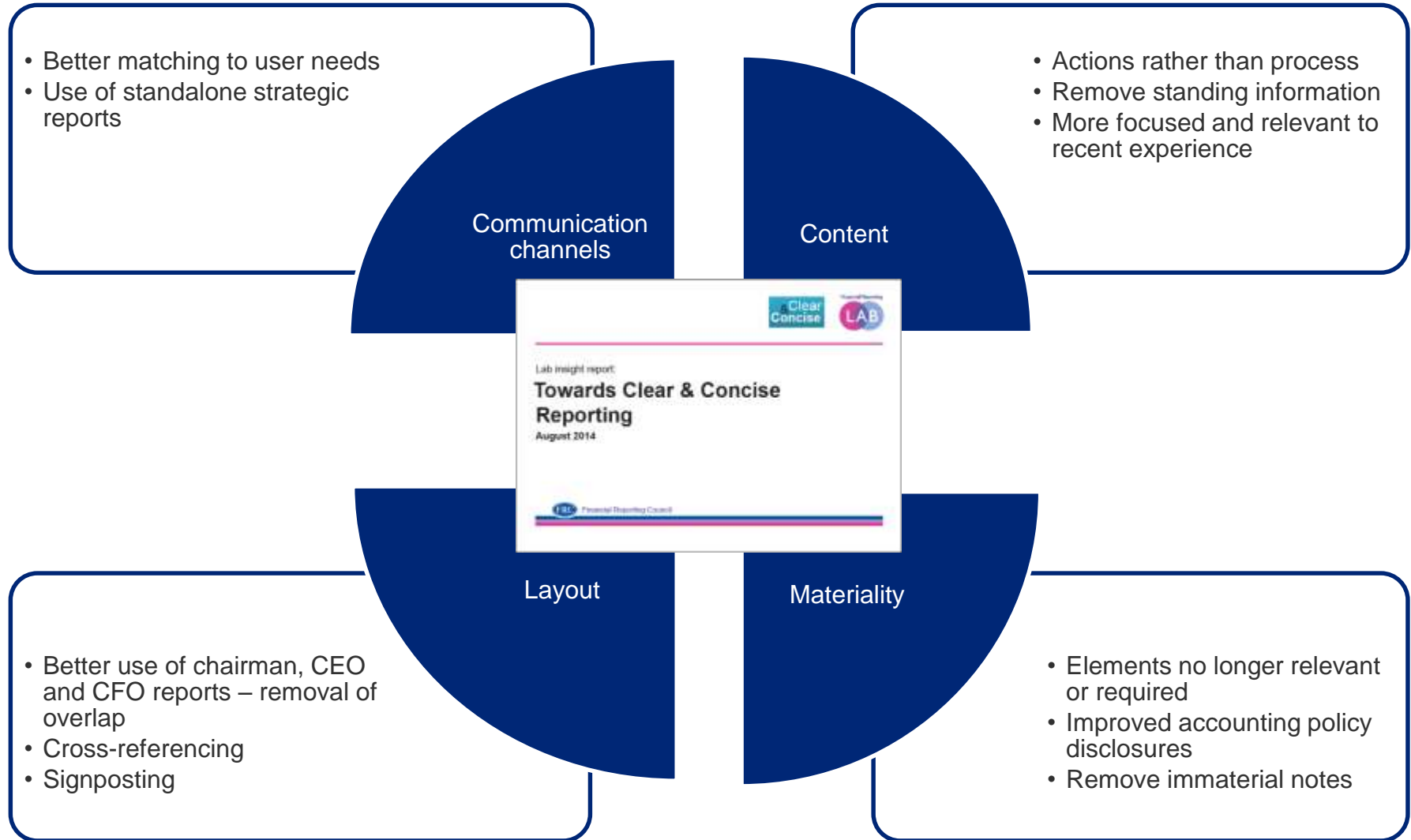
- 1** The bare minimum – complying with new and existing requirements plus key concerns of regulators;
- 2** Upping your game – looking at further regulatory areas of focus, including linkage;
- 3** Clearer communication – considering the qualitative characteristics of effective communication and ways to cut clutter; and
- 4** Going the extra mile



Eight questions for preparers to ask themselves as they strive to cut clutter from their annual reports.

The Financial Reporting Lab insight report

Observations on clearer & more concise reporting





Deloitte Finance Club
Managing pensions risks & costs

Paul Geeson
Neil Campbell



Managing pensions risks & costs

Agenda

1. Pensions risk management
 - Operational risk
 - Governance risk
 - Funding risk
2. 2014 Budget
3. *DBflex*



What is pensions risk?

- **Employer sponsored pensions landscape**

- Different types of workplace pensions
- Different structures and scheme designs
- New legal duties

- **Pensions risk definition**

“Future uncertainties that could impact on the employer’s achievement of its pensions objectives”

- **Objectives are defined by each employer, but typically might include**

- Controlling pensions costs
- Improving employee outcomes
- Regulatory and legislative compliance
- Supporting retention and recruitment
- Security of assets
- Managing pensions risks!

Who is responsible for managing pensions risk?

