

STAKEHOLDER PENSIONS

Draft Regulations For

Establishment Of Schemes
Conversion and Restriction of Discretion To
Approve
Personal Pension Transfers
Information Powers



5th July 2000

1. The tax regime for stakeholder pensions was proposed in a joint DSS and Inland Revenue consultation document issued on 16th September 1999. The main legislation covering these changes forms part of the Finance Bill currently before Parliament and earlier regulations covering the relief at source scheme have already been issued in draft.

The regulations now issued for comment cover:

- establishment of trust based pension schemes;
- conversion of existing Money Purchase Occupational Schemes;
- transfers;
- information powers.

This note contains a short commentary on each set of regulations.

2. Copies of the regulations can be accessed on the Inland Revenue site at www.inlandrevenue.gov.uk or by e-mailing stakeholder@ir.gsi.gov.uk and including "subscribe regulations" in the subject. Printed copies can be obtained by telephoning 020 7438 7514.

3. Comments on the draft regulations and information requirements or the regulatory impact of the proposals are invited by Friday 28th July 2000 and should be sent to:

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Commentary on The Personal Pension Schemes (Establishment of Schemes) Order 2000

4. This regulation sets out details of a new category of person who may establish a Personal Pension Scheme that is capable of approval by the Board of Inland Revenue under S632 ICTA 1988.

5. The Finance Bill 2000 includes details of a simple integrated tax regime for defined contribution (DC) pensions, including stakeholder pensions. Inherent in the new regime is the fact that the establishment and approval of Personal Pensions should become more widely available.

6. Existing legislation lists the categories of person that may establish and receive approval for a Personal Pension. Until now the categories have been restricted to financial institutions. This regulation adds a new, non-financial category to the list.

New category of person

7. The regulation is very widely drawn. It allows a scheme to be established under trust by any person or body not already included in the existing list. An employer of a member of the scheme is specifically mentioned only to make clear that this link between the person establishing the scheme and the member is not precluded.

Link to Board's existing power to prescribe restrictions on approval

8. The regulation on establishment operates in conjunction with the Occupational Pension Schemes (Restriction on Discretion to Approve and Conversion of Retirement Benefits Schemes) Regulations 2000. These regulations (regulation 8) make clear that the Board will approve a personal Pension Scheme established under trust by a person fitting the description in paragraph 7 above only if certain conditions are met. These are either that:

- the scheme is an occupational pension scheme for DSS purposes and the trust deed contains provisions so that, where there are fewer than 12 members, the scheme is required to appoint an independent trustee. This trustee will be similar in all respects to the Pensioner trustee appointed under regulations relating to Small Self-administered schemes approved under Chapter 1 Part XIV ICTA; or
- the scheme must have applied for registration as a stakeholder scheme. In these circumstances tax approval will be conditional on the stakeholder approval being given. However, in practice it is likely that the tax approval

and stakeholder registration will be contained in a single document issued by Pensions Schemes Office.

Further Amendments to s632

9. Further regulations reflecting the new regulatory references contained within Financial Services and Markets Act 2000 appropriate to the existing categories of provider will be issued in due course.

Commentary on the Occupational Pension Schemes (Restriction on Discretion to Approve and Conversion of Retirement Benefits Schemes) Regulations 2000

10. These regulations set out the requirements to be met by occupational money purchase pension schemes, currently tax approved under Chapter I of Part XIV of the Taxes Acts 1988, that change their tax approval to Chapter IV of Part XIV. They also contain a general restriction to approve that applies to schemes established under trust (paragraph 8 of this document covers this restriction).

Requirements For Conversion

11. Before a scheme's application to change its tax status can be approved, the scheme must satisfy the Pensions Scheme Office (PSO) that:

- (a) it has been valued, under the relevant funding test contained in Part 13 of the Occupational Pension Schemes Practice Notes published by the Pension Schemes Office (PN) , within the last three years (regulation 3(2));
- (b) it has valued the benefits (regulation 6(2)) of any controlling directors and those earning over half the cap (regulation 5);
- (c) it has determined that the asset values under (a) do not exceed the maximum benefits prescribed by the Inland Revenue (regulation 6(4));
- (d) it will restrict (regulation 8), in the case of controlling directors (regulation 8(2), the use to which the fund may be put in the event that the member dies before taking benefits (regulation 9);
- (e) it will restrict (regulation 8), in the case of controlling directors, the amount of the fund which may be paid in the form of a tax free lump sum (regulation 9).

