

A

APPENDIX TO REGULATORY IMPACT ASSESSMENT FOR PENSION SIMPLIFICATION

Introduction

A.1 This is an appendix to the Regulatory Impact Assessment “*Simplifying the taxation of pensions*” published on 8 April 2004. It updates the pensions simplification measures as set out in that Assessment to take account of additional legislative changes announced at PBR 2004 and Budget 2005.

Background

A.2 The taxation of pensions will be radically simplified from 6 April 2006. There will be a single, universal regime for tax privileged pensions to replace the existing complex regimes. This will improve choice and flexibility for pension providers, employers and individual pension savers, provide greater encouragement for individuals to save for retirement and reduce administration and compliance costs for the pensions industry. The relevant legislation is contained in Finance Act 2004 and regulations to be made under that Act.

A.3 A further package of pensions simplification measures, building on those in Finance Act 2004, is now being introduced. Many have been developed as a result of ongoing liaison with the pensions industry following Finance Act 2004.

Summary of Measures

A.4 The full package of additional measures is set out in the Inland Revenue Technical note published on 16 February 2005.¹

A.5 The package includes measures requested by the pensions industry since Finance Act 2004, to allow additional flexibility in scheme design. There are some new transitional rules, which protect existing rights, and smooth the transition to the new regime for individuals, employers and schemes. Some examples are set out below. There are also some minor rules that clarify the Finance Act 2004 legislation, and some anti-abuse measures, to counter potential exploitation of the new regime’s very generous tax privileges.

Measures to Increase Flexibility

A.6 These include:

- a rule to allow the maximum tax free lump sum that may be taken to be calculated at a scheme level, rather than, as now, at an arrangement level. This will allow individuals more flexibility to amalgamate AVCs and other pension benefits within the same scheme, so as to maximise their tax free lump sum within the authorised limits;
- a rule to deal with annuities that provide for an income to be paid to the member’s dependant following the death of the member. The cost of the dependant’s annuity will be included from both the amount tested against

¹ Technical note: *Pensions Simplification*, February 2005, available at: <http://www.inlandrevenue.gov.uk/pensionschemes/pensions-simplification-tn.pdf>

the lifetime allowance and the calculation of the maximum tax free lump sum;

- The requirement for schemes with fewer than 50 members to provide scheme pensions through an insurance company will be removed. This should give schemes and employers more flexibility in the provision of pensions. The definition of lifetime annuity will be extended to allow more flexible annuity products; and
- The definition of dependant will be extended so that schemes may provide a dependant's pension to an individual married to the member when the member began to receive a pension, but divorced from the member before the member's death.

Measures to Smooth Transition to the New Regime

A.7 These include:

- transitional measures to allow schemes to continue to make payments that otherwise could be caught under unauthorised payment rules – such as allowing pensions in payment to children over 23 in full time education to continue and allowing funeral expenses to be met where the right already existed and the member has retired before 6 April 2006;
- measures to deal with legacy schemes to minimise administration costs such as ensuring burdensome data input obligations are not imposed on annuity providers and bringing all pensions annuities into PAYE from 6 April 2007;
- a measure to allow relief to continue to be claimed on contributions to overseas schemes where the claimant was entitled to relief at 6 April 2006; and
- a rule to protect an individual's accrued rights at 6 April 2006 to draw a pension commencement lump sum even if there is no right to a pension under the particular scheme.

Implementation

A.8 We are continuing to work closely with those impacted to ensure they understand their obligations in advance of 6 April 2006 and that changes are implemented in a way that reduces the administrative burden to the pensions industry. For example workshops have been run to discuss online filing arising for schemes and are liaising with industry on how we can work with providers to bring all pensions annuities into PAYE. We have set up a readers' panel to help us produce guidance for the new regime.

Impact of Additional Measures

A.9 Having carefully considered the impact of the additional measures our assessment is that they do not alter the assessment of impacts and costs set out in the original Regulatory Impact Assessment. In particular the measures to assist scheme flexibility and to smooth the transition to the new regime will enable the full benefits as set out in the original assessment to be realised. The minor technical amendments introduced merely ensure that the legislation works as intended and will not affect the

costs or impacts as originally assessed. The anti-abuse measures being introduced will help prevent the new rules being used for unintended purposes.

A.10 Overall these represent constructive additions to the simplification package and will help deliver a system that is flexible, easy to operate and tailored to the needs of its users.

Contact Point

Barbara Conroy
Pensions Policy
Room G63
1 Parliament Street
London
SW1A 2BQ

Tel: 020 7147 2872

E-mail: pensionsconsult@ir.gsi.gov.uk

Please put the phrase “Regulatory Impact Assessment” in the subject line of your e-mail or letter.