Trust based

- Employer established trust and appoints trustees
- Fiduciary duties
- Pensions Regulator
- Trustees have primary responsibility
- ...but Employer underwrites the scheme

Contract based

- Employer selects and appoints a regulated provider
- Regulated financial services product
- Financial Conduct Authority
- Employers have responsibility, but delegate via contract

Employers' Duties

- Legal obligation to assess the workforce and automatically enrol eligible jobholders
- Prescribes timescales, enrolment processes, comms and minimum benefits
- Fines for non-compliance

Pensions risk management

3 step approach



Identification

- Systematic reviews of employee pension arrangements
- Covering operations, governance and funding requirements

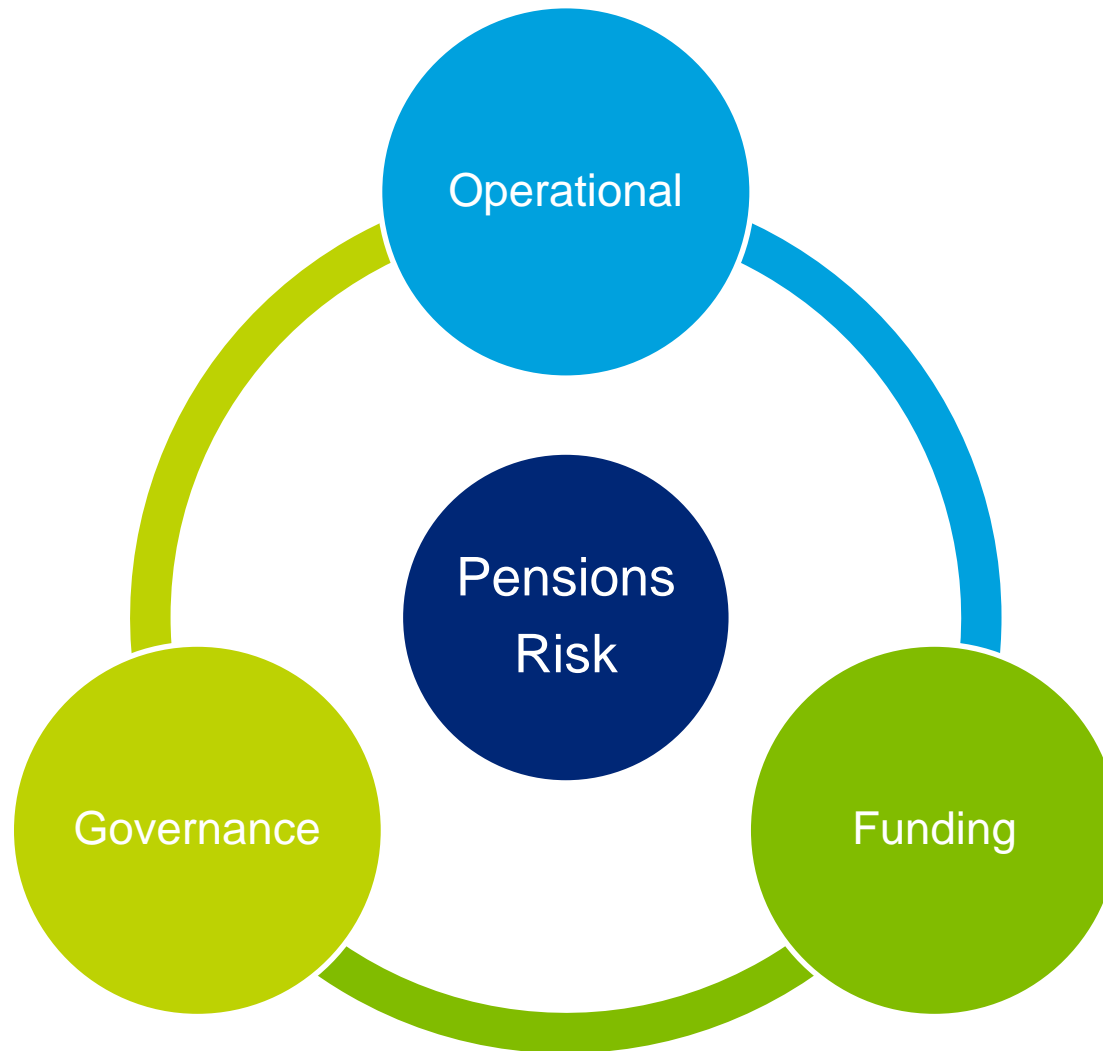
Analysis

- Quantification of risks identified and their potential to adversely impact agreed objectives

