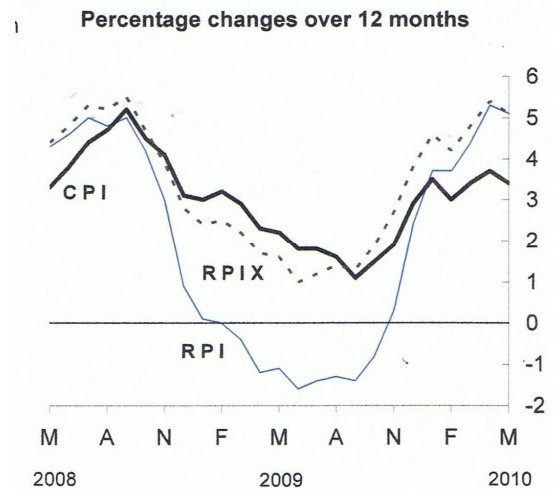


The Budget; Retail Price Index (RPI) & Consumer Price Index (CPI)

Thirteen years ago Chancellor Brown slipped in a £5bn p.a. tax charge on pension schemes. Chancellor Osborne has arguably not been quite so sneaky with the state pension indexation switch from RPI to CPI as most voters will be aware that RPI has historically exceeded CPI albeit the opposite applied in 2009 (see graph).

RPI is the most familiar UK measure of inflation. It dates back to 1947. In contrast the CPI is a more recent index used across Europe where it is known as the Harmonised Index of Consumer Prices (HICP). It was launched in 1997 as the Europe wide measure of inflation required for the Maastricht Treaty. It is the basis for the Bank of England’s Monetary Policy Committee’s inflation target.

Differences between RPI and CPI are a bit technical, for example the latter is based on a geometric mean rather than arithmetic mean! More importantly the CPI excludes mortgage interest payments and this is reflected in another common index RPIX (= RPI minus mortgage interest payments). In contrast RPI excludes university accommodation fees. For those studying statistics or looking for further details I recommend the ONS CPI Statistical [Bulletin](#).



Interest and capital repayments on Index Linked Government Stocks (ILGS) are also RPI linked. Interestingly recent issuance, see the Treasury Gilt 2047 [Prospectus](#), caters for an index other than RPI to be used. Whilst the stated reason for the change must reflect the fact that the RPI index ceases to be published, the principle appears to be that Chancellor of the Exchequer, after consultation with a body that the Chancellor considers to be independent, can change things.

The Budget; High Earners

From April 2011 the previous Labour Government had planned tax changes affecting high earners (>£130,000). The new coalition government is considering drastically reducing the annual allowance (£255,000 for 2010/11). In order to raise an estimated £3.5bn extra tax previously envisaged, the annual allowance will need to be reduced to between £30,000 and £45,000. For defined contribution arrangements this is pretty straight forward, however, as with many changes the difficulty will come with converting defined benefit promises into capital values. Ministers, MPs and top civil servants will all be affected, so we can only hope their conflicts of interest policies are in place!

Employer Covenant

The Pensions Regulator (TPR) has issued further [guidance](#) for trustees on the importance of assessing and monitoring employer covenant. The help includes case studies, checklists, necessary information and an appropriate assessor brief. The guidance is complemented by a new bite sized e-learning module and a short guide tailored for employers! Quite rightly TPR indicates that the employer covenant is a crucial element in protecting members’ benefits and highlights -

- the importance of measuring covenant;
- understanding a sponsor’s legal structure and legal obligations;
- what to consider when assessing the employer’s financial position;
- what to consider when valuing alternative forms of scheme security other than cash payments to the scheme;
- when to appoint external covenant assessors and the process to follow in doing so; and
- the importance of regular monitoring of covenant, and actions to take based on this.

Not having an independent employer covenant assessment is almost guaranteed to give rise to additional scrutiny.

And finally; The CPI link with the European index HICP reminds me that the Governor of the Bank of England is obliged to write a letter of explanation to the Chancellor of the Exchequer if this inflation target is exceeded. Needless to say when the target is missed it is a Harmonised Index of Consumer, Culture and Unit Prices, a (temporary) hiccup!

Feedback on Pension Snippets is also always welcome. For any comment, further assistance, advisory or trustee services, contact me on 07714 064964 or via allan@acmca.co.uk For further ACM/ACMCA detail, the full CV, occasional lecture notes and published articles and previous Snippets - visit the web site at www.acmca.co.uk