12. The scheme must also present PSO with the following documentation (regulation 4):

- (i) a copy of the rules to apply as a Chapter IV scheme;
- (ii) confirmation that the assets held are earmarked for each member;
- (iii) an outline of how the earmarking is achieved;
- (iv) if the OMPS was established as a common trust fund the explanation at (iii) should set out how the common trust fund was converted to earmarked funds;
- (v) details of the valuations set out in (a) to (c) above.

Valuation of Prescribed Sum

13. If a converting scheme has members who earn over half the earnings cap or who are controlling directors then the scheme must ensure that the transfer value for each of these members does not exceed a "prescribed sum". The "prescribed sum" will be calculated by a new, simplified valuation test that will also be used for calculating maximum transfer values. This forms a separate part of this consultation package and is discussed in paragraphs 26 and 27 below. This method of valuation will be published in PN before the final regulations are laid. These regulations will therefore refer to the valuation test as published on the day the regulations are made. If changes are made to the valuation test these will not be pertinent to these regulations unless an amending regulation is laid to apply the changes to the valuation method.

Excessive Valuations

14. A scheme that is in surplus under the appropriate test in PN Part 13 will not be approved to switch its tax approval until such time as a future PN Part 13 test shows that there is not a surplus.

15. Where a controlling director or someone earning over half the cap is found to have excessive benefits under the tests in regulation 6 that person may not be a member of the migrating scheme until such time as the value of his benefits falls below "the prescribed sum". Any action to reduce the value of the benefits must be within the scheme rules and with the approval of the member (regulation 7).

Restriction On Death Benefits

16. If a controlling director dies before taking benefits and leaves a spouse or dependant only 25% of the fund at the point of conversion, and any subsequent investment growth attributable to that fund, may be paid out as a tax free lump sum. The remainder of the fund must be used to buy a survivor's annuity or the survivor may elect to defer this and take income withdrawals instead (regulation 10).

Restriction on Lump Sums

17. The lump sum payable to a controlling director must be restricted to that which would have been payable under the occupational scheme updated by

changes in the retail price index between the date of conversion and the date that the lump sum is taken. (regulation 11).

COMMENTRY ON THE PERSONAL PENSION SCHEMES (TRANSFER PAYMENTS) REGULATIONS 2000

18. These regulations set out the requirements on Personal Pension Schemes (PPS) for the making, acceptance and application of transfer payments which originated wholly or partly in an Approved Retirement Benefit Scheme (ARBS) or an equivalent statutory scheme, referred to as a Relevant Statutory Scheme (RSS). They will replace in their entirety the existing regulations (SI 1988/1014) as amended.

19. The new regulations will accommodate pension sharing on divorce and allow funds in drawdown to be transferred to a different PPS.

20. They will also better focus the existing requirements by simplifying the arrangements for the vast majority of transfers from ARBS and RSS. In particular:

- there will be a simpler valuation test which will apply only to controlling directors and those earning over half the earnings cap;
- certificates of the amount of retirement lump sum available from the transfer payment (other than "nil" certificates) will no longer need to be supplied for people over age 45 unless they are controlling directors or earning more than half the earnings cap. This will remove the need for ARBS and RSS to compile certificates in most cases, and consequentially PPS will have to ring-fence transfer payments in only a small proportion of cases;
- the current rules for determining the lump sum which can be paid on death from transferred funds will no longer apply to all transferees. It will instead apply only to controlling directors and those earning over half the earnings cap. This should simplify the administration of PPS by reducing the need for special rules and also cutting back on the need for transfer payments in the PPS to be ring-fenced.

21. We estimate that these changes will mean that 96% of ARBS and RSS members will be able to make transfers to a PPS without any special rules being applied. We believe that this will significantly reduce the administrative burden for ARBS, RSS and PPS.

22. In addition to comments on the substance of the changes, we would welcome views on their impact with particular reference to the effect on scheme administration and costs.

23. The rest of this commentary provides details of the main requirements.

Requirements as to the making of transfer payments (Part II)

24. The administrator of a PPS who makes a transfer payment which originated in an ARBS or RSS must pass on with the payment any certificate held which shows the amount which may be taken as a lump sum (including nil) when benefits are paid.

25. Regulation 4 covers transfers from a PPS to another PPS, and Regulation 5 covers transfers from a PPS to an ARBS or RSS. Regulation 5 requires only a nil lump sum certificate to be passed on, because the normal lump sum rules would apply to the transfer payment once it is held by the ARBS or RSS.