Control

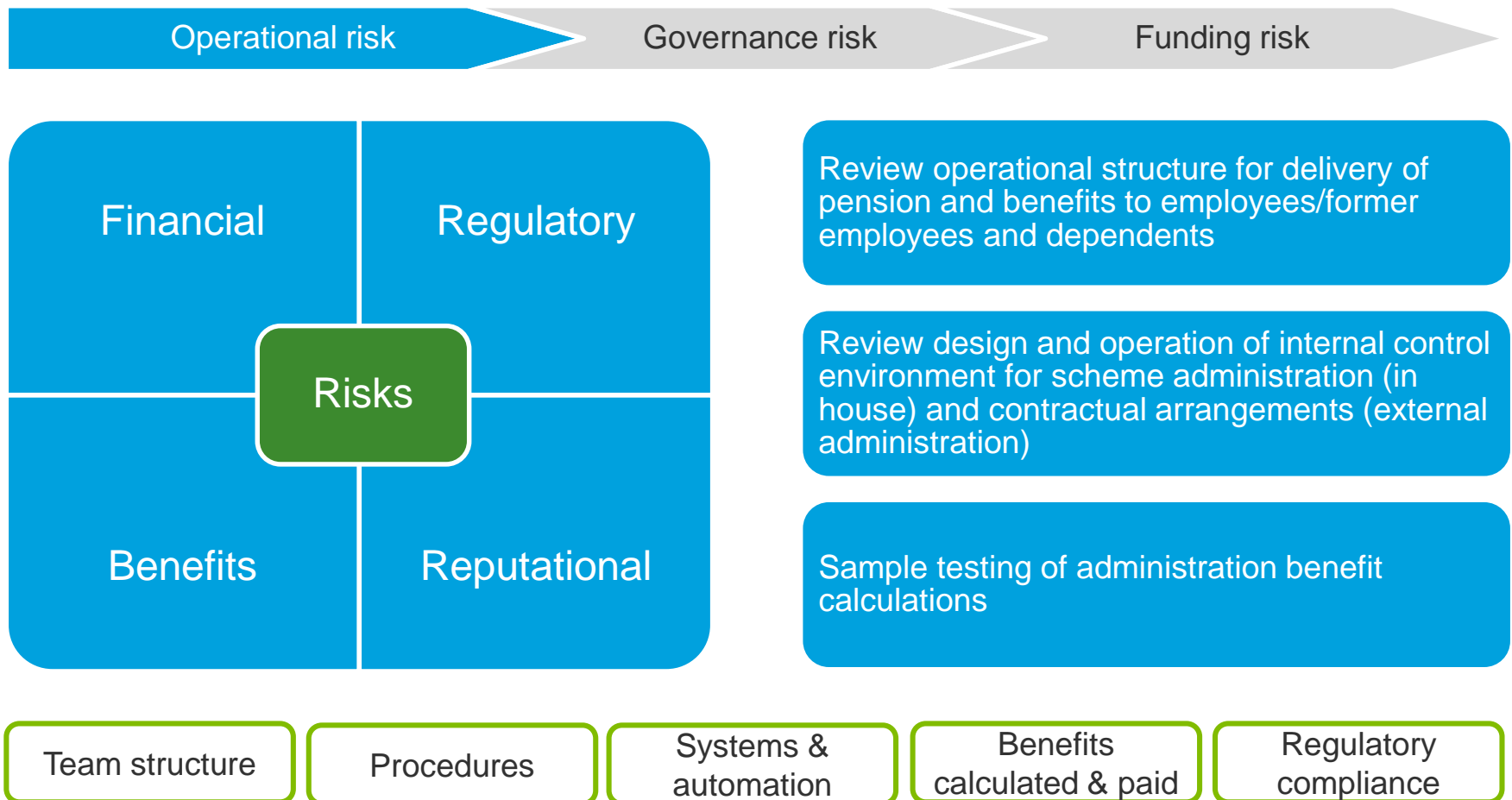
- Proportionate controls developed and implemented
- Ongoing monitoring of effectiveness of controls

Pensions risk areas

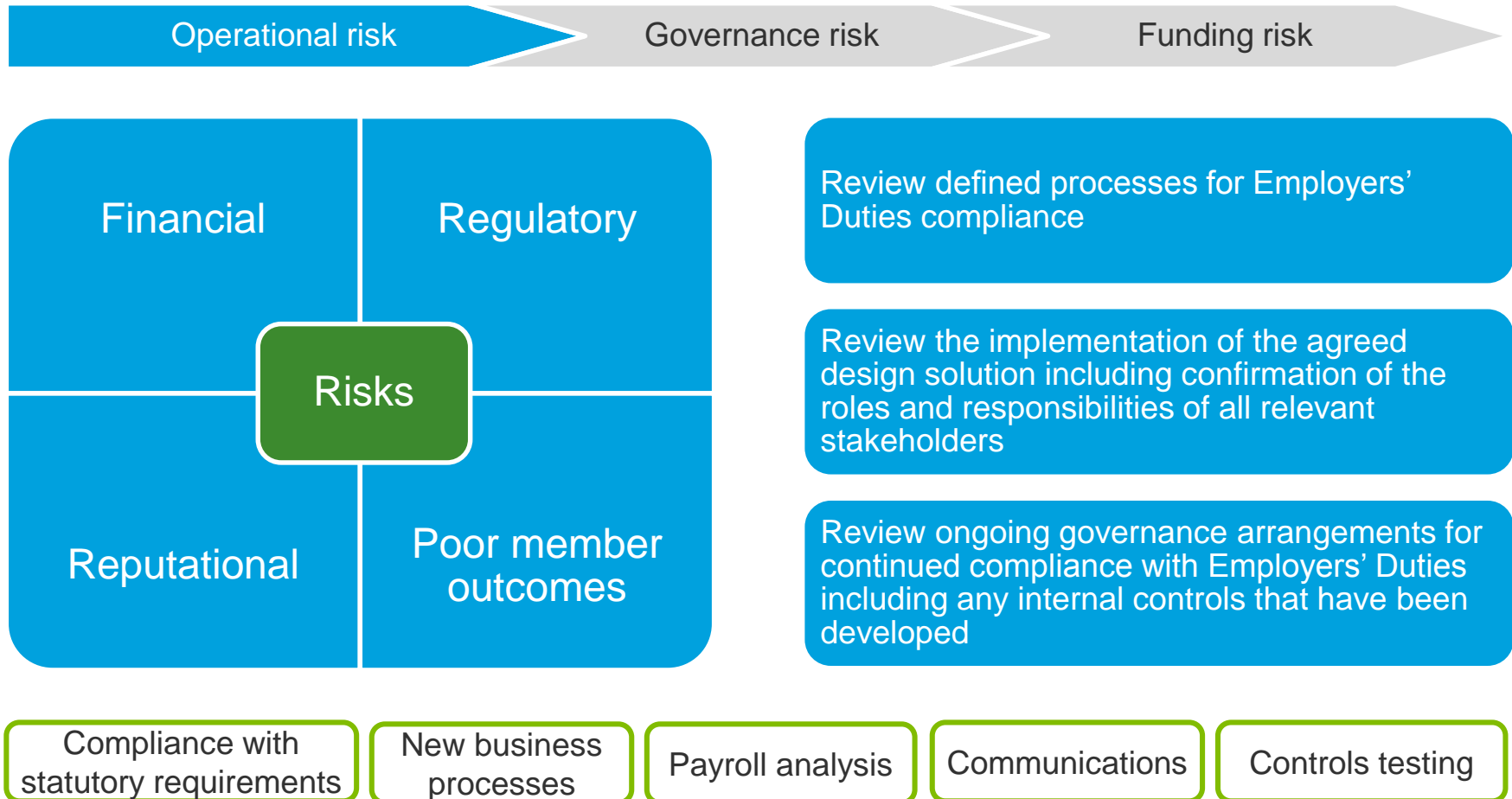


Operational risk

Operational risk



Employers' duties



Governance risk

Governance risk



Review pensions governance arrangements for both DB and DC provision, including corporate input into key decisions.

