

PREMIER PENSIONS MANAGEMENT

LEGISLATION UPDATE: 09/07

Pensions Act 2004 - Administration Anomalies

The following are two areas where the Pensions Act 2004 seems to have had an inadvertent impact on the administration of Pension Schemes.

1 Refunds of Contributions

Under new rules that have applied since 6 April 2006, members who leave the Scheme with at least 3 months service but less than 2 years qualifying service, now have a statutory entitlement to a transfer value. This will include the value of both employee and employer contributions and is offered as an alternative to a refund of the members' contributions.

The legislation states that the transfer value should be calculated at the date on which the member's pensionable service terminates. The transfer value is therefore subject to a guarantee minimum of the value of a member's fund at the date of leaving pensionable service. There is no plan to amend this for Money Purchase/Defined Contribution (DC) schemes.

Virtually all Trustees currently treat the transfer value as the full value of the member's fund at the date the transfer is completed. In practice, the transfer value is likely to be paid some months after the date that a member left the scheme.

There is therefore, a risk that the transfer value paid may be less than the full value at the date of leaving pensionable service.

Trustees may wish to introduce a guarantee for the amount of cash transfer sum in line with the legislation. It is the Trustees responsibility to make good any shortfall between the guaranteed cash transfer at the date the member left pensionable service and the Fund value at the date of the transfer payment. One idea may be to switch the assets to a cash fund as soon as the member leaves.

Legal advice should be sought by all Trustees on this matter.

2 Payment of Tax Free Cash Sums

Again, following the A-Day regulations, the Pensions Industry has been in consultation with HMRC regarding the correct approach to paying the tax free cash sum where a pension is secured through a lifetime annuity. A life time annuity is an annuity purchased from an insurer that the member had the opportunity to select (applies therefore to DC arrangements only).

The conclusion of the discussions is that a tax free cash sum cannot be paid until immediately before the annuity is purchased i.e. when funds are passed to the annuity provider. Earlier payment would constitute an unauthorised member payment. This can be against the Rules and can have significant tax implications.

The effect of this is that if an annuity is being purchased, payment of the tax free cash sum must be delayed until the annuity is selected and payment to the provider made.

Under pre A-Day rules it was common practice to pay the tax free cash sum as soon as practicable following retirement. This allows the pensioner capital to live off, until the choice of provider and establishment of the annuity is complete. In many cases this could be several months after retirement.

All scheme Trustees should discuss this with their administrators and agree procedures and then advise their members of the likely delay in the payment of the tax free cash sum in the future.

August 2007

This update includes general information and cannot be relied upon for individual schemes issues. You should contact your adviser or Paul Couchman at Premier Pensions Management Ltd, Capital Business Centre, Units 14 & 15, 22 Carlton Road, South Croydon, Surrey, CR2 0BS. DL: 020 8916 2129. Email: paul.couchman@premierpensions.co.uk, if you require definitive advice