Requirements as to the acceptance of transfer payments (Part III)

26. A PPS may not accept a transfer payment from an ARBS or RSS where the transfer payment relates to:

- a controlling director; or
- an individual whose earnings exceed half the earnings cap,

unless the administrator of the transferring scheme has been able to certify that the payment represents no more than the value of maximum benefits which could have been provided under that scheme (Regulation 7).

27. The calculation method will form an Appendix to the *Occupational Pension Scheme Practice Notes (IR12)*. A copy of the draft Appendix is attached.

Requirements as to the application of transfer payments (Part IV)

28. The current regulations limit death benefits to 25% of the fund and require the balance to be used to secure an annuity. The regulations update this to include the option of income withdrawal. It will also now apply only to controlling directors and those whose earnings exceed half the earnings cap. (Regulation 9)

29. Regulation 10 requires that retirement lump sum benefits for controlling directors and those earning over half the earnings cap are to be paid only as certified.

30. The lump sum benefit payable will be the amount certified under the rules of the transferring ARBS or RSS as enhanced by indexation from the transfer date to the date of payment. The absence of such a certificate will not prevent a transfer value being accepted, but in such a case, none of the transferred funds will be payable in lump sum form.

31. Regulation 11 provides that where a nil retirement lump sum certificate is held, no lump sum may be paid to an individual on their pension date from the transferred funds

32. Regulation 12 applies where a transfer payment has been accepted by a PPS and a pension sharing order is subsequently made. In such a case the administrator has to recalculate and re-certify the lump sum which may be taken in respect of the individual's pension as reduced by the pension sharing order.

33. The regulation also requires that where a nil lump sum certificate is held, a nil lump sum certificate has also to be prepared in respect of an ex-spouse's pension credit.

34. The regulation also requires a nil lump sum certificate to be prepared in respect of an ex-spouse's pension credit where the pension sharing order takes place after the member's pension date.

Exceptions to the prohibition on transfers after pension date (Part V)

35. Regulation 13 allows people to choose a different investment manager by transferring their funds under income withdrawal to a different PPS.

36. The regulation permits such a transfer only if the receiving scheme limits the benefits and range of options available under the new arrangement to those which would have applied had the member (or survivor) continued with income drawdown under the original arrangement.

Commentary on the Personal Pension Schemes (Information Powers) Regulations 2000

37. These regulations set out revised information requirements to apply to all schemes approved under Chapter IV Part XIV ICTA. They mirror, to a very large extent, existing information requirements that apply to schemes approved under Chapter I. The regulations are not intended to impose a burden on personal pension schemes, the information that they are required to hold and provide is similar to that which it would be reasonable to expect a well managed and run scheme to hold in the normal conduct of its business.

38. Part I of the regulation contains definitions, including, in regulation 3, a comprehensive definition of a self invested personal pension.

39. The regulations define self invested personal pensions (SIPPs) as arrangements, where the assets held are not entirely as:

- life insurance contracts or units in a unit trust scheme over which the member has no special control (i.e. if the scheme offers the same choice of investments to all members; or
- all contributions are invested in deposits with a deposit taker and the only income of the scheme is the interest on those deposits. (Regulation 3)

The remaining parts of the regulations deal with:

- information to be provided without notice;
- information to be provided after notice;
- inspection and retention of documents.

Information to be provided without notice

Self Invested Transactions

40. SIPPs must inform the Board within 90 days of the following transactions taking place:

- acquisition or disposal of land (regulation 4(4)(a));
- borrowing of money (regulation 4(4)(b));
- the purchase, sale or lease of any asset other than land (regulation 4(4)(c)).

Chargeable Events

41. All personal pension schemes must inform the Board, within 30 days of the end of the year of assessment in which a member has received a return of contributions after an arrangement's pension date. (Regulation 5).

42. The forms to be provided for reporting SIPP transactions and the return of contributions after pension date will require schemes to return only certain classes of transactions. So although, at first sight, the regulations appear to require schemes to report all transactions this will be limited to those transactions that meet specified criteria. PSO will be discussing with the various representative bodies the exact categories to be used.

Information to be provided after notice

Approved Personal Pensions (including SIPPs)

43. All approved personal pension schemes must provide, if requested to do so by the Board any information and supporting documentation regarding:

- contributions (regulation 6(1)(a));
- investments (regulation 6(1)(b));
- payments from the fund (regulation 6(1)(c)).

Annuity Contracts

44. Insurance companies and friendly societies providing annuity contracts shall provide the Board with any document relating to annuity contracts written by the company or society. (Regulation 7).

Inspection and Retention of Documents

45. Schemes must keep specified books and records for six years and should make this available for inspection if given notice by the Board (regulation 9).