Review current Trustee governance arrangements and comparison with industry best practice.

Terms of reference

Decision making

Conflicts of interest

Risk management

Regulatory Guidance

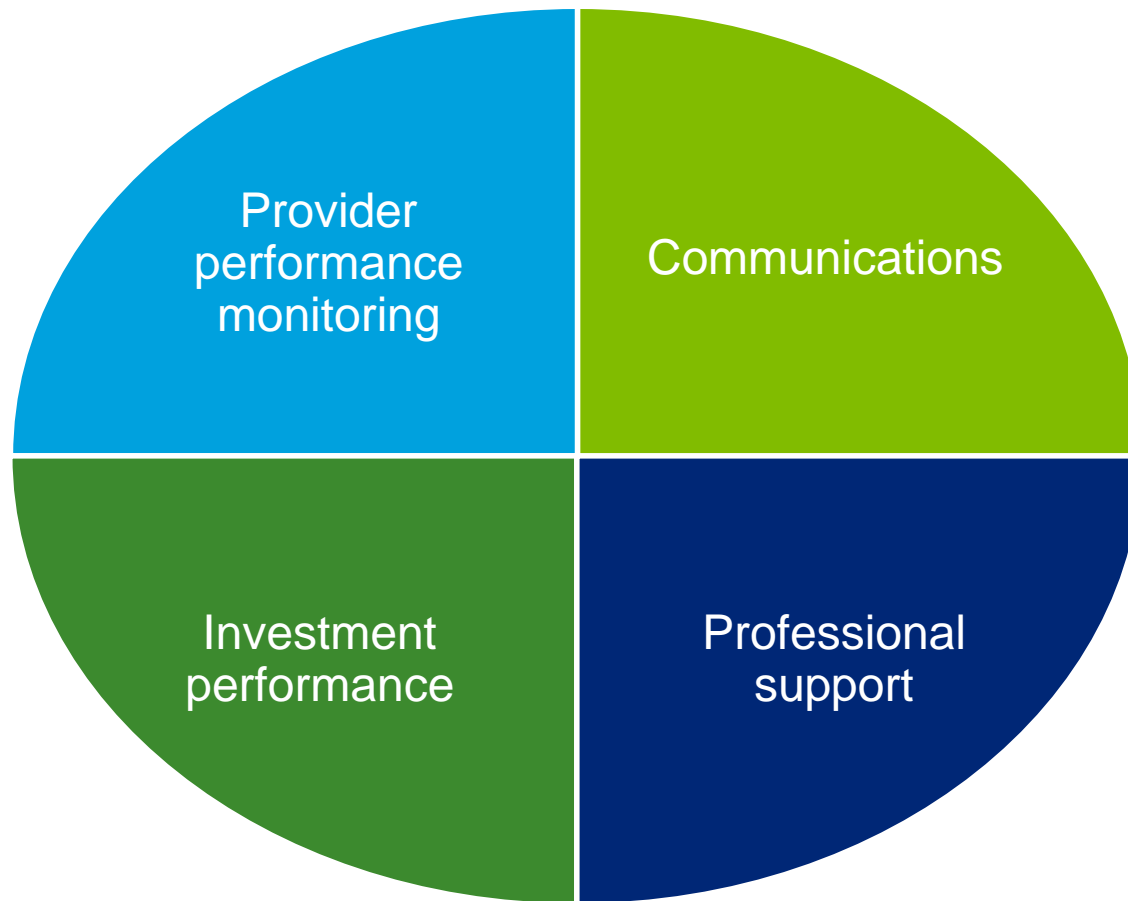
Communications

3rd party appointments

Employer level governance

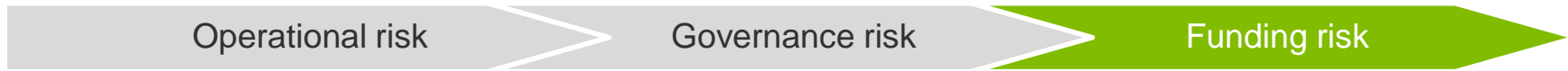
- Regulatory focus on good DC scheme governance
- Automatic enrolment increases the focus

- DC Code of Practice
- Pensions governance committee



Funding risk

Funding risk



Analysis of potential future volatility in the funding level(s) of defined benefit pension liabilities

Review funding basis of defined benefit pension liabilities and the alignment with investment strategy

Consider funding basis relative to covenant and sensitivity to changes in funding basis

Review the control environment for corporate sponsor input to the funding negotiations with trustees and investment strategy

Risk exposure of DB schemes

Value at Risk (VAR) analysis

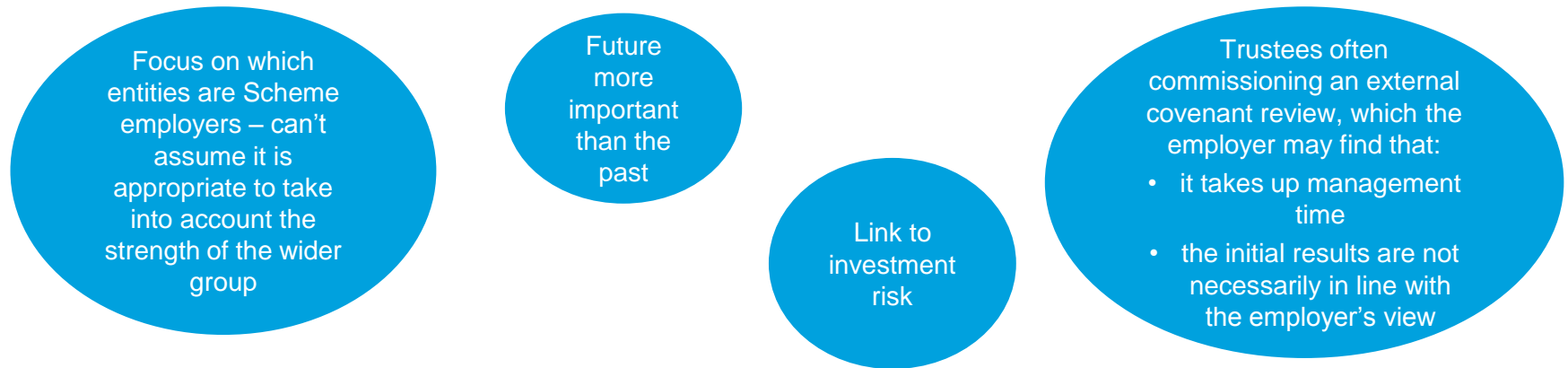
Governance of funding risk

3rd party appointments

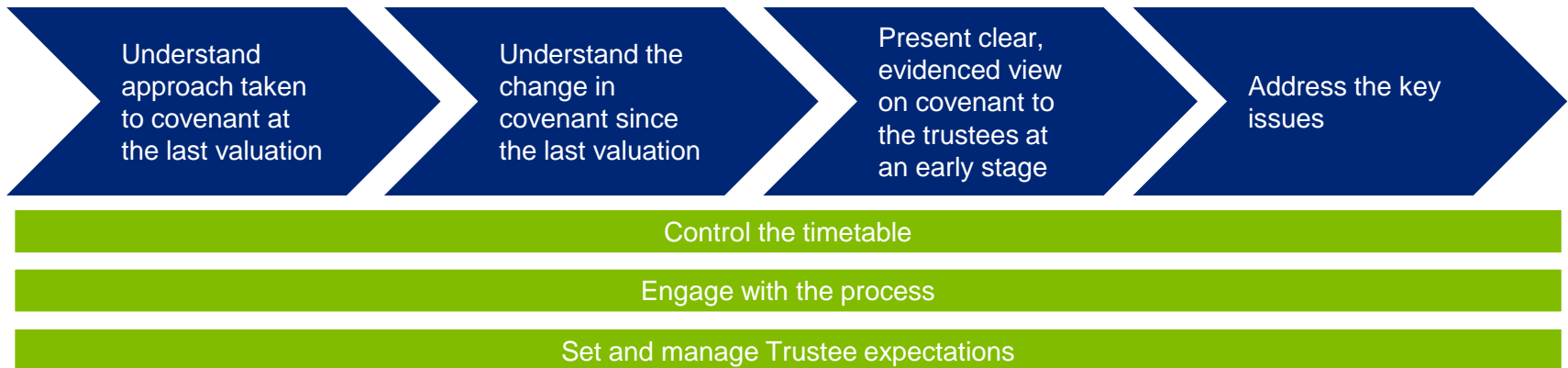
Controls testing

Funding negotiations

Employer considerations



Suggested employer strategy

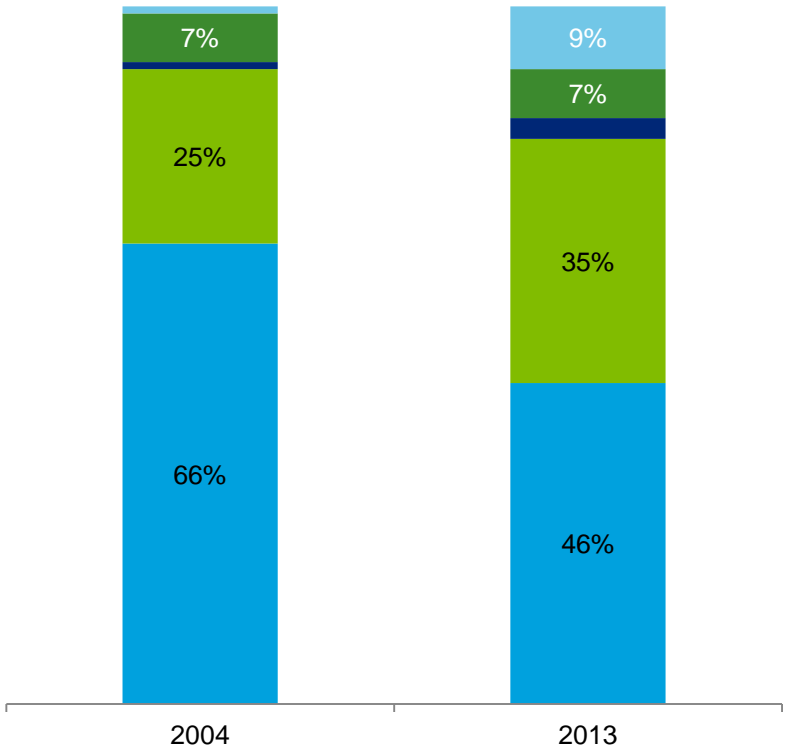


Change of average pension scheme asset allocation from 2004 to 2013

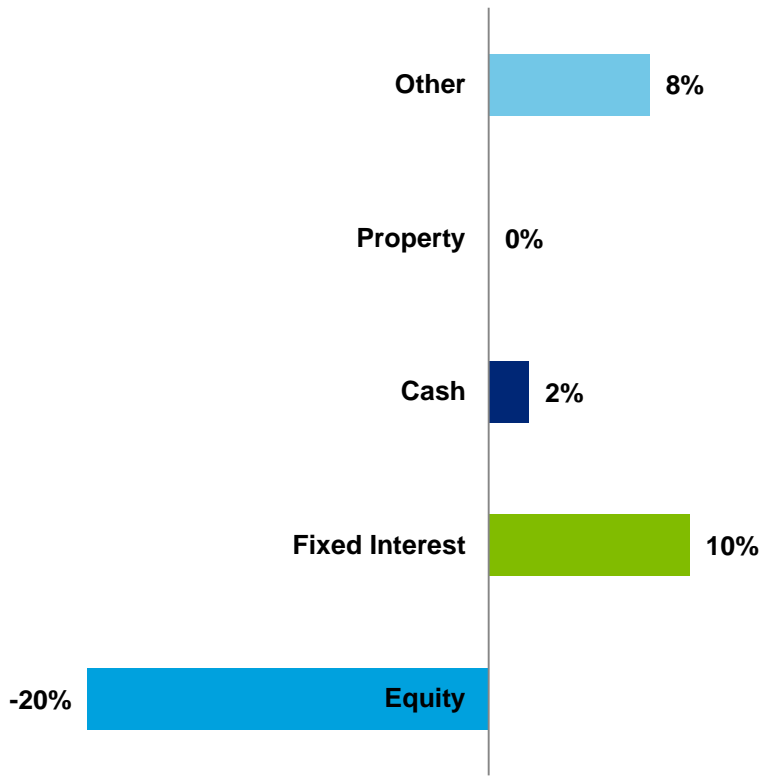
- Allocation to fixed income has increased significantly at the expense of equity
- Also increase in alternatives driven by demand for diversification

Average asset allocation

Equity Fixed Interest Cash Property Other



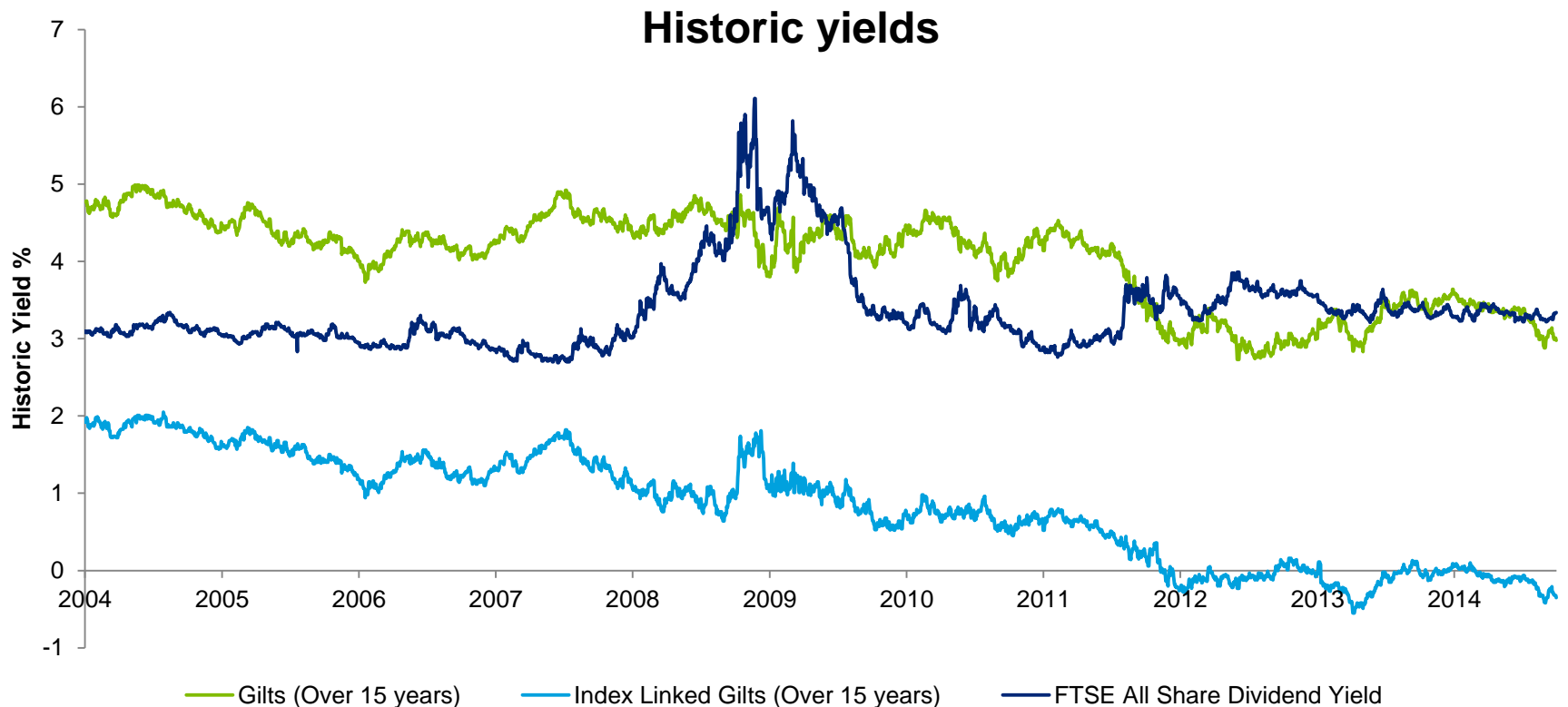
Change in allocation



Are equities relatively good value?

From 2004 to 2014

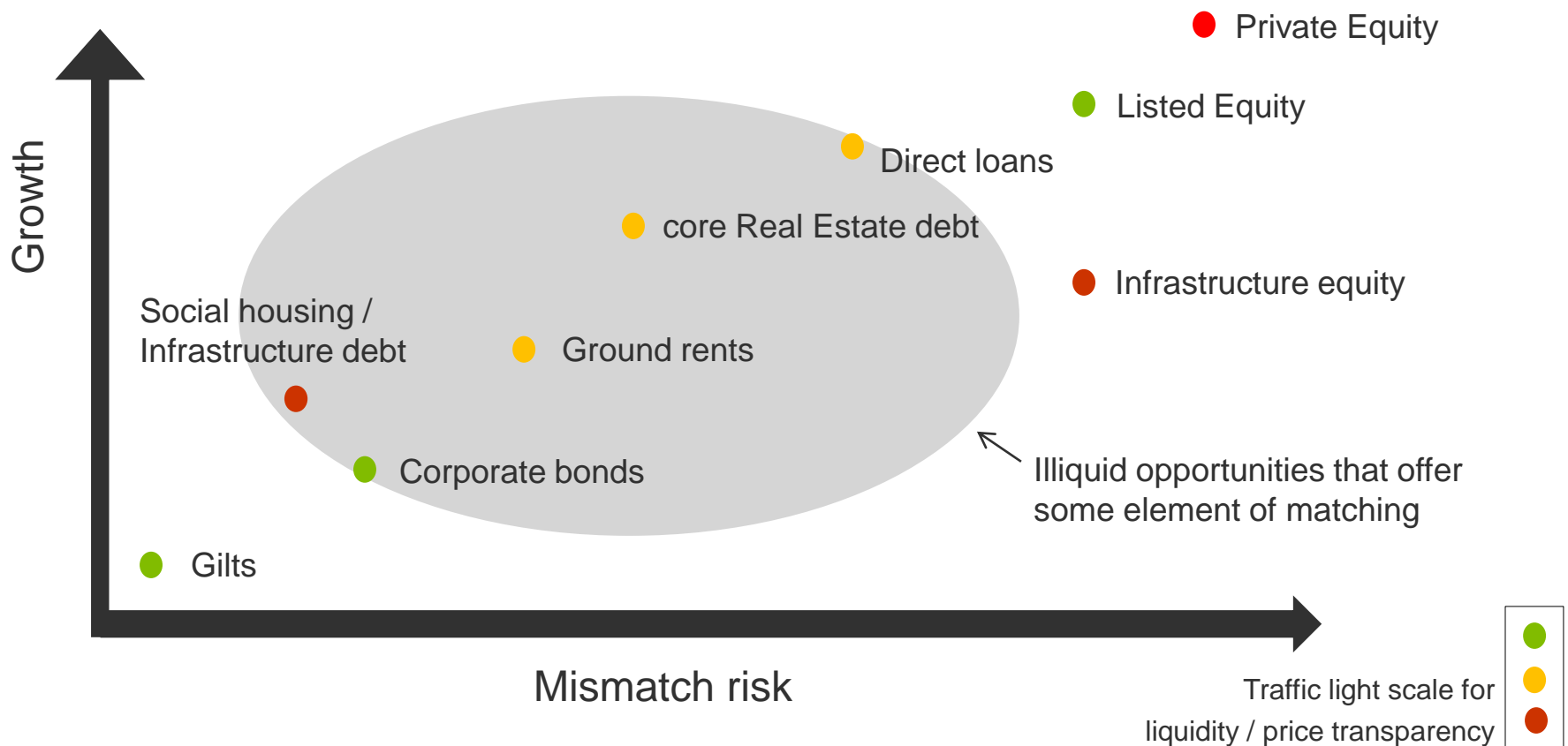
- Real yields have gone negative
- Dividend yields are significantly higher than Gilt yields
- Asymmetric risk for trustees?



Opportunities that exist for pension funds

Some choices

- These opportunities when compared to gilts can all be broadly categorised as: higher yield/return, higher mismatch risk, more illiquid, difficult to access, more complex, and requiring higher due diligence



Opportunities that exist for pension funds

Some choices

Social housing

- High yields (some inflation-linkage)
- Long maturity
- Very illiquid, difficult to price
- Low accessibility to managed products

Infrastructure

- Good yields (some inflation-linkage)
- Long maturity (entry/exit strategy)
- Choice of Green/Brown field projects
- Choice of Debt/Equity

Ground rents

- Good yields (some inflation-linkage)
- Limited supply

Direct company loans

- High yields
- Short maturity (refinancing)
- Specialist intermediary to source, transact, and manage deals

Real estate debt financing

- High yields
- Various tranches of debt security

Private Equity

- No yield, but high capital return potential
- Medium maturity around the business cycle (exit strategy risk)
- Specialist intermediary to source, transact, and manage deals

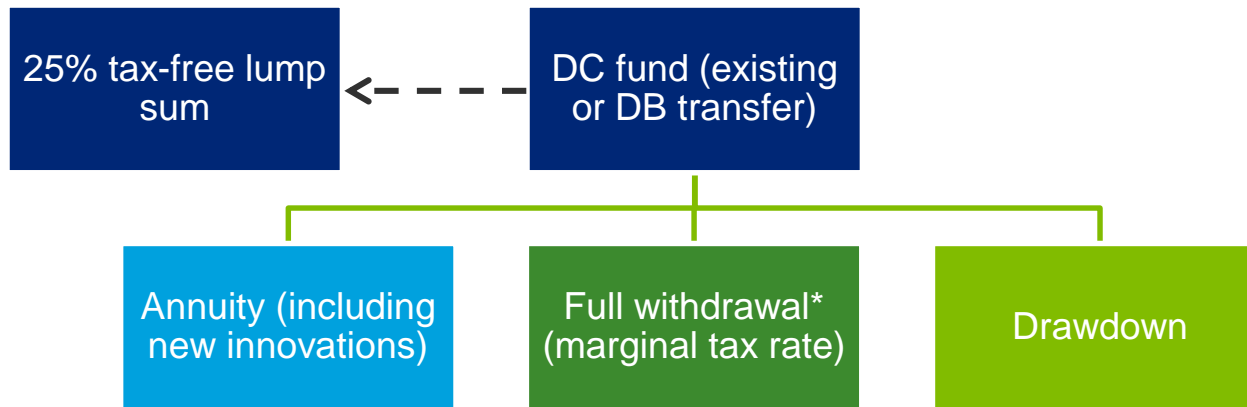
- Potentially these assets offer excess return with reduced volatility which is, in part, a result of illiquidity
- Significant premium available for long term investors able to provide liquidity

2014 Budget

DC pensions in the UK

April 2015 onwards

- Private sector DB-DC transfers permitted for pensions not yet in payment
- No requirement for annuity purchase
- Full access to DC pot (subject to marginal rate of income tax) from age 55 (57 from 2028)
- **“Guidance Guarantee”** – all members entitled to free, independent and impartial guidance at retirement, funded by a new levy on regulated financial services firms and collected by FCA (detail under consultation)
- Trivial commutation limit increased from £18,000 to £30,000 (immediate)
- Up to three “small pots” of under £10,000 can be taken tax-free from age 55



*The Government intends to consult on whether the requirement to transfer first to DC schemes, before full or partial withdrawal, should be removed

DC pensions in the UK

Legislation, innovation and tax changes

Legislation

- All members with DC or cash balance arrangement able to directly access pension flexibly from April 2015
- Government introducing statutory override to ensure all DC schemes are able to offer increased flexibility
- Schemes can “ignore the scheme rules” and “follow the tax rules instead” in order to pay out benefits flexibly or via drawdown
- Individuals will be able to transfer between DC schemes, up to the point of retirement, if their scheme does not offer flexible access

Innovation

- Increasing demand for more flexible retirement products to meet consumer needs
- The Government intends to change the current tax rules in order to:
 - allow lifetime annuities to decrease;
 - allow lump sums to be taken from lifetime annuities;
 - remove the ten-year maximum guarantee period for guaranteed annuities; and
- Variety of new drawdown products expected
- Temporary annuities also likely (for example in old age).
- Level/ timing of innovation will impact pensions strategy.

Tax

- The Government will introduce new tax rules to ensure that over-55s do not abuse the new flexibilities by diverting their salary into their pension with tax relief and then immediately withdrawing 25% tax-free
- The Government will announce changes to the tax charge applied to pension savings in a drawdown account at death (currently 55%) in the Autumn Statement
- Tax planning becomes vital in decision making for members.

DBflex

Flexibility at retirement

Offering members the option at retirement to transfer **some or all** of their DB pension into a DC fund, commute 25% of the benefits tax-free and then either:

- purchase an annuity product with an insurer;
- drawdown; or
- withdraw the remaining transfer value in full subject to the member's marginal rate of income tax.

Options for transfer values

Consideration will need to be given to the basis used in calculating transfer values. A prudent basis will result in higher transfer values and likely increase member take-up rates. Sponsors will need to ensure the transfer value basis reflects the company objectives – typically a trade-off between short-term costs and long-term risk reduction.

What annuity can members buy?

- Level
- Index-linked
- Escalating/decreasing
- Lump sum convertible (under £30,000)
- Fixed term
- With-profits
- Guaranteed

Drawdown

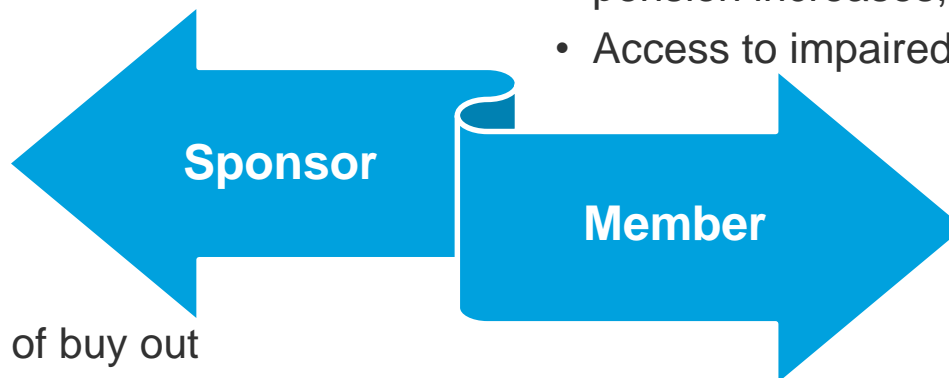
Enables members to proactively invest their retirement pot post-retirement and drawdown income as required (subject to marginal rate of income tax)

Key benefits

Risk management (cash, balance sheet) by reducing risk exposure of:

- Longevity
- Investment
- Inflation

- Remain in Company scheme
- Increased tax-free lump sum
- Increased retirement flexibility, including pension increases, spouse option etc
- Access to impaired life annuities



Cost saving

- Reduces the cost of buy out
- No impact on funding position if members offered funding reserve
- PPF levy reduction (depending on transfer basis)

- Drawdown options
- May assist retirement (and estate) planning, particularly for executives
- Transfer only occurs at point of retirement which removes risk of low pre-retirement investment performance of DC fund (drawback of an ETV exercise)

Reduction in volatility of balance sheet position

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Resources:

- Deloitte Finance Club home page: www.deloitte.co.uk/financeclub
- UK Accounting Plus (formerly IAS Plus): www.ukaccountingplus.co.uk
- Future of UK GAAP: www.deloitte.co.uk/futureofukgaap
- Annual Report Insights 2014: www.deloitte.co.uk/annualreportinsights
- Deloitte Actuarial & Pensions Services: www.deloitte.co.uk/actuarialpensions



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